

## Chapter 2 Balance Sheet

### The Balance Sheet

The formal way of presenting financial position is by means of a balance sheet. A **balance sheet** is a statement showing the financial position of a person, business, or other organization. Figure 2.1 contains the balance sheet that shows the financial position of Chris Turner whom you met on page 18.

Chris Turner										
Balance Sheet										
September 15, 20--										
<u>Assets</u>					<u>Liabilities</u>					
Cash	\$		5	5	00	Owed to brother Philip	\$	2	2	00
Bank Balance			2	4	50	Owed to Dad		3	0	00
Canada Savings Bonds		3	0	0	00	Mobile Phone Bill		4	0	00
Mountain Bike			6	2	00	Total Liabilities	\$	9	2	00
Snowboard			7	5	00					
Computer and Electronics		1	9	0	00	<u>Owner's Equity</u>				
Mobile Phone			5	0	00	Chris Turner, Capital		8	8	50
Clothes			2	7	00					
Total Assets	\$	9	7	7	00	Total Liabilities and Equity	\$	9	7	70

**Figure 2.1**

A personal balance sheet

What do you notice about the Owner's Equity Section?

Only shows Chris Turner, Capital

## Equity Relationships and the Balance Sheet

◀ 5.3

### Understanding Equity Relationships

You are now familiar with the expanded ledger, and you have learned how to show the balances of new accounts on an income statement. You also now know that the income statement is the second major financial statement in accounting. The first major statement you learned was the balance sheet. To show equity on the balance sheet—and to ensure your balance sheet balances—it is important to fully understand equity accounts and how they relate to each other mathematically.

Consider again the trial balance for Eve Boa, LLB.

EVE BOA, LLB TRIAL BALANCE JANUARY 31, 20—		
	Dr	Cr
Bank	2 439	
A/R – H. Geroux	1 420	
A/R – J. Magill	757	
<b>BANK LOAN</b>		<b>940</b>
E. Boa, Capital		21 878
E. Boa, Drawings	3 950	
Fees Earned		23 660
Advertising Expense	1 321	
Car Expense	615	
Rent Expense	3 300	
Sundry Expense	385	
Wages Expense	9 830	
	<u>52 078</u>	<u>52 078</u>

  

<b>NET INCOME</b>	8 209	}	<b>26 137</b>	<b>BALANCE OF CAPITAL</b>
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**Figure 5.7**

Eve Boa's trial balance with components of the equity section highlighted

The trial balance is in balance with totals of \$52 078. These totals include the new equity accounts. To make the balance sheet totals agree, each amount in the trial balance could be transferred to the balance sheet, but this would be impractical, especially in the case of large companies with many revenue and expense accounts. Instead, equity calculations can be developed and recorded on the balance sheet.

You will now examine Figure 5.7 carefully. The debit and credit amounts listed in the equity section will help you understand the mathematical calculations needed for the balance sheet.

E. Boa, Capital (\$21 878) is the starting capital and is a credit balance. The other blue numbers represent changes to equity during the month. The numbers with the blue shading make up the income statement. If revenues are greater than expenses (net income), the balance of the shaded numbers (\$8209) is a credit. Since credits are added to credits, we can start to build an equity equation by writing the following:

$$\text{Beginning Capital} + \text{Net Income}$$

The net income figure summarizes all the revenue and expense amounts. The only remaining amount unaccounted for in the equity section of Figure 5.7 is E. Boa, Drawings. It is a debit and therefore is subtracted from credits. To finish the equation, subtract drawings, and write the result:



$$\text{Beginning Capital} + \text{Net Income} - \text{Drawings} = \text{Ending Capital}$$

We will call this formula the equity equation. The **equity equation** is a mathematical description of the relationship between the different components of the equity section in the expanded ledger. For Eve Boa, the amounts in her equity equation are

$$21\,878 + 8\,209 - 3\,950 = 26\,137$$

If there is a net loss, you need to adjust the equity equation because expenses are greater than revenues. If this were the case for Eve Boa, the balance of the shaded area in Figure 5.7 would be a debit. The net loss (a debit) would be subtracted from the beginning capital (a credit). The adjustment to the equity equation is



$$\text{Beginning Capital} - \text{Net Loss} - \text{Drawings} = \text{Ending Capital}$$

### Showing Equity on the Balance Sheet

To prepare a balance sheet, you need to take the equity equation and present it in good form. For example, the balance sheet for Eve Boa would look similar to Figure 5.8 (on the next page).

