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## Basics of Accounting and Reporting: Foundation for Financial Success



This is a foundational course in accounting, designed especially for those who are completely new to the subject or looking to strengthen their understanding of accounting and reporting basics. This course has been structured in a way that all the key concepts are explained using one end-to-end example, making it easier to follow.

## Course Coverage



- Need for Accounting
- Classification of Accounts
- Accounting: Journal Entry, Ledger Accounts, Trial Balance
- Golden Rules of Accounting
- Reporting : Income Statement & Balance Sheet
- Key Accounting Principles

## Need for Accounting



Accounting provides a framework for recording and reporting financial transactions, ensuring transparency and accountability.



Accounting is defined as the systematic process of recording, measuring, and communicating financial information.



Its purpose is to provide valuable insights into an organization's financial performance and position.

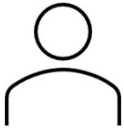
**Accounting** is needed to keep track of money in any business or organization. It helps you know:

- How much money is coming in
- How much is being spent
- What you own (assets)
- What you owe (liabilities)

**Without accounting, it would be very hard to:**

- Know if you're making a profit or loss
- Make good financial decisions
- Pay the correct taxes
- Show your performance to investors, banks, or the government

In short, accounting tells the financial story of an organization in a clear and organized way.



<b>Income:</b>	
Income from Salary	1,00,000
Income from Rent	25,000
<b>Total</b>	<b>1,25,000</b>

<b>Expenses:</b>	
Electricity Bill	1,500
Telephone Bill	2,000
Grocery	15,000
Medical expenses	1,000
School fees	5,000
EMI	55,500
<b>Total</b>	<b>80,000</b>



Income Statement



<b>Assets</b>	
Land	25,00,000
Apartment	40,00,000
Bank Balance-Savings	2,00,000
Jewellery	5,00,000
Mutual Funds	3,00,000
<b>Total</b>	<b>75,00,000</b>

<b>Liabilities</b>	
Loan for land	8,00,000
Loan for Apartment	25,00,000
Personal Loan	3,00,000
<b>Total</b>	<b>36,00,000</b>



Balance Sheet

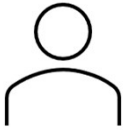
### Personal Accounts vs Company Accounts:

As individuals we all track our income and expenses for each period. All the income and expense for that period is recorded to determine how much we have earned, spent and saved. We also calculate our net worth occasionally which are our Assets minus Liabilities.

Similarly entities report their income, expenses, gains and losses in 'Income Statement' and their assets, liabilities and shareholders equity in 'Balance Sheet'. Thus Income Statement is for a period and Balance Sheet is as on a particular date.

Financial statements provide a summary of an organization's financial activities and position. They are essential for stakeholders to make informed decisions regarding the organization's financial health.

<b>Income:</b>	
Income from Salary	1,00,000
Income from Rent	25,000
<b>Total</b>	<b>1,25,000</b>



<b>Expenses:</b>	
Electricity Bill	1,500
Telephone Bill	2,000
Grocery	15,000
Medical expenses	1,000
School fees	5,000
EMI	55,500
<b>Total</b>	<b>80,000</b>

Savings: 1,25,000-80,000  
 = **45,000** ↑

<b>Assets</b>	
Land	25,00,000
Apartment	40,00,000
Bank Balance-Savings	2,00,000
Jewellery	5,00,000
Mutual Funds	3,00,000
<b>Total</b>	<b>75,00,000</b>

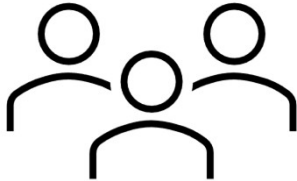


<b>Liabilities</b>	
Loan for land	8,00,000
Loan for Apartment	25,00,000
Personal Loan	3,00,000
<b>Total</b>	<b>36,00,000</b>

Net worth: 75,00,000-36,00,000  
 = **39,00,000** ↑

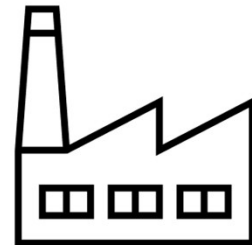
When personal savings increases, it will increase the Net Worth.

