



Fundamentals of Finance

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Three Levels of Record Keeping

- **Level 1 (Source)**

- **Source Documents/Business Papers**

- Examples: Cancelled Checks, Receipts, Deposit slips, Sales tickets, etc.

- **Level 2 (Organization)**

- **Chronological Listing** (By date)

- Journals

- **Categorical listing** (By type)

- Ledgers

- **Level 3 (Summary)**

- **Financial Statements** (Summaries of ledgers)

- Income Statement
- Balance Sheet

Video Library Example

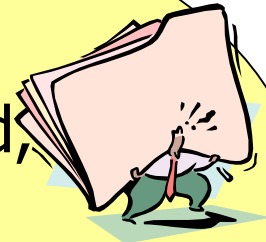
Source

Sales Receipts,
Cancelled Checks,
Labels



Organizing

List of Videos,
By Date Purchased,
By Kind of Movie



Summary

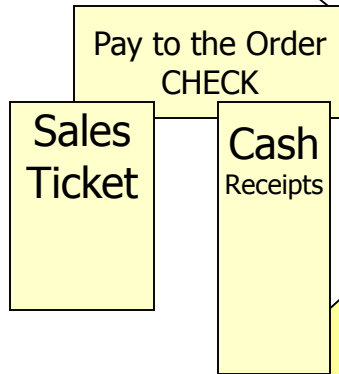
Summary Page



Finance System in Action

Source

Sales Receipts,
Cancelled Checks,
Sales Tickets, Etc.

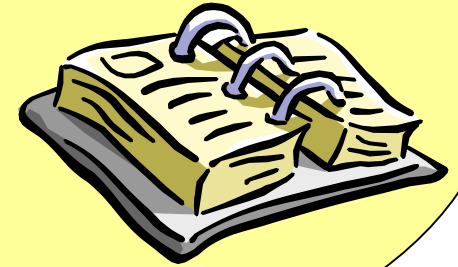


Organizing

Journals

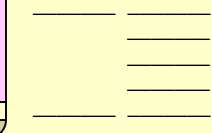


Ledgers

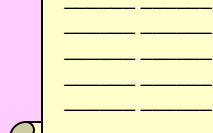


Summary

Income
Statement



Balance
Sheet





Types of Accounts

- **Revenue**

- An inflow of assets in exchange for goods or services

- **Expenses**

- Goods or services consumed in operating a business

- **Assets**

- Property or economic resources owned

- **Liabilities**

- A debt owed

- **Equity**

- Ownership, leftover profits



Income Statement

- Measures the Profit or Loss of a business entity for a **specific period of time**
- Revenues increase Assets and Equity
- Expenses decrease Assets and Equity
- Income Statement tells what the company has made or lost
- Revenues – Expenses = Profit or Loss



Balance Sheet

- An **ongoing** Statement that shows the financial position of a company for any period of time
- The Balance Sheets shows what the company owes or owns
- $\text{Assets} - \text{Liabilities} = \text{Equity}$



Finance Formulas

Income Statement

Revenues – Expenses = Profit or Loss

Balance Sheet

Assets – Liabilities = Equity

Accounting Formula

(Revenues – Expenses) + Assets - Liabilities = Equity

Formula Examples

Income Statement

T.V. Sells for \$750

Cost \$600

Delivery Cost \$50



Revenue **\$750** – Expense **\$600** + **\$50** = Profit **\$100**

If we have other cost like:

Overhead Cost \$40

Insurance Cost \$50

Finance Cost \$15

Revenue **\$750** – Expense **\$600** **\$50** **\$40** **\$50** **\$15** = **Loss \$5**

Formula Examples

Balance Sheet

Do I really own MY car?



Car was bought for	\$10,000
After 2 years I owe	\$8,000
Assets (\$10,000) – Liability (\$8,000) = Equity (\$2,000)	
Car is worth	\$10,000 - \$2,500 Depreciation
After 2 years I owe	\$8,000
Assets (\$7,500) – Liability (\$8,000) = Equity (- \$500)	



What is Accounting?

The systematic organization, recording and summary of the financial information of a business