EVE BOA, LLB BALANCE SHEET JANUARY 31, 20--		
<b>ASSETS</b>		
<i>Current Assets</i>		
Bank	\$ 2 439	
A/R – H. Geroux	1 420	
A/R – J. Magill	757	
A/R – E. Parsons	1 395	
Supplies	<u>2 316</u>	
<i>Total Current Assets</i>		\$ 8 327
<i>Long-Term Assets</i>		
Office Equipment	\$ 7 550	
Automobile	<u>16 800</u>	
<i>Total Long-Term Assets</i>		<u>24 350</u>
<b>Total Assets</b>		<u><u>\$ 32 677</u></u>
<b>LIABILITIES</b>		
<i>Current Liabilities</i>		
A/P – OK Supply	\$ 4 400	
A/P – Computer Outlet	1 200	
Bank Loan	<u>940</u>	
<i>Total Current Liabilities</i>		\$ 6 540
<b>OWNER'S EQUITY</b>		
<i>Eve Boa, Capital</i>		
Balance January 1	\$ 21 878	
Net Income	\$ 8 209	
Less: Drawings	<u>(3 950)</u>	
Increase in Capital	<u>4 259</u>	
<i>Balance January 31</i>		26 137
<b>Total Liabilities and Owner's Equity</b>		<u><u>\$ 32 677</u></u>

For this balance sheet, the ASSETS section is placed above the LIABILITIES and EQUITY sections instead of beside them. This format is referred to as the report form of the balance sheet.

This balance sheet also classifies assets and liabilities as either current or long-term. (See Chapter 2.)

Recall that under IFRS, the balance sheet is called the Statement of Financial Position.

**Figure 5.8**

Eve Boa's balance sheet with an expanded equity section

What do you notice about the Owner's Equity section now?

- It is expanded
- ↳ Contains Capital, Net income, and Drawings

\* 
$$\text{Net Income} = \text{Revenues} - \text{Expenses}$$

$$\text{Net Loss}$$

### Other Possible Changes to Equity

In Eve Boa's case, net income was greater than drawings. This caused an increase in equity. Consider other cases that can describe what happens to equity over a fiscal period.

Owner's Equity

The net loss and drawings are added first because both have the effect of reducing capital.

<b>Drawings greater than Net Income</b>			
<i>T. Smith, Capital</i>			
Balance January 1		\$ 20 376.64	
+ Net Income	\$ 10 594.03		
- Less: Drawings	(15 376.70)		
- Decrease in Capital		(4 782.67)	
Balance December 31			15 593.97
<b>Net Loss</b>			
<i>S. Brown, Capital</i>			
Balance July 1		\$ 31 216.40	
- Net Loss	(\$ 5 147.62)		
- Plus: Drawings	(19 400.00)		
- Decrease in Capital		(24 547.62)	
Balance June 30			6 668.78
<b>Additional Investments</b>			
<i>S. D'Angio, Capital</i>			
Balance January 1		\$ 47 005.12	
+ Plus: Additional Investments		30 000.00	
+ Net Income	\$ 23 604.89		
- Less: Drawings	(20 000.00)		
+ Increase in Capital		3 604.89	
Balance December 31			80 610.01

**Figure 5.9**

Three other equity sections showing how equity changes in a fiscal period

## Homework

Chapter 5 Review on page 164

<b>CHAPTER 5</b>	<b>REVIEW EXERCISES</b> (page 164)
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**Using Your Knowledge****Exercise 1, p. 164**