Owners/  
Shareholders



Company Name <b>Balance Sheet</b> As of December 31, Year 1	
<u>Assets</u>	<u>Liabilities and Stockholders' Equity</u>
<b>Current assets</b> Cash and cash equivalents Trading securities, at fair value Accounts receivable, net of allowance Notes receivable Inventory Prepaid expenses  <b>Investments</b> Available-for-sale securities, at fair value Held-to-maturity securities Investments in affiliates  <b>Property, plant, and equipment</b> Land Building Equipment Less: accumulated depreciation  <b>Intangible assets</b> Goodwill Patents, net of amortization  <b>Other assets</b> Pension and other postretirement benefit assets Deferred income tax asset  <b>Total assets</b>	<b>Current liabilities</b> Current portion of long-term debt Accounts payable Notes payable Interest payable Salaries payable Unearned revenue  <b>Long-term liabilities</b> Bonds payable Deferred income tax liability Pension and other postretirement benefit liabilities  <b>Total liabilities</b>  <b>Stockholders' equity</b> Capital stock Preferred stock, \$10 par, 8% cumulative and nonparticipating, 10,000 shares authorized, 5,000 shares issued and outstanding Common stock, \$0.01 par, 600,000,000 shares authorized, 57,598,000 shares issued and 57,178,485 shares outstanding Paid-in capital in excess of par Retained earnings Accumulated other comprehensive income (Treasury stock at cost) (419,515 shares)  <b>Total stockholders' equity</b> <b>Total liabilities and stockholders' equity</b>

Company



An entity is distinct from its owners. The capital contributed by owners is a liability because the entity owes it back to them. The goal of any entity is to earn profits, which attract investors. In the Balance Sheet, contributed capital and retained earnings are termed as 'Equity'. Therefore, all assets owned by the entity are funded by external liabilities and shareholders' contributions plus earnings.

Income Statement	
Particulars	Amount (USD)
Sales / Revenue	XXXX
Less: Cost of Goods Sold (COGS)	(XXXX)
<b>Gross Profit</b>	XXXX
Less: Selling, General & Administrative Expenses (S,G&A)	(XXXX)
<b>Operating Income</b>	XXXX
Add/Less: Other Income/Expenses	(XXXX)
<b>Income Before Tax</b>	XXXX
Less: Income Taxes	(XXXX)
<b>Income from Continuing Operations</b>	XXXX
Add/ Less: Discontinued Operations(net of tax)	XXXX
<b>Net Income</b>	<b>XXXX</b>

Company Name Balance Sheet As of December 31, Year 1	
Assets	Liabilities and Stockholders' Equity
<b>Current assets</b> Cash and cash equivalents Trading securities, at fair value Accounts receivable, net of allowance Notes receivable Inventory Prepaid expenses  <b>Investments</b> Available-for-sale securities, at fair value Held-to-maturity securities Investments in affiliates  <b>Property, plant, and equipment</b> Land Building Equipment Less: accumulated depreciation  <b>Intangible assets</b> Goodwill Patents, net of amortization  <b>Other assets</b>  Deferred income tax asset  <b>Total assets</b>	<b>Current liabilities</b> Current portion of long-term debt Accounts payable Notes payable Interest payable Salaries payable Unearned revenue  <b>Long-term liabilities</b> Bonds payable Deferred income tax liability Pension and other postretirement benefit liabilities  <b>Total liabilities</b>  <b>Stockholders' equity</b> Capital stock Preferred stock, \$10 par, 8% cumulative and nonparticipating, 10,000 shares authorized, 5,000 shares issued and outstanding Common stock, \$0.01 par, 600,000,000 shares authorized, 57,598,000 shares issued and 57,178,485 shares  <b>Retained Earnings</b> Accumulated other comprehensive income (Treasury stock at cost) (419,515 shares)  <b>Total stockholders' equity</b>  <b>Total liabilities and stockholders' equity</b>

When a company earns profits, they flow from the Income Statement to 'Retained Earnings' under 'Stockholder's Equity' on the Balance Sheet. Thus, as profits increase, Retained Earnings also increase, and vice versa. This is analogous to how an individual's net worth grows with their savings. For a company,  $Assets = Liabilities + Equity$ .

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## Example- Accounting & Reporting

Let's assume Ms.J starts a manufacturing business, "CLU Manufacturing", with the following simplified transactions occurring in the order below between 01st Jan & 31st Dec XXXX:

No.	Transaction	Amount(\$)
1	Ms.J starts business by contributing capital in cash	5,00,000
2	Purchases Land for cash	1,50,000
3	Purchases Machinery & Building for cash	2,00,000
4	Purchases Raw Material on credit	50,000
5	Pays Labor wages in cash	20,000
6	Pays Factory Rent in cash	10,000
7	Sells Materials for cash (Cost \$30,000, Sold at \$80,000)	

The above is an end-to-end example outlining the flow of transactions from accounting to reporting, with each transaction detailed individually.

