

# BACHELOR of ECONOMICS



**Thammasat University  
Faculty of Economics  
Bachelor of Economics (International Program)**

# AC201

## Fundamental Accounting

Semester 2/2011  
(January - April, 2012)

### Course Materials

**Topic:**

Chapter 02 Investing and Financing  
Decisions and the Balance Sheet

**Session:**

Session #2

**Instructor:**

Ajarn Santana Singhasaneh





## CHAPTER 2: INVESTING AND FINANCING DECISIONS AND THE BALANCE SHEET

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## Overview of Accounting Concepts

2



## Objective of Financial Reporting

To provide *useful* economic information  
about a business  
to help external users  
make sound financial decisions.

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## Qualitative Characteristics of Financial Information

For the information to be useful:

1. **Relevancy**
  - possessing predictive and feedback value
  - timely
2. **Reliability**
  - neutral
  - represents reality
  - verifiable

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## Accounting Assumptions & Principle (1)

Four accounting assumptions & principle underlie reporting on the balance sheet:

- a. **Separate-entity assumption** - transactions of the business are accounted for separately from transactions of the owner.
- b. **Unit-of-measure assumption** - financial information is reported in the national monetary unit.

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## Accounting Assumptions & Principle (2)

- c. **Continuity (going-concern) assumption** - a business is expected to continue to operate into the foreseeable future.
- d. **Historical cost principle** - financial statements elements should be recorded at the cash-equivalent cost on the date of the transaction.

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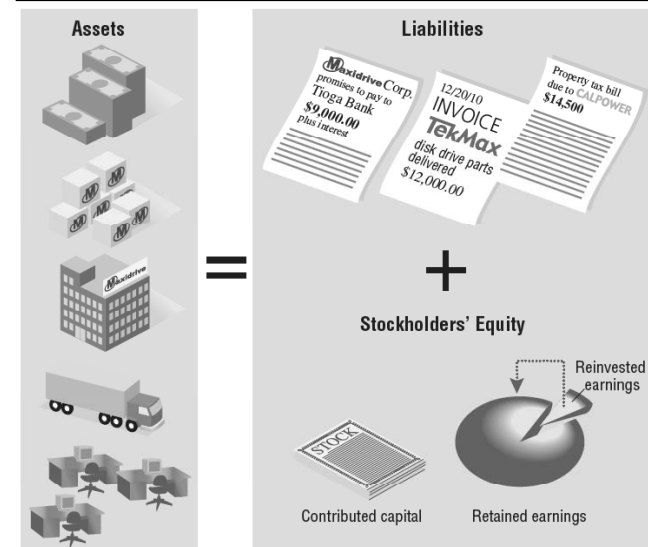
## Exceptions to Measurement & Reporting Rules

- a. **Materiality exception** - immaterial amounts (those that do not affect a decision) can be accounted for in the least costly, most expedient manner.
- b. **Conservatism exception** - information should be conservative (assets and revenues are not overstated and liabilities and expenses are not understated).

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## The Accounting Equation



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## Elements of the Balance Sheet

$$A = L + SE$$

Economic resources with probable future benefits owned or controlled by the entity. Measured by the historical cost principle.

Probable debts or obligations (claims to a company's resources) that result from a company's past transactions and will be paid with assets or services. Entities that a company owes money to are called creditors.

The financing provided by the owners and by business operations. Often referred to as contributed capital.

<b>Assets</b>	=	<b>Liabilities</b>	+	<b>Owners' Equity</b>
[Resources]		[A method of financing resources that requires repayment]*		[A method of financing resources that does not require repayment and represents ownership interests in the business]



## Papa John's Balance Sheet

Papa John's Balance Sheet as at **December 31, 2008**

PAPA JOHN'S INTERNATIONAL, INC.  
**Consolidated Balance Sheet**  
**December 31, 2008**  
(dollars in thousands)

*point in time the balance sheet is prepared  
(at year-end in this case)*

**ASSETS**

**Current Assets**

Current assets

Cash	\$ 11,000
Accounts receivable	24,000
Supplies	17,000
Prepaid expenses	10,000
Other current assets	<u>13,000</u>
<b>Total current assets</b>	<b>75,000</b>

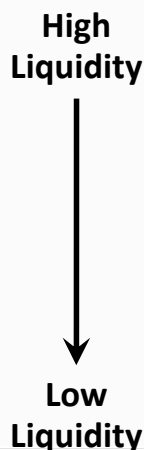
*payments due from franchisees and others on account  
food, beverages, and paper supplies on hand  
rent, advertising, and/or insurance paid in advance  
a summary of several current assets with smaller balances*

**Noncurrent Assets**

Noncurrent assets

Investments	1,000
Property and equipment (net)	190,000
Notes receivable	8,000
Intangibles	77,000
Other assets	<u>36,000</u>
<b>Total assets</b>	<b><u>\$387,000</u></b>

*another company's stocks and bonds purchased with excess cash  
the remaining cost of long-lived assets to be used in future  
operations (original cost \$388,000 minus \$198,000,  
the estimated portion of cost already used in the past)  
long-term amounts due from franchisees  
patents, trademarks, and goodwill  
a summary of several long-term assets with smaller balances*