<b>A.</b> Asset debit		<b>Dr</b>	<b>Cr</b>
<b>B.</b> Asset credit	<b>1.</b> Purchase a new car on account.	1. <i>A</i>	<i>D</i>
<b>C.</b> Liability debit	<b>2.</b> Receive payment on account from a customer.	2. <i>A</i>	<i>B</i>
<b>D.</b> Liability credit	<b>3.</b> Owner withdraws cash for personal use.	3. <i>G</i>	<i>B</i>
<b>E.</b> Capital debit	<b>4.</b> Owner starts a new business by investing cash.	4. <i>A</i>	<i>F</i>
<b>F.</b> Capital credit	<b>5.</b> The car is repaired and paid for in cash immediately.	5. <i>K</i>	<i>B</i>
<b>G.</b> Drawings debit	<b>6.</b> Perform a service for a customer for cash.	6. <i>A</i>	<i>J</i>
<b>H.</b> Drawings credit	<b>7.</b> Perform a service for a customer on account.	7. <i>A</i>	<i>J</i>
<b>I.</b> Revenue debit	<b>8.</b> Purchase supplies for cash.	8. <i>A</i>	<i>B</i>
<b>J.</b> Revenue credit	<b>9.</b> Receive a bill for gas and oil for the car.	9. <i>K</i>	<i>D</i>
<b>K.</b> Expense debit	<b>10.</b> Pay a creditor on account.	10. <i>C</i>	<i>B</i>
<b>L.</b> Expense credit	<b>11.</b> Throw out some ruined supplies.	11. <i>K</i>	<i>B</i>

Exercise 2, p. 165

BIANCO COMPANY  
INCOME STATEMENT  
YEAR ENDED DECEMBER 31, 20-

<u>Revenue</u>													
<i>Fees Earned</i>									\$47	4	1	6	-
<u>Operating Expenses</u>													
<i>Car Expense</i>	\$	2	4	8	2	-							
<i>Rent Expense</i>		3	5	0	0	-							
<i>Utilities Expense</i>		1	0	7	5	-							
<i>Wages Expense</i>		18	0	7	2	-							
<i>Total Expenses</i>									25	1	2	9	-
<i>Net Income</i>									\$22	2	8	7	-



Exercise 3, p. 165

A.

	Debits		Credits	
	Account(s)	Amount	Account(s)	Amount
1.	<i>P. Garside, Capital</i>	150	<i>Revenue</i>	150
2.	<i>P. Garside, Drawings</i>	500	<i>Wages Expense</i>	500
3.	<i>Car Expense</i>	400	<i>Automobiles</i>	400
4.	<i>Equipment</i>	110	<i>Car Expense</i>	110

<b>Bank</b> <hr/> 1 745	<b>A/R— P. Alder</b> <hr/> 50	<b>A/R— A. Jackson</b> <hr/> 70	<b>Supplies</b> <hr/> 610
<b>Equipment</b> <hr/> 5 000 ④ 110	<b>Automobiles</b> <hr/> 7 900    400 ③	<b>A/P— B &amp; B Stone</b> <hr/> 110	<b>A/P— Century Finance</b> <hr/> 5 500
<b>P. Garside, Capital</b> <hr/> ① 150    5625	<b>P. Garside, Drawings</b> <hr/> 200 ② 500	<b>Revenue</b> <hr/> 11 920 150 ①	<b>Car Expense</b> <hr/> 500    110 ④ ③ 400
<b>Utilities Expense</b> <hr/> 280	<b>Rent Expense</b> <hr/> 300	<b>Wages Expense</b> <hr/> 6 500    500 ②	