**MS.J starts a business, 'CLU Manufacturing' by contributing capital in cash-\$500,000**

Balance Sheet			
Asset	Amount	Liability	Amount
Cash	5,00,000	Capital	5,00,000
Total	5,00,000		5,00,000

<b>Assets</b>	Increase ↑	Debit
	Decrease ↓	Credit

<b>Liabilities</b>	Increase ↑	Credit
	Decrease ↓	Debit

Real Account- Debit what comes in and Credit what goes out.

Personal Account: Debit the receiver and Credit the giver.

Every transaction has two aspects — a debit and a credit. Depending on the nature of the transaction, appropriate accounts are identified for recording. Based on the classification of accounts into Personal, Real, and Nominal, the relevant accounting rules (also known as Golden Rules of Accounting) are applied to create the journal entries.

Transactions must be considered from CLU's perspective. CLU receives \$500,000 in cash as capital funding. This receipt is an asset while the owed capital to Ms. J represents liability.

Cash is a tangible asset, classified as a 'Real Account' under the rule: 'Debit what comes in, Credit what goes out'. Real accounts appear in the Balance Sheet as assets.

Capital, which the entity owes its owner, is a liability and a 'Personal Account', governed by: 'Debit the Receiver, Credit the Giver'. It appears in the Balance Sheet as an asset or liability

**MS.J starts a business, 'CLU Manufacturing' by contributing capital in cash-\$500,000**

• **Journal Entry:**

Debit Cash A/c                      5,00,000  
 Credit Capital A/c                5,00,000

• **Ledger Accounts:**

Cash A/c			
Particulars(Debit)	Amount	Particulars(Credit)	Amount
Capital	5,00,000	Balance c/f	5,00,000
Total	5,00,000	Total	5,00,000

Capital A/c			
Particulars(Debit)	Amount	Particulars(Credit)	Amount
Balance c/f	5,00,000	Cash	5,00,000
Total	5,00,000	Total	5,00,000

• **Trial Balance:**

Trial Balance			
Debit	Amount	Credit	Amount
Cash a/c	5,00,000	Capital a/c	5,00,000
Total	5,00,000	Total	5,00,000

**Income Statement**

Particulars	Amount (\$)
Revenue (Sales)	
Less: Cost of Goods Sold	
Gross Profit	
Operating Expenses:	
- Wages	
- Factory Rent	
- Electricity	
Total Expenses	
<b>Net Profit/Loss</b>	

**Balance Sheet**

Asset	Amount	Liability	Amount
Cash	5,00,000	Capital	5,00,000
Total	5,00,000		5,00,000

First, record transactions in a journal entry:

Debit Cash A/c \$500,000  
 Credit Capital A/c \$500,000

Since accounts can have multiple transactions, journal entries alone don't determine balances. Transactions are transferred to the ledger (T-account). To check arithmetic accuracy of postings, prepare a Trial Balance. It lists all ledger accounts with their Debit or Credit balances. Equal totals in Debit and Credit columns indicate arithmetic correctness but not error-free records.

Use journal entries, ledgers, and trial balances to record and verify financial transactions. Then create financial statements, like the income statement and balance sheet. The transaction above doesn't affect the Income Statement but increases both assets and liabilities on the Balance Sheet, maintaining balance.

## Purchases Land for cash-\$150,000

- Journal Entry:**

Debit Land A/c 1,50,000  
Credit Cash A/c 1,50,000

Debit what comes in  
Credit what goes out

- Ledger Accounts:**

Cash A/c			
Particulars	Amount	Particulars	Amount
Capital	5,00,000	Land	1,50,000
		<b>Balance c/f</b>	<b>3,50,000</b>
Total	5,00,000	Total	5,00,000

Land A/c			
Particulars	Amount	Particulars	Amount
Cash	1,50,000	<b>Balance c/f</b>	<b>1,50,000</b>
Total	1,50,000	Total	1,50,000

- Trial Balance:**

Trial Balance			
Debit	Amount	Credit	Amount
Cash a/c	3,50,000	Capital a/c	5,00,000
Land a/c	1,50,000		
Total	5,00,000	Total	5,00,000

### Income Statement

Particulars	Amount (\$)
Revenue (Sales)	
Less: Cost of Goods Sold	
Gross Profit	
Operating Expenses:	
- Wages	
- Factory Rent	
- Electricity	
Total Expenses	
<b>Net Profit/Loss</b>	

### Balance Sheet

Asset	Amount	Liability	Amount
Cash	3,50,000	Capital	5,00,000
Land	1,50,000		
Total	5,00,000	Total	5,00,000

Land is acquired by CLU for \$150,000 cash. Both are 'Real Accounts'.