## Papa John's Balance Sheet

Papa John's Balance Sheet as at **December 31, 2008 (cont'd)**

**LIABILITIES AND STOCKHOLDERS' EQUITY**

**Current Liabilities**

Current liabilities

Accounts payable	\$ 29,000
Accrued expenses payable	<u>71,000</u>
<b>Total current liabilities</b>	<b>100,000</b>

*payments due to suppliers  
a summary of payroll, rent, and other obligations*

**Noncurrent Liabilities**

Noncurrent liabilities

Unearned franchise fees	6,000
Notes payable	124,000
Other long-term liabilities	<u>27,000</u>
<b>Total liabilities</b>	<b>257,000</b>

*amounts paid by franchisees for services they will receive  
loans from creditors*

**Stockholders' Equity\***

Contributed capital	7,000
Retained earnings	<u>123,000</u>
<b>Total stockholders' equity</b>	<b>130,000</b>

*amounts received from contributors (investors)  
cumulative profits not distributed to investors*

<b>Total liabilities and stockholders' equity</b>	<b><u>\$387,000</u></b>
---	-------------------------

**Investment Reinvestment**





## What Business Activities Cause Changes in Financial Statement Amounts ?



## Transactions

**Transactions** are events that have an economic impact on the entity.

Transactions include 2 types of events:

- **External event** - an exchange between a business and one or more external parties to a business
- **Internal event** - a measurable internal event, such as adjustments for the use of assets in operations.



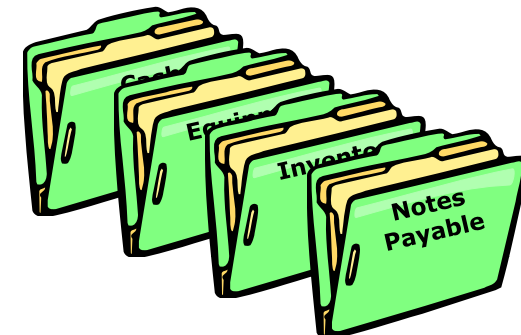
## Nature of Business Transactions

Most transactions with external parties involve an exchange where the business entity gives up something but receives something in return.



## Accounts

An account is a standardized format that organizations use to accumulate the dollar effects of transactions related to each financial statement item.





## Accounts

EXHIBIT 3.6 Chart of Accounts for a Typical Company

### Assets (100-199)

**Current Assets (100-150):**  
 101 Cash  
 103 Notes Receivable  
 105 Accounts Receivable  
 107 Inventory  
 108 Supplies

**Long-Term Assets (151-199):**  
 151 Land  
 152 Buildings  
 154 Office Furniture or Equipment

### Liabilities (200-299)

**Current Liabilities (200-219):**  
 201 Notes Payable  
 202 Accounts Payable  
 203 Salaries Payable  
 204 Interest Payable  
 206 Income Taxes Payable

**Long-Term Liabilities (220-239):**  
 222 Mortgage Payable

### Owners' Equity (300-399)

301 Capital Stock  
 330 Retained Earnings

### Sales (400-499)

400 Sales Revenue

### Expenses (500-599)

500 Cost of Goods Sold  
 501 Sales Salaries and Commissions  
 523 Rent Expense  
 525 Travel Expense  
 528 Advertising Expense  
 551 Officers' Salaries  
 553 Administrative Salaries  
 570 Payroll Taxes  
 571 Office Supplies Expense  
 573 Utilities Expense  
 578 Office Equipment Rent Expense  
 579 Accounting and Legal Fees



## Balance Sheet Accounts

### Typical Balance Sheet Account Titles

#### Assets

Cash  
 Short-Term Investment  
 Accounts Receivable  
 Notes Receivable  
 Inventory (to be sold)  
 Supplies  
 Prepaid Expenses  
 Long-Term Investments  
 Equipment  
 Buildings  
 Land  
 Intangibles

#### Liabilities

Accounts Payable  
 Accrued Expenses  
 Notes Payable  
 Taxes Payable  
 Unearned Revenue  
 Bonds Payable

#### Stockholders' Equity

Contributed Capital  
 Retained Earnings



## How do Transactions Affect Accounts?



## The Accounting Cycle

### Start of new period

### During the Period (Chapters 2 and 3)

- Analyze transactions → **Transaction Analysis**
- Record journal entries in the general journal
- Post amounts to the general ledger

### At the End of the Period (Chapter 4)

- Prepare a trial balance to determine if debits equal credits
- Adjust revenues and expenses and related balance sheet accounts (record in journal and post to ledger)
- Prepare a complete set of financial statements and disseminate it to users
- Close revenues, gains, expenses, and losses to Retained Earnings (record in journal and post to ledger)



## Principles of Transaction Analysis

### 1. Dual Effects

Every transaction affects **at least two accounts**.

### 2. Balancing the Accounting Equation

The accounting equation must remain in **balance** after each transaction.

$$A = L + SE$$



## Steps of Transaction Analysis

### Step 1: Identify and classify accounts and effects

- **Identify the accounts** (by title) affected and make sure at least two accounts change.
- Classify them by **type of account**.  
Was each account an asset (A), a liability (L), or a stockholders' equity (SE)?
- Determine the **direction of the effects**.  
Did the account increase [+] or decrease [-]?