The Three Levels of Record Keeping



LEVEL 1

SOURCE

Source
Documents



LEVEL 2

ORGANIZATION

Journals and
Ledgers



LEVEL 3

SUMMARY

Summary
Reports



The Accounting Formula

Assets = Liabilities + Equity + Revenues - Expenses

Assets + Expenses = Liabilities + Equity + Revenues

REVENUES increase **EQUITY**

EXPENSES decrease **EQUITY**



Debits and Credits

Left and Right

**Type of
Account**

**Increased
by**

**Decreased
by**

ASSETS

DEBITS

CREDITS

LIABILITIES

CREDITS

DEBITS

EQUITY

CREDITS

DEBITS

REVENUE

CREDITS

DEBITS

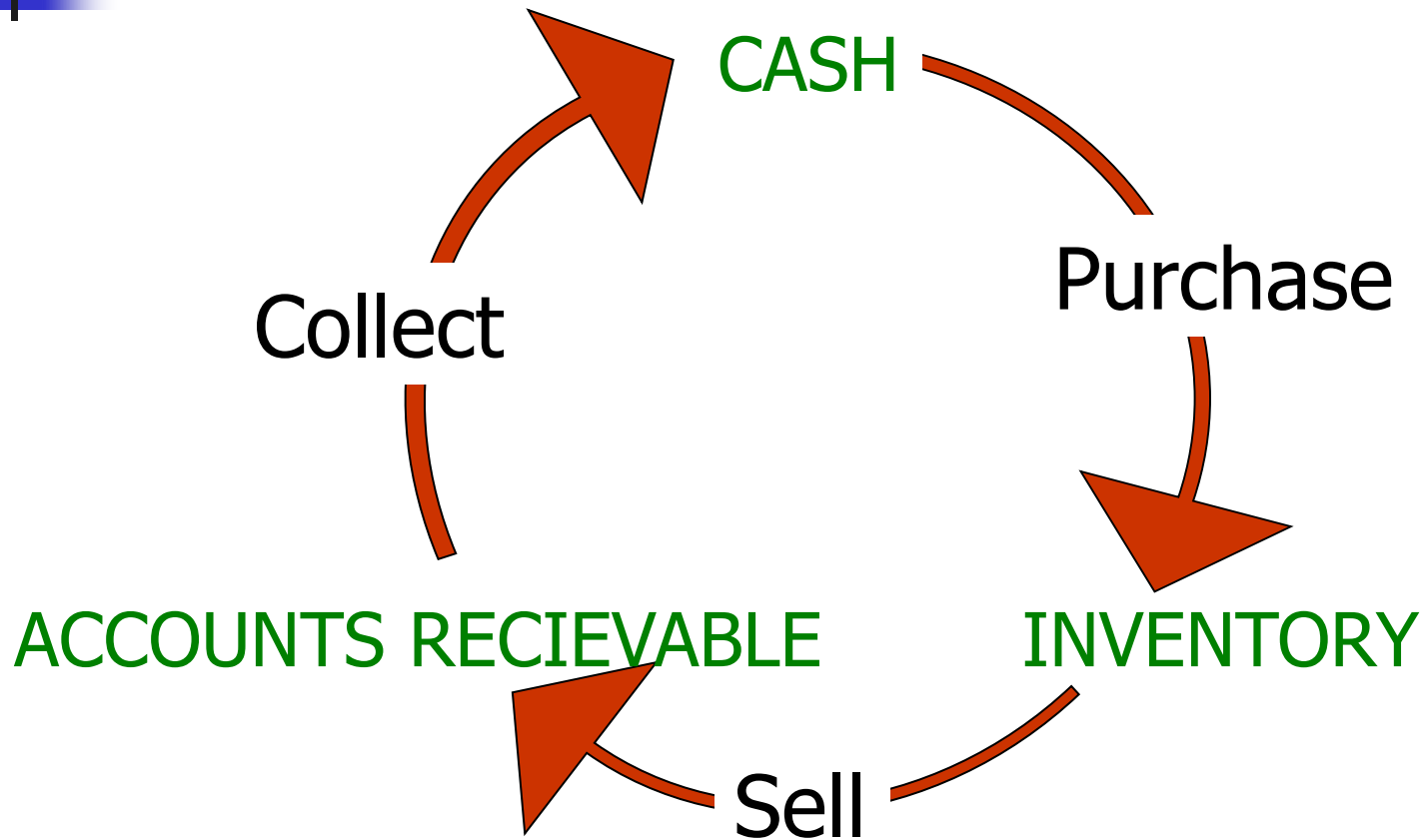
EXPENSE

DEBITS

CREDITS



Normal Operating Cycle





Assets and Liabilities

Assets

Current Assets (Expected to be CASH in 1 year)

Cash, Marketable Securities, Accounts Receivable, Inventory, Prepaid expense

Non-current Assets (Expected to last more than 1 year)

Investments, Property, Plant, and Equipment

Liabilities

Current Liabilities (Expected to be paid in 1 year)

Accounts payable, Revenue Received in advance, normal billings

Long-Term Liabilities

Debts to be paid in more than 1 year



Balance Sheet

A summary of Assets, Liabilities and Equity accounts

$$\text{ASSET} - \text{LIABILITIES} = \text{EQUITY}$$



Income Statement

A summary of Revenues and Expenses

REVENUES – **EXPENSES** = **PROFIT** (or **LOSS**)