**Rule:** 'Debit what comes in, Credit what goes out'. So, Land is debited and Cash is credited.

**Journal Entry:**

Debit Land A/c \$150,000  
Credit Cash A/c \$150,000

**Ledger:**

Posting the transaction reduces Cash to a debit balance of \$350,000 because the debit side (\$500,000) exceeds the credit side (\$150,000). The Land account reflects a debit balance of \$150,000.

**Trial Balance:** Balanced as indicated.

**Income Statement:** No effect.

**Balance Sheet:** Increases 'Land' asset and decreases 'Cash' asset by \$150,000, keeping both sides balanced.

## Purchases Machinery & Building for cash-\$200,000

### Journal Entry:

Debit Machinery & Building A/c 2,00,000  
 Credit Cash A/c 2,00,000

Debit what comes in  
 Credit what goes out

### Ledger Accounts:

Cash A/c			
Particulars	Amount	Particulars	Amount
Capital	5,00,000	Land	1,50,000
		Machinery & Building	2,00,000
		<b>Balance c/f</b>	<b>1,50,000</b>
Total	5,00,000	Total	5,00,000

Machinery & Building			
Particulars	Amount	Particulars	Amount
Cash	2,00,000	<b>Balance c/f</b>	<b>2,00,000</b>
Total	2,00,000	Total	2,00,000

### Trial Balance:

Trial Balance			
Debit	Amount	Credit	Amount
Cash a/c	1,50,000	Capital a/c	5,00,000
Land a/c	1,50,000		
Machinery & Building	2,00,000		
Total	5,00,000	Total	5,00,000

### Income Statement

Particulars	Amount (\$)
Revenue (Sales)	
Less: Cost of Goods Sold	
Gross Profit	
Operating Expenses:	
- Wages	
- Factory Rent	
- Electricity	
Total Expenses	
<b>Net Profit/Loss</b>	

### Balance Sheet

Asset	Amount	Liability	Amount
Cash	1,50,000	Capital	5,00,000
Land	1,50,000		
Machinery & Building	2,00,000		
Total	5,00,000	Total	5,00,000

Machinery and Building are tangibles asset acquired by CLU in exchange for Cash, which is also a tangible asset. Therefore, both are classified as 'Real Accounts. **Rule:** 'Debit what comes in, Credit what goes out'. Hence, 'Machinery and Building account' is debited and Cash account is credited.

### Journal Entry:

Debit Machinery and Building A/c \$200,000  
 Credit Cash A/c \$200,000

### Ledger:

When posted to the Ledger, the Cash account already contains an entry for the previous transactions of Capital receipt and Land purchased. After recording the Machinery and Building purchase, the Cash amount reduces and the Cash account reflects a debit balance of \$150,000. This is because the debit side (\$500,000) exceeds the credit side (\$350,000). The corresponding posting is made to the Machinery and Building account, which shows a debit balance of \$200,000.

**Trial Balance:** Consequently, the Trial Balance is balanced as indicated.

**Income Statement:** The aforementioned transaction does not affect the Income Statement.

**Balance Sheet:** On the Balance Sheet, it increases one asset (i.e., 'Machinery and Building') and decreases another asset (i.e., 'Cash') by \$200,000, thereby ensuring that both the asset and liability sides remain balanced.

## Purchases Raw Material on credit-\$50,000

### Journal Entry:

Debit Raw Materials(Inventory)A/c 50,000  
 Credit Accounts Payable A/c 50,000

### Ledger Accounts:

Raw Material			
Particulars	Amount	Particulars	Amount
Accounts Payable	50,000	Balance c/f	50,000
Total	50,000	Total	50,000

Accounts Payable			
Particulars	Amount	Particulars	Amount
Balance c/f	50,000	Raw Materials	50,000
Total	50,000	Total	50,000

### Trial Balance:

Trial Balance			
Debit	Amount	Credit	Amount
Cash a/c	1,50,000	Capital a/c	5,00,000
Land a/c	1,50,000	Accounts Payable	50,000
Machinery & Building	2,00,000		
Raw Materials	50,000		
Total	5,50,000	Total	5,50,000

### On making payment to the vendor:

Debit Accounts Payable A/c 50,000  
 Credit Cash A/c 50,000

### Income Statement

Particulars	Amount (\$)
Revenue (Sales)	
Less: Cost of Goods Sold	
Gross Profit	
Operating Expenses:	
- Wages	
- Factory Rent	
- Electricity	
Total Expenses	
Net Profit/Loss	

### Balance Sheet

Asset	Amount	Liability	Amount
Cash	1,50,000	Capital	5,00,000
Land	1,50,000	Accounts Payable	50,000
Machinery & Building	2,00,000		
Raw Materials	50,000		
Total	5,50,000	Total	5,50,000

Raw Materials (Inventory) are tangible assets acquired by CLU, with a promise to pay the creditor (classified as a Personal Account).