### Step 2: Verify account equation is in balance

- Verify that the accounting equation ( $A = L + SE$ ) remains in balance.



## Using Accounts to Categorize Transactions

- An account is a specific accounting record that provides an efficient way to categorize similar transactions.
- An individual account is a summary of every transaction affecting a certain item (like cash).

	Assets				=	Liabilities		+	Stockholders' Equity	
	Cash	Investments	Equip.	Notes Receivable		Dividends Payable	Notes Payable		Contributed Capital	Retained Earnings
(a)										
(b)										
(c)										
(d)										
(e)										
(f) Effect					=					



## Transaction Analysis: Example

### Papa John's Balance Sheet as at December 31, 2008

PAPA JOHN'S INTERNATIONAL, INC.  
Consolidated Balance Sheet  
December 31, 2008  
(dollars in thousands)

*point in time the balance sheet is prepared  
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*payments due from franchisees and others on account  
food, beverages, and paper supplies on hand  
rent, advertising, and/or insurance paid in advance  
a summary of several current assets with smaller balances*

**Total current assets** 75,000

Investments	1,000
Property and equipment (net)	190,000

Noncurrent assets

Notes receivable	8,000
Intangibles	77,000
Other assets	<u>36,000</u>

*another company's stocks and bonds purchased with excess cash  
the remaining cost of long-lived assets to be used in future  
operations (original cost \$388,000 minus \$198,000,  
the estimated portion of cost already used in the past)  
long-term amounts due from franchisees  
patents, trademarks, and goodwill  
a summary of several long-term assets with smaller balances*

**Total assets** \$387,000

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## Transaction Analysis: Example

### Papa John's Balance Sheet as at December 31, 2008 (cont'd)

**LIABILITIES AND STOCKHOLDERS' EQUITY**

**Current Liabilities**

Current liabilities

Accounts payable	\$ 29,000
Accrued expenses payable	<u>71,000</u>

*payments due to suppliers  
a summary of payroll, rent, and other obligations*

**Total current liabilities** 100,000

Noncurrent liabilities

Unearned franchise fees	6,000
Notes payable	124,000
Other long-term liabilities	<u>27,000</u>

*amounts paid by franchisees for services they will receive  
loans from creditors*

**Total liabilities** 257,000

**Stockholders' Equity\***

Contributed capital	7,000
Retained earnings	<u>123,000</u>

*amounts received from contributors (investors)  
cumulative profits not distributed to investors*

**Total stockholders' equity** 130,000

**Total liabilities and stockholders' equity** \$387,000

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## Transaction Analysis: Example

Followings were transactions incurred during the month of **January 2009** for Papa John's International Inc.:

- Papa John's issues \$2,000 of additional common stock to new investors for cash.
- Papa John's borrows \$6,000 from the bank signing a three-year note.
- Papa John's purchases new ovens, counters, refrigerators, and other equipment costing \$10,000, paying \$2,000 in cash and signing a two-year note for the balance.
- Papa John's lends \$3,000 cash to new franchisees who sign notes to be repaid in five years.
- Papa John's purchases the stock of another company as a long-term investment, paying \$1,000 in cash.
- The board of directors declares that Papa John's will pay \$3,000 in cash dividends to shareholder next month.

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## Analyzing Transactions

- Papa John's issues \$2,000 of additional common stock to new investors for cash.

### Step 1: Identify and classify accounts and effects

- Cash (+A) \$2,000.
- Contributed Capital (+SE) \$2,000.

### Step 2: Is the accounting equation in balance?

	Assets				=	Liabilities		+	Stockholders' Equity	
	Cash	Investments	Equip.	Notes Receivable		Dividends Payable	Notes Payable		Contributed Capital	Retained Earnings
(a)	2,000								2,000	
(b)										
(c)										
(d)										
(e)										
(f)										
Effect					=					
				2,000					2,000	

$$A = L + SE$$

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## Analyzing Transactions

- Papa John's borrows \$6,000 from the bank signing a three-year note.

### Step 1: Identify and classify accounts and effects

- Cash (+A) \$6,000.
- Notes Payable (+L) \$6,000.

### Step 2: Is the accounting equation in balance?

	Assets				=	Liabilities		+	Stockholders' Equity	
	Cash	Investments	Equip.	Notes Receivable		Dividends Payable	Notes Payable		Contributed Capital	Retained Earnings
(a)	2,000								2,000	
(b)	6,000						6,000			
(c)										
(d)										
(e)										
(f)										
Effect					=					
				8,000					8,000	

$$A = L + SE$$

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## Analyzing Transactions

- Papa John's purchases new ovens, counters, refrigerators, and other equipment costing \$10,000, paying \$2,000 in cash and signing a two-year note for the balance.

### Step 1: Identify and classify accounts and effects

- Equipment (+A) \$10,000.
- Cash (-A) \$2,000  
Notes Payable (+L) \$8,000.

