

Accounting Principles 2 (Speedy Study Guides) (Accounting Made Simple For Beginners)

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ACCOUNTING PRINCIPLES II

How Transactions Impact The Accounting Equation

The preceding balance sheet for Edelweiss represented the financial condition at the noted date. But, each new transaction brings about a change in financial condition. Business activity will impact various asset, liability, and/or equity accounts without disturbing the equality of the accounting equation. How does this happen? To reveal the answer to this question, look at four specific cases for Edelweiss. See how each impacts the balance sheet without upsetting the basic equality.

CASE A: COLLECT AN ACCOUNT RECEIVABLE

If Edelweiss Corporation collected \$10,000 from a customer on an existing account receivable (i.e., not a new sale, just the collection of an amount that is due from some previous transaction), then the balance sheet would be revised to show that cash (an asset) increased from \$25,000 to \$35,000, and accounts receivable (an asset) decreased from \$50,000 to \$40,000. As a result total assets did not change, and liabilities and equity accounts were unaffected, as shown in the following illustration.

Assets		Assets		
Cash	\$ 25,000	+ \$10,000	Cash	\$ 35,000
Accounts receivable	50,000	- \$10,000	Accounts receivable	40,000
Inventories	35,000		Inventories	35,000
Land	125,000		Land	125,000
Building	400,000		Building	400,000
Equipment	250,000		Equipment	250,000
Other assets	10,000		Other assets	10,000
Total assets	\$895,000		Total assets	\$895,000

Liabilities		Liabilities		
Accounts payable	\$ 50,000		Accounts payable	\$ 50,000
Loans payable	125,000		Loans payable	125,000
Total liabilities	\$175,000		Total liabilities	\$175,000

Stockholders' equity		Stockholders' equity		
Capital stock	\$120,000		Capital stock	\$120,000
Retained earnings	600,000		Retained earnings	600,000
Total stockholders' equity	720,000		Total stockholders' equity	720,000
Total liabilities and equity	\$895,000		Total liabilities and equity	\$895,000

CASE B: BUY EQUIPMENT VIA LOAN

If Edelweiss Corporation purchased \$30,000 of equipment, agreeing to pay for it later (i.e. taking out a loan), then the balance sheet would be further revised. The Case B illustration shows that equipment (an asset) increased from \$250,000 to \$280,000, and loans payable (a liability) increased from \$125,000 to \$155,000. As a result, both total assets and total liabilities increased by \$30,000.



#1168591 in eBooks 2015-01-21 2015-01-21 File Name: B00SNPITRA | File size: 41.Mb

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