### Rules:

Real Accounts: Debit what comes in, Credit what goes out.

Personal Accounts: Debit the receiver, Credit the giver.

### Journal Entry:

Debit Raw Materials (Inventory) A/c \$50,000  
 Credit Accounts Payable A/c \$50,000

### Ledger:

Raw Materials (Inventory): Debit balance of \$50,000

Accounts Payable: Credit balance of \$50,000

**Income Statement:** No effect.

**Balance Sheet:** Increases both asset (Raw Materials) and liability (Accounts Payable) by \$50,000.

## Pays Labor wages in cash-\$20,000

### • Ledger Accounts:

Cash A/c			
Particulars	Amount	Particulars	Amount
Capital	5,00,000	Land	1,50,000
		Machinery & Building	2,00,000
		Wages	20,000
		<b>Balance c/f</b>	<b>1,30,000</b>
Total	5,00,000	Total	5,00,000

Wages a/c			
Particulars	Amount	Particulars	Amount
Cash	20,000	<b>Balance c/f</b>	<b>20,000</b>
Total	20,000	Total	20,000

### • Trial Balance:

Trial Balance			
Debit	Amount	Credit	Amount
Cash a/c	1,30,000	Capital a/c	5,00,000
Land a/c	1,50,000	Accounts Payable	50,000
Machinery & Building	2,00,000		
Raw Materials	50,000		
Wages	20,000		
Total	5,50,000	Total	5,50,000

### Journal Entry:

Debit Wages A/c	20,000
Credit Cash A/c	20,000

Income Statement	
Particulars	Amount (\$)
Revenue (Sales)	0
Less: Cost of Goods Sold	
Gross Profit	
Operating Expenses:	
- Wages	20,000
- Factory Rent	
- Electricity	
Total Expenses	20,000
<b>Net Profit/Loss</b>	<b>-20,000</b>

Balance Sheet			
Asset	Amount	Liability	Amount
Cash	1,30,000	Capital	5,00,000
Land	1,50,000	Less: Loss	20,000
Machinery & Building	2,00,000	Accounts Payable	50,000
Raw Materials	50,000		
Total	5,30,000		5,30,000

Payment of wages is an expense for CLU, where cash is paid out. Expenses, losses, incomes, and gains are 'Nominal' accounts that affect profitability and appear in the Income Statement. Cash is a 'Real' account.

### Rules:

Real Accounts: Debit what comes in, credit what goes out.

Nominal Accounts: Debit all expenses and losses, credit all incomes and gains. Thus, Wages Account is debited, and Cash Account is credited.

### Journal Entry:

Debit Wages A/c \$20,000

Credit Cash A/c \$20,000

### Ledger:

Wages Account shows a debit balance of \$20,000.

Cash Account shows a debit balance of \$130,000.

### Trial Balance:

Debit side increases by \$20,000 due to Wages a/c and decreases by \$20,000 due to Cash a/c, balancing both sides.

This transaction impacts the Income Statement as payment of wages reduces profit by \$20,000. It also reduces CLU's liability to Ms. J, reflected in the Balance Sheet as reduced capital.

**Balance Sheet:**

Asset side: Cash decreases by \$20,000.

Liability side: Capital decreases by \$20,000.

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## Classification of Accounts

**Personal Accounts**-The accounts related to individuals, firms, and institutions (e.g., debtors, creditors, banks).



Will reflect in the Balance Sheet as an asset or liability.  
Rule: Debit the Receiver, Credit the Giver

**Real Accounts**- These are tangible and intangible properties



Will reflect in the Balance Sheet as an assets.  
Rule: Debit what comes in, Credit what goes out

**Nominal Accounts**-Include income, gains, expenses, and losses.



Will reflect in the Income Statement  
Rule: Debit all expenses and losses, Credit all incomes and gains

Each transaction involves two components: **a debit and a credit**. The appropriate accounts are determined according to the type of transaction. Accounts are categorized into **Personal, Real, and Nominal**, and the corresponding accounting principles (referred to as **Golden Rules of Accounting**) are used to record journal entries.