### Step 2: Is the accounting equation in balance?

	Assets				=	Liabilities		+	Stockholders' Equity	
	Cash	Investments	Equip.	Notes Receivable		Dividends Payable	Notes Payable		Contributed Capital	Retained Earnings
(a)	2,000								2,000	
(b)	6,000						6,000			
(c)	(2,000)		10,000				8,000			
(d)										
(e)										
(f)										
Effect					=					
				16,000					16,000	

$$A = L + SE$$

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## Analyzing Transactions

- (d) Papa John's lends \$3,000 cash to new franchisees who sign notes to be repaid in five years.

### Step 1: Identify and classify accounts and effects

1. Notes Receivable (+A) \$3,000. 2. Cash (-A) \$3,000.

### Step 2: Is the accounting equation in balance?

	Assets				=	Liabilities		+	Stockholders' Equity		
	Cash	Investments	Equip.	Notes Receivable		Dividends Payable	Notes Payable		Contributed Capital	Retained Earnings	
(a)	2,000								2,000		
(b)	6,000										
(c)	(2,000)		10,000				6,000				
(d)	(3,000)			3,000			8,000				
(e)											
(f)											
Effect	16,000				=	16,000					

**A = L + SE**

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## Analyzing Transactions

- (e) Papa John's purchases the stock of another company as a long-term investment, paying \$1,000 in cash.

### Step 1: Identify and classify accounts and effects

1. Investment (+A) \$1,000. 2. Cash (-A) \$1,000.

### Step 2: Is the accounting equation in balance?

	Assets				=	Liabilities		+	Stockholders' Equity		
	Cash	Investments	Equip.	Notes Receivable		Dividends Payable	Notes Payable		Contributed Capital	Retained Earnings	
(a)	2,000								2,000		
(b)	6,000										
(c)	(2,000)		10,000				6,000				
(d)	(3,000)			3,000			8,000				
(e)	(1,000)	1,000									
(f)											
Effect	16,000				=	16,000					

**A = L + SE**

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## Analyzing Transactions

- (f) The board of directors declares that Papa John's will pay \$3,000 in cash dividends to shareholder next month.

### Step 1: Identify and classify accounts and effects

1. Retained Earnings (-SE) \$3,000. 2. Dividends Payable (+L) \$3,000.

### Step 2: Is the accounting equation in balance?

	Assets				=	Liabilities		+	Stockholders' Equity		
	Cash	Investments	Equip.	Notes Receivable		Dividends Payable	Notes Payable		Contributed Capital	Retained Earnings	
(a)	2,000								2,000		
(b)	6,000										
(c)	(2,000)		10,000				6,000				
(d)	(3,000)			3,000			8,000				
(e)	(1,000)	1,000									
(f)						3,000				(3,000)	
Effect	16,000				=	16,000					

**A = L + SE**

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## How do Companies Keep Track of Account Balances ?

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## How Do Companies Keep Track of Account Balances ?

- There are difficulties of tracking multiple accounts, involving hundreds of transactions, using the spreadsheet method below while doing all the computations by hand.

	Assets				=	Liabilities		+	Stockholders' Equity	
	Cash	Investments	Equip.	Notes Receivable		Dividends Payable	Notes Payable		Contributed Capital	Retained Earnings
(a)	2,000								2,000	
(b)	6,000									
(c)	(2,000)		10,000				6,000			
(d)	(3,000)			3,000			8,000			
(e)	(1,000)	1,000								
(f)						3,000				(3,000)
Effect	16,000				=	16,000				

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## How Do Companies Keep Track of Account Balances ?

- The problem can be solved by separating the “+” and the “-” for each account into separate columns, totaling each column, and then computing the difference between the columns to arrive at an ending balance.
- The simplest, most fundamental format is the configuration of the letter T. This is called a **T-account**.
- A T-account is an abbreviated representation of an actual account (illustrated later) and is used as a teaching and learning tool.

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## How Do Companies Keep Track of Account Balances ?

- The followings are examples of T-accounts, representing the transactions described previously.
- The account title (Cash, for example) appears at the top of the T-account. Transaction amounts may be recorded on both the left side and the right side of the T-account.

Cash	Investments	Equipment
Notes Receivable	Dividend Payable	Notes Payable
Contributed Capital	Retained Earnings	

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## How Do Companies Keep Track of Account Balances ?

- Instead of using the terms left and right to indicate which side of a T-account is affected, terms unique to accounting were developed.
- **Debit** (abbreviated Dr) is used to indicate the left side of a T-account.
- **Credit** (abbreviated Cr) is used to indicate the right side of a T-account.
- **Debit means left, credit means right.**

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## How Do Companies Keep Track of Account Balances ?

Assets		=	Liabilities		+	Stockholders' Equity	
Debit	Credit		Debit	Credit		Debit	Credit
(+)	(-)		(-)	(+)		(-)	(+)
Accounts have debit balances				Accounts have credit balances			Accounts have credit balances

**Asset accounts**  
are increased by *debits* and decreased by *credits*.

**Liability and owners' equity accounts**  
are decreased by *debits* and increased by *credits*.

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## How Do Companies Keep Track of Account Balances ?