B. The corrected net income will be           \$4700          .

**Exercise 4, p. 166**

A. ATLAS ASSOCIATES  
INCOME STATEMENT  
MONTH ENDED NOVEMBER 30, 20-

<u>Revenue</u>										
<i>Fees Earned</i>						\$31	7	0	0	-
<u>Expenses</u>										
<i>Salaries Expense</i>	\$13	4	0	0	-					
<i>Rent Expense</i>	6	0	0	0	-					
<i>General Expense</i>	1	2	0	0	-					
<i>Advertising Expense</i>		6	0	0	-					
<i>Car Expenses</i>	3	7	0	0	-					
<i>Utilities Expense</i>	3	5	0	0	-					
<i>Total Expenses</i>						28	4	0	0	-
<i>Net Income</i>						\$	3	3	0	0

- B. The clerk violated the matching principle (GAAP and ASPE) or the framework of reliability under IFRS. The wage advance should be accounted for in the month it is earned so it can be matched with the revenue it helped generate.
- 
- C.  $\$31\,700 - (\$28\,400 - \$1\,400) = \$4\,700$   
The November net income should be \$4700.
- 
- D. The net income in December would be higher if the matching principle was not followed.

**Exercise 5, p. 166**

	<b>Assets</b>	<b>=</b>	<b>Liabilities</b>	<b>+</b>	<b>Beginning Capital</b>	<b>+</b>	<b>Revenues</b>	<b>-</b>	<b>Expenses</b>	<b>-</b>	<b>Drawings</b>
End of Year 1	100	=	20	+	70	+	60	-	45	-	5
End of Year 2	120	=	30	+	<i>80</i>	+	90	-	60	-	<i>20</i>
End of Year 3	130	=	<i>35</i>	+	<i>90</i>	+	105	-	80	-	20
End of Year 4	<i>130</i>	=	30	+	<i>95</i>	+	110	-	95	-	10

**Exercise 6, p. 167**

	<b>Assets</b>	<b>Liabilities</b>	<b>Equity</b>
End of 20-1	<i>\$44 700</i>	\$ 27 400	<i>\$17 300</i>
End of 20-2	<i>\$39 700</i>	<i>\$20 400</i>	\$ 19 300

Exercise 7, p. 167

A., B.

<p><b>Bank</b></p> <table border="1"> <tr><td>5 000</td><td>300 (1)</td></tr> <tr><td>(5) 175</td><td>50 (2)</td></tr> <tr><td>(7) 300</td><td>100 (6)</td></tr> <tr><td>(17) 5 000</td><td>500 (8)</td></tr> <tr><td></td><td>120 (9)</td></tr> <tr><td></td><td>750 (11)</td></tr> <tr><td></td><td>120 (12)</td></tr> <tr><td></td><td>50 (13)</td></tr> <tr><td></td><td>70 (15)</td></tr> <tr><td></td><td>1 500 (16)</td></tr> <tr><td><u>10 475</u></td><td><u>3 560</u></td></tr> <tr><td><u>(6 915)</u></td><td></td></tr> </table>	5 000	300 (1)	(5) 175	50 (2)	(7) 300	100 (6)	(17) 5 000	500 (8)		120 (9)		750 (11)		120 (12)		50 (13)		70 (15)		1 500 (16)	<u>10 475</u>	<u>3 560</u>	<u>(6 915)</u>		<p><b>A/R—Jenkins and Co.</b></p> <table border="1"> <tr><td>(4) 900</td><td>300 (7)</td></tr> <tr><td>(14) 600</td><td></td></tr> <tr><td></td><td><u>1 500</u></td></tr> <tr><td><u>(1 200)</u></td><td></td></tr> </table>	(4) 900	300 (7)	(14) 600			<u>1 500</u>	<u>(1 200)</u>		<p><b>Office Supplies</b></p> <table border="1"> <tr><td>(1) 300</td><td></td></tr> <tr><td>(12) 120</td><td></td></tr> <tr><td></td><td><u>(420)</u></td></tr> </table>	(1) 300		(12) 120			<u>(420)</u>
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<p><b>Fees Earned</b></p> <table border="1"> <tr><td></td><td>900 (4)</td></tr> <tr><td></td><td>175 (5)</td></tr> <tr><td></td><td>200 (10)</td></tr> <tr><td></td><td>600 (14)</td></tr> <tr><td></td><td><u>(1 875)</u></td></tr> </table>		900 (4)		175 (5)		200 (10)		600 (14)		<u>(1 875)</u>	<p><b>Advertising Expense</b></p> <table border="1"> <tr><td>(2) 50</td><td></td></tr> <tr><td>(13) 50</td><td></td></tr> <tr><td></td><td><u>(100)</u></td></tr> </table>	(2) 50		(13) 50			<u>(100)</u>	<p><b>Car Expense</b></p> <table border="1"> <tr><td>(9) 120</td><td></td></tr> </table>	(9) 120																					
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<p><b>Donations Expense</b></p> <table border="1"> <tr><td>(6) 100</td><td></td></tr> </table>	(6) 100		<p><b>Miscellaneous Expense</b></p> <table border="1"> <tr><td>(15) 70</td><td></td></tr> </table>	(15) 70		<p><b>Rent Expense</b></p> <table border="1"> <tr><td>(11) 750</td><td></td></tr> </table>	(11) 750																																	
(6) 100																																								
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(11) 750																																								