## Pays Factory Rent in cash-\$10,000

### • Ledger Accounts:

Cash A/c			
Particulars	Amount	Particulars	Amount
Capital	5,00,000	Land	1,50,000
		Machinery & Building	2,00,000
		Wages	20,000
		Factory Rent	10,000
		<b>Balance c/f</b>	<b>1,20,000</b>
Total	5,00,000	Total	5,00,000

Factory Rent a/c			
Particulars	Amount	Particulars	Amount
Cash	10,000	<b>Balance c/f</b>	<b>10,000</b>
Total	10,000	Total	10,000

### • Trial Balance:

Trial Balance			
Debit	Amount	Credit	Amount
Cash a/c	1,20,000	Capital a/c	5,00,000
Land a/c	1,50,000	Accounts Payable	50,000
Machinery & Building	2,00,000		
Raw Materials	50,000		
Wages	20,000		
Factory Rent	10,000		
Total	5,50,000	Total	5,50,000

### Journal Entry:

Debit Factory Rent A/c	10,000
Credit Cash A/c	10,000

Income Statement	
Particulars	Amount (\$)
Revenue (Sales)	0
Less: Cost of Goods Sold	
Gross Profit	
Operating Expenses:	
- Wages	20,000
- Factory Rent	10,000
- Electricity	
Total Expenses	30,000
<b>Net Profit/Loss</b>	<b>-30,000</b>

Balance Sheet			
Asset	Amount	Liability	Amount
Cash	1,20,000	Capital	5,00,000
Land	1,50,000	Less: Loss	30,000
Machinery & Building	2,00,000	Accounts Payable	50,000
Raw Materials	50,000		
Total	5,20,000	Total	5,20,000

Based on the understanding so far, list the flow of entries for this transaction.

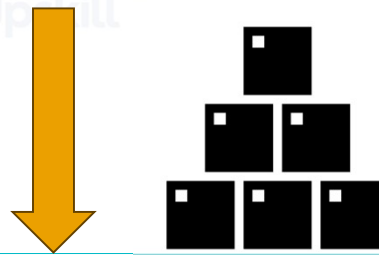
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## Sells Materials for cash (Cost \$30,000, Sold at \$80,000)

- Cash is received
- Sales revenue is recognized



- Cost of Goods Sold increases
- Raw material reduces



In the latest transaction, CLU sold materials for cash amounting to \$80,000. The cost of these materials was \$30,000. This transaction has two components:

1. Sales revenue is recognized with the receipt of \$80,000 in cash.
2. Cost of Goods Sold increases by \$30,000, reducing the inventory balance as these materials are moved out of inventory.

Each component will be examined separately.

## Sells Materials for cash (Cost \$30,000, Sold at \$80,000)

### Ledger Accounts:

Cash A/c			
Particulars	Amount	Particulars	Amount
Capital	5,00,000	Land	1,50,000
Sales	80,000	Machinery & Building	2,00,000
		Wages	20,000
		Factory Rent	10,000
		<b>Balance c/f</b>	<b>2,00,000</b>
<b>Total</b>	<b>5,80,000</b>	<b>Total</b>	<b>5,80,000</b>

Sales a/c			
Particulars	Amount	Particulars	Amount
<b>Balance c/f</b>	<b>80,000</b>	Cash	<b>80,000</b>
<b>Total</b>	<b>80,000</b>	<b>Total</b>	<b>80,000</b>

### Trial Balance:

Trial Balance			
Debit	Amount	Credit	Amount
Cash a/c	2,00,000	Capital a/c	5,00,000
Land a/c	1,50,000	Accounts Payable	50,000
Machinery & Building	2,00,000	Sales a/c	80,000
Raw Materials	50,000		
Wages	20,000		
Factory Rent	10,000		
<b>Total</b>	<b>6,30,000</b>	<b>Total</b>	<b>6,30,000</b>

### Journal Entry:

Debit Cash A/c	80,000
Credit Sales A/c	80,000

### Income Statement

Particulars	Amount (\$)
Revenue (Sales)	80,000
Less: Cost of Goods Sold	
Gross Profit	<b>80,000</b>
Operating Expenses:	
- Wages	20,000
- Factory Rent	10,000
- Electricity	
Total Expenses	<b>30,000</b>
<b>Net Profit/Loss</b>	<b>50,000</b>

### Balance Sheet

Asset	Amount	Liability	Amount
Cash	2,00,000	Capital	5,00,000
Land	1,50,000	Add: Profit	50,000
Machinery & Building	2,00,000	Accounts Payable	50,000
Raw Materials	50,000		
<b>Total</b>	<b>6,00,000</b>		<b>6,00,000</b>

When materials (inventory) are sold for cash:

Cash (real account) is received. There is an income (nominal account) recognized for the amount received on sales.

### Rules:

Real Accounts: Debit what comes in, credit what goes out.

Nominal Accounts: Debit all expenses and losses, and credit all incomes and gains.

Cash is debited and sales revenue is credited.

### Journal Entry:

Debit Cash account	\$80,000
Credit Sales account	\$80,000

### Ledger:

The Sales Account will show a credit balance of \$80,000.