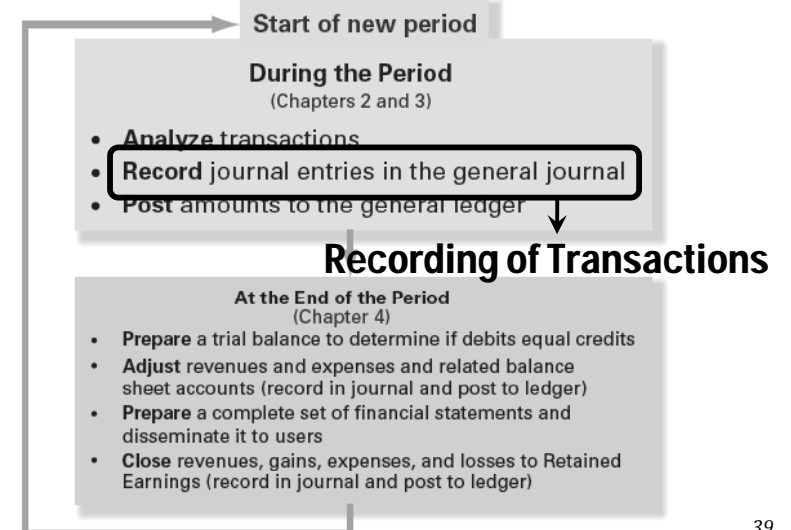
Basic facts regarding **double-entry accounting**:

1. Debits are always entered on the left side of an account and credits on the right side.
2. For every transaction, there must be at least one debit and one credit.
3. Debits must always equal credits for each transaction.

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## The Accounting Cycle



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## Recording of Transactions

Two important tools used by accountants:

- Journal Entries** – After analyzing a transaction, the effects of the transaction is recorded in a debits-equal-credits format. The accounts and amounts to be debited are listed first. Then the accounts and amounts to be credited are listed below the debits and indented, resulting in debits on the left and credits on the right.

### General Journal Entry Format

Date    Debit Entry ..... XX  
           Credit Entry ..... XX  
           Explanation.



## Recording of Transactions

A journal entry might look like this:

		Debit	Credit
(c)	Property and Equipment (+A)	10,000	
	Cash (-A)		2,000
	Notes Payable (+L)		8,000

Reference:  
Letter,  
number, or  
date.

Account Titles:  
Debited accounts on top.  
Credited accounts on bottom  
usually indented.

Amounts:  
Debited amounts on left.  
Credited amounts on right.

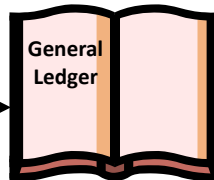


## Recording of Transactions

After journal entries are prepared, the accountant posts (transfers) the dollar amounts to each account affected by the transaction to the **General Ledger**

	Debit	Credit
(c) Property and Equipment (+A)	10,000	
Cash (-A)		2,000
Notes Payable (+L)		8,000

Post →



Journal entries  
do NOT provide  
the account balances

Posting to general ledgers  
help determining  
the account balances



## Recording of Transactions

### 2. T-Account

- a simplified representation of a ledger account
- a useful tool for summarizing the transactions effects and determining the balances for each account.

101 - Cash	
12/31/08 Bal.	11,000
1/2/09	2,000
1/6/09	6,000
	<u>19,000</u>



## Analyzing Transactions

- (a) Papa John's issues \$2,000 of additional common stock to new investors for cash.

### Step 1: Identify and classify accounts and effects

1. Cash (+A) \$2,000.      2. Contributed Capital (+SE) \$2,000.

### Step 2: Is the accounting equation in balance?

	Assets				= Liabilities		+ Stockholders' Equity	
	Cash	Investments	Equip.	Notes Receivable	Dividends Payable	Notes Payable	Contributed Capital	Retained Earnings
(a)	2,000						2,000	
(b)								
(c)								
(d)								
(e)								
(f)								
Effect	2,000				=		2,000	

$$A = L + SE$$

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## Analyzing Transactions

- (b) Papa John's borrows \$6,000 from the bank signing a three-year note.

### Step 1: Identify and classify accounts and effects

1. Cash (+A) \$6,000.      2. Notes Payable (+L) \$6,000.

### Step 2: Is the accounting equation in balance?

	Assets				= Liabilities		+ Stockholders' Equity	
	Cash	Investments	Equip.	Notes Receivable	Dividends Payable	Notes Payable	Contributed Capital	Retained Earnings
(a)	2,000						2,000	
(b)	6,000					6,000		
(c)								
(d)								
(e)								
(f)								
Effect	8,000				=		8,000	

$$A = L + SE$$

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## Recording of Transactions

- (a) Papa John's issues \$2,000 of additional common stock to new investors for cash.

### General Journal

Date	Account Titles and Explanation	Ref.	Debit	Credit
1/2/09	Cash	101	2,000	
	Contributed Capital	301		2,000
	Investment by stockholders			

### 101 - Cash

12/31/08 Bal.	11,000
1/2/09	2,000
	<u>13,000</u>

### 301 - Contributed Capital

	7,000	12/31/08 Bal.
	2,000	1/2/09
	<u>9,000</u>	

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## Analyzing Transactions

- (b) Papa John's borrows \$6,000 from the bank signing a three-year note.