**Exercise 7, p. 167** (continued)

C.

*N.A. JAMES**TRIAL BALANCE**OCTOBER 31, 20-*

ACCOUNTS	DEBIT					CREDIT				
<i>Bank</i>	6	9	1	5	-					
<i>A/R—Jenkins and Co.</i>	1	2	0	0	-					
<i>Office Supplies</i>		4	2	0	-					
<i>Office Equipment</i>	1	1	0	0	-					
<i>Automobile</i>	18	0	0	0	-					
<i>A/P—Office Equippers</i>							6	0	0	-
<i>Bank Loan</i>							5	0	0	0
<i>N.A. James, Capital</i>							23	0	0	0
<i>N.A. James, Drawings</i>	1	7	0	0	-					
<i>Fees Earned</i>							1	8	7	5
<i>Advertising Expense</i>		1	0	0	-					
<i>Car Expense</i>		1	2	0	-					
<i>Donations Expense</i>		1	0	0	-					
<i>Miscellaneous Expense</i>			7	0	-					
<i>Rent Expense</i>		7	5	0	-					
	30	4	7	5	-	30	4	7	5	-

D. N.A. JAMES  
INCOME STATEMENT  
MONTH ENDED OCTOBER 31, 20-

<u>Revenue</u>															
<i>Fees Earned</i>									\$1	8	7	5	-		
<u>Expenses</u>															
<i>Advertising Expense</i>						\$	1	0	0	-					
<i>Car Expense</i>							1	2	0	-					
<i>Donations Expense</i>							1	0	0	-					
<i>Miscellaneous Expense</i>								7	0	-					
<i>Rent Expense</i>							7	5	0	-					
<i>Total Expenses</i>											1	1	4	0	-
<i>Net Income</i>											\$	7	3	5	-

**Exercise 7, p. 167** (continued)

E.

N.A. JAMES  
BALANCE SHEET  
OCTOBER 31, 20-

<u>ASSETS</u>														
<i>Current Assets</i>														
<i>Bank</i>														
<i>A/R—Jenkins and Co.</i>														
<i>Office Supplies</i>														
<i>Total Current Assets</i>														
<i>Long-Term Assets</i>														
<i>Office Equipment</i>														
<i>Automobile</i>														
<i>Total Long-Term Assets</i>														
<i>Total Assets</i>														
<u>LIABILITIES</u>														
<i>Current Liabilities</i>														
<i>A/P—Office Equippers</i>														
<i>Bank Loan</i>														
<i>Total Current Liabilities</i>														
<u>OWNER'S EQUITY</u>														
<i>N.A. James, Capital</i>														
<i>Balance October 1</i>														
<i>Net Income</i>														
<i>Less: Drawings</i>														
<i>Decrease in Capital</i>														
<i>Balance October 31</i>														
<i>Total Liabilities and Owner's Equity</i>														