The Cash Account will show a debit balance of \$200,000.

### Trial Balance:

The debit side increases by \$80,000 due to the receipt of cash, and the credit side increases by \$80,000 due to sales revenue, thereby balancing both sides.

### Income Statement:

This transaction impacts the Income Statement since the recording of sales for

\$80,000 increases the profit by \$50,000. Consequently, the amount owed by CLU to Ms. J increases, which is subsequently reflected in the Balance Sheet as an increase in capital.

**Balance Sheet:**

Asset side: The increase in cash raises the asset side by \$80,000.

Liability side: The increase in profit by \$50,000 enhances the liability side by \$50,000 (-30,000 + 80,000).

**Sells Materials for cash (Cost \$30,000, Sold at \$80,000)**

**Ledger Accounts:**

Raw Material			
Particulars	Amount	Particulars	Amount
Cash	50,000	Cost of Goods Sold	30,000
		<b>Balance c/f</b>	<b>20,000</b>
<b>Total</b>	<b>50,000</b>	<b>Total</b>	<b>50,000</b>

Cost of Goods Sold			
Particulars	Amount	Particulars	Amount
Raw Materials	30,000	<b>Balance c/f</b>	<b>30,000</b>
<b>Total</b>	<b>30,000</b>	<b>Total</b>	<b>30,000</b>

**Trial Balance:**

Trial Balance			
Debit	Amount	Credit	Amount
Cash a/c	2,00,000	Capital a/c	5,00,000
Land a/c	1,50,000	Accounts Payable	50,000
Machinery & Building	2,00,000	Sales a/c	80,000
<b>Raw Materials</b>	<b>20,000</b>		
Wages	20,000		
Factory Rent	10,000		
<b>Cost of Goods Sold</b>	<b>30,000</b>		
<b>Total</b>	<b>6,30,000</b>	<b>Total</b>	<b>6,30,000</b>

**Journal Entry:**

Debit Cost of Goods Sold(COGS)	30,000
Credit Raw Materials A/c	30,000

Income Statement	
Particulars	Amount (\$)
Revenue (Sales)	80000
<b>Less: Cost of Goods Sold</b>	<b>30000</b>
Gross Profit	50000
Operating Expenses:	
- Wages	20000
- Factory Rent	10000
- Electricity	
Total Expenses	30000
<b>Net Profit/Loss</b>	<b>20000</b>

Balance Sheet			
Asset	Amount	Liability	Amount
Cash	2,00,000	Capital	5,00,000
Land	1,50,000	<b>Add: Profit</b>	<b>20,000</b>
Machinery & Building	2,00,000	Accounts Payable	50,000
<b>Raw Materials</b>	<b>20,000</b>		
<b>Total</b>	<b>5,70,000</b>	<b>Total</b>	<b>5,70,000</b>

When materials (inventory) are sold, there is a reduction in inventory (real account) because the items are sold from the inventory. This needs to be accounted for. It increases the cost of goods sold (nominal account) and reduces the inventory. Cost of goods sold is an expense.

**Rules:**

Real Accounts: Debit what comes in, credit what goes out.

Nominal Accounts: Debit all expenses and losses, and credit all incomes and gains.

**Journal Entry:**

Debit Cost of Goods Sold (COGS) \$30,000

Credit Raw Materials (Inventory) A/c \$30,000

**In the Ledger:**

The Raw Material Account will show a debit balance of \$20,000.

The Cost of Goods Sold Account will show a credit balance of \$30,000.

**Trial Balance:**

The debit side increases by \$30,000 due to Cost of Goods Sold, and the credit side decreases by \$30,000 due to reduction in inventory, thereby balancing both sides.

**Income Statement:**

This transaction impacts the Income Statement since the recording of cost of goods sold for \$30,000 reduces the profit to \$20,000. Consequently, the amount owed by CLU to Ms. J reduces, which is subsequently reflected in the Balance Sheet as a decrease in capital.

**Balance Sheet:**

Asset side: Decrease in Raw Material by \$30,000.

Liability side: Decrease in profit to \$30,000 reduces the Capital side by \$30,000 (from \$550,000 to \$520,000).

### Income Statement

Particulars	Amount (\$)
Revenue (Sales)	80,000
Less: Cost of Goods Sold	30,000
<b>Gross Profit</b>	<b>50,000</b>
Operating Expenses:	
- Wages	20,000
- Factory Rent	10,000
- Electricity	
Total Expenses	30,000
<b>Net Profit/Loss</b>	<b>20,000</b>

#### PERFORMANCE INDICATORS:

1. Gross Profit Margin= 62.5%.
2. Net Profit Margin= 25%.
3. Operating Expense Ratio= 37.5%.

#### INFERENCE:

- ❖ The business is profitable.
- ❖ Expenses are in control.