### Step 1: Identify and classify accounts and effects

1. Cash (+A) \$6,000.      2. Notes Payable (+L) \$6,000.

### Step 2: Is the accounting equation in balance?

### General Journal

Date	Account Titles and Explanation	Ref.	Debit	Credit
1/6/09	Cash	101	6,000	
	Notes Payable	204		6,000
	Borrowed from bank			

### 101 - Cash

12/31/08 Bal.	11,000
1/2/09	2,000
1/6/09	6,000
	<u>19,000</u>

### 204 - Notes Payable

	124,000	12/31/08 Bal.
	6,000	1/6/09
	<u>130,000</u>	

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Following are the T-accounts (in thousands of dollars) that **changed** during the period because of these transactions. The beginning balances are the amounts from the December 31, 2008, Papa John's balance sheet. The balances of all other accounts remained the same.

+ Cash (A) -			
12/31/08 bal.	11,000		
(a)	2,000	2,000	(c)
(b)	6,000	3,000	(d)
		1,000	(e)
1/31/09 bal.		<u>13,000</u>	

+ Investments (A) -			
12/31/08 bal.	1,000		
(e)	1,000		
1/31/09 bal.		<u>2,000</u>	

+ Property and Equipment, Net (A) -			
12/31/08 bal.	190,000		
(c)	10,000		
1/31/09 bal.		<u>200,000</u>	

+ Notes Receivable (A) -			
12/31/08 bal.	8,000		
(d)	3,000		
1/31/09 bal.		<u>11,000</u>	

- Notes Payable (L) +			
	124,000	12/31/08 bal.	
	6,000	(b)	
	8,000	(c)	
		<u>138,000</u>	
1/31/09 bal.			

- Dividends Payable (L) +			
	0	12/31/08 bal.	
	3,000	(f)	
		<u>3,000</u>	
1/31/09 bal.			

- Contributed Capital (SE) +			
	7,000	12/31/08 bal.	
	2,000	(a)	
		<u>9,000</u>	
1/31/09 bal.			

- Retained Earnings (SE) +			
(f)	3,000	123,000	12/31/08 bal.
		<u>120,000</u>	
1/31/09 bal.			



## How is the Balance Sheet Prepared and Analyzed?

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## How is the Balance Sheet Prepared and Analyzed?

- After analyzing a transaction, a **JOURNAL ENTRY** is posted.
- The transaction is then posted to the **GENERAL LEDGER**.
- **T-ACCOUNTS** are used to illustrate this process.
- The **BALANCE SHEET** is then prepared using the balances shown in the T-accounts.

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## Papa John's Balance Sheets

Balance Sheets as at **January 31, 2009** and **December 31, 2008**

Most recent balance sheet amounts are usually listed on the left

A JOHN'S INTERNATIONAL, INC.  
Consolidated Balance Sheets  
(dollars in thousands)

\$ are indicated at the top and bottom of the asset sections and of the liabilities & shareholders' equity section

	January 31, 2009	December 31, 2008
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash	\$ 13,000	\$ 11,000
Accounts receivable	24,000	24,000
Supplies	17,000	17,000
Prepaid expenses	10,000	10,000
Other current assets	13,000	13,000
<b>Total current assets</b>	<b>77,000</b>	<b>75,000</b>
Investments	2,000	1,000
Property and equipment (net)	200,000	190,000
Notes receivable	11,000	8,000
Intangibles	77,000	77,000
Other assets	36,000	36,000
<b>Total assets</b>	<b>\$403,000</b>	<b>\$387,000</b>

**Assets and liabilities are classified into two categories: current and noncurrent.**

**Current assets are those to be used or turned into cash within the upcoming year**

**Noncurrent assets are those that will last longer than one year**



## Papa John's Balance Sheets

Balance Sheets as at **January 31, 2009** and **December 31, 2008**

\$ are indicated at the top and bottom of the asset sections and of the liabilities & shareholders' equity section

<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 29,000	\$ 29,000
Dividends payable	3,000	0
Accrued expenses payable	71,000	71,000
<b>Total current liabilities</b>	<b>103,000</b>	<b>100,000</b>
Unearned franchise fees	6,000	6,000
Notes payable	138,000	124,000
Other long-term liabilities	27,000	27,000
<b>Total liabilities</b>	<b>274,000</b>	<b>257,000</b>
<b>Stockholders' Equity</b>		
Contributed capital	9,000	7,000
Retained earnings	20,000	123,000
<b>Total stockholders' equity</b>	<b>29,000</b>	<b>130,000</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$403,000</b>	<b>\$387,000</b>

**Current liabilities are those obligations to be paid or settled within the next 12 months with current assets.**



## Current Ratio

$$\text{Current Ratio} = \frac{\text{Current Assets}}{\text{Current Liabilities}}$$

Current ratio for Papa John's:

2006 = 0.83

2007 = 0.68

2008 = 0.75

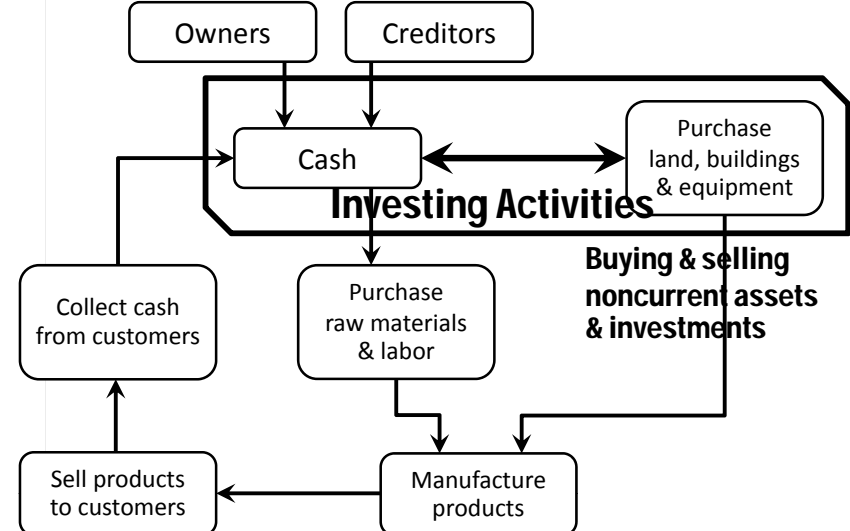
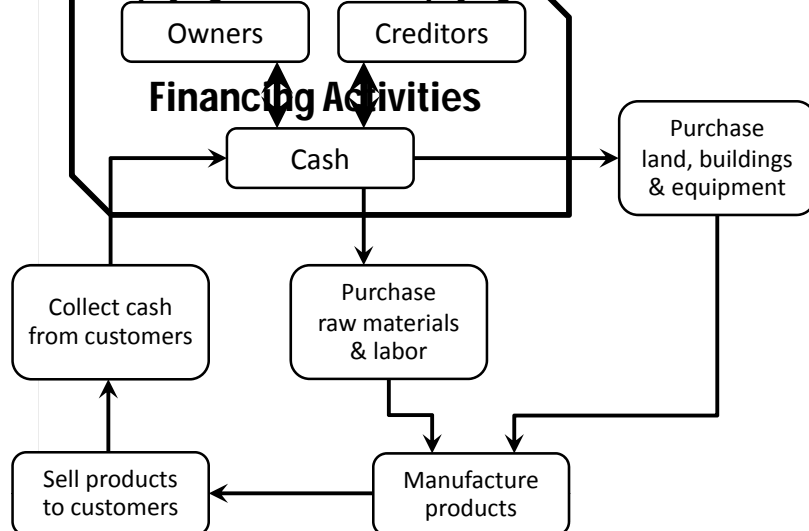
The current ratio for Papa John's shows a low level of liquidity, below 1.



## Focus on Cash Flows - Investing & Financing Activities



## Issuing & repurchasing stocks & paying dividends Borrowing & repaying debts





## Statement of Cash Flows

Companies report cash inflows and outflows over a period in their statement of cash flows.

<b>Operating activities</b>	
(Covered in the next chapter.)	
<b>Investing Activities</b>	
Purchasing long-term assets and investments for cash	—
Selling long-term assets and investments for cash	+
Lending cash to others	—
Receiving principal payments on loans made to others	+
<b>Financing Activities</b>	
Borrowing cash from banks	+
Repaying the principal on borrowings from banks	—
Issuing stock for cash	+
Repurchasing stock with cash	—
Paying cash dividends	—

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## Investing & Financing Activities

PAPA JOHN'S INTERNATIONAL, INC.  
 Consolidated Statement of Cash Flows  
 For the month ended January 31, 2009  
 (in thousands)

<b>Operating activities</b>	
(None in this chapter.)	
<b>Investing activities</b>	
Purchased property and equipment (c)	\$ (2,000)
Purchased investments (e)	(1,000)
Lent funds to franchisees (d)	(3,000)
Net cash used in investing activities	<b>(6,000)</b>
<b>Financing activities</b>	
Issued common stock (a)	2,000
Borrowed from banks (b)	6,000
Net cash provided by financing activities	<b>8,000</b>
Net increase in cash	2,000
Cash at beginning of month	11,000
<b>Cash at end of month</b>	<b><u>\$13,000</u></b>

Items are referenced to events (a) through (f) illustrated in this chapter.

Also called capital expenditures.

← Agrees with the amount on the balance sheet.

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## End of Chapter 2



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## **EXERCISE 2 – 1**

### **ANALYZING TRANSACTIONS**

Analyze each of the following transactions of World Wide Webster by performing each of the following. Then, use the chart on the following page to keep track of the amount in each account:

(a) Stockholder invests \$10,000 into the business.

1.	Decide if a transaction took place.	Yes – received cash and gave stock.
2.	Identify the accounts affected.	Cash and Contributed Capital
3.	Classify each account affected.	Cash is an Asset (A) and Contributed Capital is Stockholders' Equity (SE)
4.	Identify direction and amount.	Cash (A) + \$10,000 = Stockholders' Equity (SE) + \$10,000.
5.	Ensure the accounting equation is in balance.	Yes – see below.

(b) Borrow \$15,000, using a note payable to the bank.

1.	Decide if a transaction took place.	
2.	Identify the accounts affected.	
3.	Classify each account affected.	
4.	Identify direction and amount.	
5.	Ensure the accounting equation is in balance.	

(c) Acquire a \$15,000 truck and \$5,000 worth of equipment.