### Balance Sheet

Asset	Amount	Liability	Amount
Cash	200,000	Capital 5,00,000 Add: Profit 20,000	5,20,000
Land	150,000		
Machinery & Building	200,000	Accounts Payable	50,000
Raw Materials	20,000		
<b>Total</b>	<b>570,000</b>	<b>Total</b>	<b>570,000</b>

#### INFERENCE:

1. Cash makes up ~35% of total assets → strong liquidity.
2. No long-term debt, and liabilities (₹50,000) are only ~8.8% of total funding.
3. Capital increased from ₹500,000 to ₹520,000 with net profit added → reflects good retention and reinvestment of earnings.

### Income Statement Analysis: Performance indicators

1. Net Profit Margin=  $(20,000/80,000) \times 100 = 25\%$ .
  - The business is profitable with a 25% net profit margin:
2. Gross Profit Margin=  $(50,000/80,000) \times 100 = 62.5\%$ .
  - The business is profitable with a 62.5% gross profit margin:
3. Operating Expense Ratio=  $(30,000/80,000) \times 100 = 37.5\%$ .
  - Expenses are in control.

### Balance Sheet Analysis:

- Cash makes up ~35% of total assets → strong liquidity.
- No long-term debt, and liabilities (₹50,000) are only ~8.8% of total funding.
- Capital increased from ₹500,000 to ₹520,000 with net profit added → reflects good retention and reinvestment of earnings.

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# Financial Accounting & Reporting

## **Accounting**

- Journal Entries
  - The first place where transactions are recorded in chronological order.
  - Every Transaction will have two legs: Debit leg and a Credit leg and each goes into the respective account.
- Ledger Accounts(T accounts)
  - Summary of transactions under each account.
  - Shows the balance in the account at any given point in time.
- Trial Balance
  - A list of all ledger account balances at a given time
  - Enable to check the arithmetic accuracy of ledger posting

## **Reporting**

- Income Statement
- Balance Sheet
- *Statement of Cash Flows*
- *Statement of comprehensive income*
- *Statement of changes in stockholders' equity*

**Income Statement:** Displays a company's financial performance over a specified period (month, quarter, year).

**Balance Sheet:** Presents a company's financial position at a specific point in time.

### **Use of Accounting Information:**

- Accounting information aids decision-making by providing insights into financial performance and resource allocation. It allows managers to formulate strategies and establish financial objectives.
- Monitoring accounting information enables organizations to track financial performance, manage budgets, and control costs, thereby supporting financial stability and growth.
- Communicating accounting information clearly to stakeholders, including investors, creditors, and regulators, promotes trust and transparency. It is crucial for maintaining strong relationships and ensuring compliance.

# Key Accounting Principles

## Accrual Principle

The accrual principle dictates that revenue and expenses should be recognized when they occur, regardless of cash transactions.

## Consistency Principle

The consistency principle requires that companies use the same accounting methods from one period to the next for comparability.

## Matching Principle

The matching principle states that expenses should be matched with the revenues they help to generate in the same period, providing a clear picture of profitability.



Key accounting principles include the accrual principle, consistency principle, and matching principle. These guidelines ensure that financial statements are prepared consistently, providing accurate and comparable information.

## Accrual Principle:

Revenue and expenses are recorded when they are earned or incurred, not when cash is received or paid. Example: A company delivers services in December but receives payment in January. Under the accrual principle, the revenue is recorded in December (when earned), not January (when paid).

## Consistency Principle:

Once a company chooses an accounting method, it must use it consistently from one period to another. Example: A company uses the straight-line method to depreciate assets. It must continue using the same method every year unless a justified change is disclosed. If it suddenly switches to double-declining balance without explanation, it violates the consistency principle.

## Matching Principle:

Expenses should be recognized in the same period as the revenues they help to

generate. Example: A company pays sales commissions in January for sales made in December. The commissions should be recorded as December expenses, because they relate to December's sales.

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# Thank You!



We covered the following topics:

- Classification of Accounts
- Golden Rules of Accounting
- Accounting: Journal Entry, Ledger Accounts, Trial Balance
- Reporting: Income Statement & Balance Sheet

Understanding accounting becomes significantly easier when each transaction is followed from journal entry (JE) through to trial balance, and finally into the income statement and balance sheet. I strongly encourage practicing this end-to-end flow, as it is the most effective method for comprehending financial reporting.

I hope you found this session beneficial. Thank you.