1.	Decide if a transaction took place.	
2.	Identify the accounts affected.	
3.	Classify each account affected.	
4.	Identify direction and amount.	
5.	Ensure the accounting equation is in balance.	

(d) Purchase \$300 worth of supplies on credit. "On credit" means that you receive the supplies now, and pay for them later.

1.	Decide if a transaction took place.	
2.	Identify the accounts affected.	
3.	Classify each account affected.	
4.	Identify direction and amount.	
5.	Ensure the accounting equation is in balance.	

(e) Sign contract for first website design for \$10,000.

1.	Decide if a transaction took place.	No – no exchange took place.
2.	Identify the accounts affected.	
3.	Classify each account affected.	
4.	Identify direction and amount.	
5.	Ensure the accounting equation is in balance.	

(f) Company pays off \$300 Accounts Payable.

1.	Decide if a transaction took place.	
2.	Identify the accounts affected.	
3.	Classify each account affected.	
4.	Identify direction and amount.	
5.	Ensure the accounting equation is in balance.	

(g) Company pays for and receives \$600 worth of supplies.

1.	Decide if a transaction took place.	
2.	Identify the accounts affected.	
3.	Classify each account affected.	
4.	Identify direction and amount.	
5.	Ensure the accounting equation is in balance.	

(h) Company acquires and receives \$1,000 worth of equipment.

1.	Decide if a transaction took place.	Yes – paid cash to purchase equipment
2.	Identify the accounts affected.	Cash and Equipment
3.	Classify each account affected.	Cash is an Asset (A) and Equipment is an Asset (A)
4.	Identify direction and amount.	Cash (A) – \$1,000 and Equipment (A) - \$1,000
5.	Ensure the accounting equation is in balance.	Yes - see below.

(i) Order a \$900 snow blower, to be delivered next month.

1.	Decide if a transaction took place.	
2.	Identify the accounts affected.	
3.	Classify each account affected.	
4.	Identify direction and amount.	
5.	Ensure the accounting equation is in balance.	

### Chart

	Assets				=	Liabilities			+	SE	
Ref.	Cash	+	Supplies	+	Property, Plant & Equipment	=	Accounts Payable	+	Notes Payable	+	Contributed Capital
(a)											
(b)											
(c)											
(d)											
(e)											
(f)											
(g)											
(h)	-1,000				+1,000						
(i)											
Total											
						=				+	

## **EXERCISE 2 – 2**

### **THE DEBIT/CREDIT FRAMEWORK**

Analyze each of the following transactions of World Wide Webster and prepare the journal entry required to record the related transaction.

(a) Stockholder invests \$10,000 into the business.

Debit and credit the accounts affected						
(a)	Cash (+A)	10,000				
	Contributed Capital (+SE)		10,000			
Ensure the equation still balances and debits = credits						
Assets		=	Liabilities	+	Stockholders' Equity	
Cash	+10,000				Contributed Capital	+10,000

(b) Borrow \$15,000 signing a note payable to the bank that is due in three months.

Debit and credit the accounts affected						
Ensure the equation still balances and debits = credits						
Assets		=	Liabilities	+	Stockholders' Equity	

(c) Acquire a \$15,000 truck and \$5,000 worth of equipment.

Debit and credit the accounts affected						
Ensure the equation still balances and debits = credits						
Assets		=	Liabilities	+	Stockholders' Equity	

(d) Purchase \$300 worth of supplies on credit.

Debit and credit the accounts affected				
Ensure the equation still balances and debits = credits				
Assets	=	Liabilities	+	Stockholders' Equity

(e) Sign contract for first website design for \$10,000.

No entry – this is not a transaction

(f) Company pays off \$300 Accounts Payable.

Debit and credit the accounts affected				
Ensure the equation still balances and debits = credits				
Assets	=	Liabilities	+	Stockholders' Equity

(g) Company pays for and receives \$600 worth of supplies.

Debit and credit the accounts affected				
Ensure the equation still balances and debits = credits				
Assets	=	Liabilities	+	Stockholders' Equity

(h) Company acquires and receives \$1,000 worth of equipment.

Debit and credit the accounts affected				
(h)	Equipment (+A)		1,000	
	Cash (-A)			1,000
Ensure the equation still balances and debits = credits				
Assets	=	Liabilities	+	Stockholders' Equity
Equipment	+1,000			
Cash	-1,000			

(i) Order a \$900 computer, to be delivered in 90 days.

Debit and credit the accounts affected


Ensure the equation still balances and debits = credits

Assets	=	Liabilities	+	Stockholders' Equity

**EXERCISE 2 – 3**

**POSTING TO T-ACCOUNTS**

Post the transactions from exercise 2-2 and determine the ending balances of each of the following T-accounts.

Assets				Liabilities				Stockholders' Equity			
+ Cash –				- Accounts Payable +				- Contributed Capital +			
BegBal	0					0	BegBal			0	BegBal
(a)	10,000									10,000	(a)
		1,000	(h)								
+ Supplies –				- Notes Payable +				- Retained Earnings +			
BegBal	0					0	BegBal			0	BegBal
+ Equipment –											
BegBal	0										
(h)	1,000										

