

Basic Knowledge of Accounting

1.1 The Definition of Accounting

Accounting is an information system that classifies, records, measures, summarizes, interprets and reports the economic activities of a business with monetary unit as its main criterion. Under this definition three important points call for our attention: ① accounting involves such activities as classifying, recording, measuring, summarizing, interpreting, reporting and describing; ② the object of accounting is economic activities of business; ③ monetary unit is the criterion.

One of the most important functions of accounting is to accumulate and report financial information that shows an organization's financial position and the results of its operations to its interested users, which include managers, stockholders, banks and other creditors, governmental agencies, investment advisors, and the general public.

Another important function of accounting is to provide the management inside an organization with the accounting information needed in the organization's internal decision making, which relates to planning, control, and evaluation within an organization.

The growth of organizations, changes in technology, government regulations, and the globalization of economy during the twentieth century have spurred the development of accounting. As a result, a number of specialized fields of accounting have evolved in addition to financial accounting and management accounting, which include auditing, cost accounting, tax accounting, budgetary accounting, governmental and nonprofit accounting, human resources accounting, environmental accounting, social accounting, international accounting, etc. All forms of accounting, in the end, provide information to the relevant users and help them make decisions.



1.2 Accounting Elements

Financial accounting information is classified into the categories of assets, liabilities, owner's equity, revenue, expense and profit. The above accounting information is also called accounting elements, which form the basic structure of financial statements. A good understanding of these accounting elements will be a good basis and start in learning financial accounting.

1.2.1 Assets

Assets are economic resources that are owned and controlled by a business. Assets can be classified as current assets, fixed assets, or intangible assets. Current assets are short-term assets including cash, bank deposit, accounts receivable, inventory, etc. They can be converted to cash within one year. Current assets are generally listed according to liquidity, so cash is always listed first. Fixed assets are long-term assets, including land, buildings, equipment, furniture, etc. They are used in business operations, not for direct sale. Intangible assets are also long-term assets, including patents, copyrights, licenses, franchises, goodwill, etc. They are also used in the business operation but they have no physical form. In most cases, they provide their owners with competitive advantages over other firms.

1.2.2 Liabilities

Liabilities are debts of a business owed to suppliers, banks, etc. Liabilities are usually classified as current liabilities and long-term liabilities. Current liabilities are expected to be paid within one year, which include accounts payable, tax payable, salaries payable, etc. A typical current liability would usually be paid within 30 days. Long-term liabilities may last from one year to 20 or 30 years until it is fully paid. Mortgage payable is an example of long-term liabilities.

1.2.3 Owner's Equity

Owner's equity refers to the interest or the claim of the investors remaining in the net assets of an enterprise. When a business is owned by one person, the owner's equity is shown as "capital"; when it is owned by stockholders, it is shown as "Stockholder's equity". Owner's equity is affected by the results of a company's operations. If a business is profitable, owner's equity is increased; if a business is not profitable, owner's equity is decreased.

1.2.4 Revenue

Revenue is the increase in owner's equity resulting from the sales of goods or services

by the business. Manufacturing and merchandising business receive revenues from the sale of products or merchandise. A service enterprise such as a law firm gets revenue from the fees it charges for the services it provides. Please note that a cash receipt qualifies as revenue only when it helps increase owner's equity. Thus, cash borrowed from a bank is not a revenue but simply liability.

1.2.5 Expense

Expenses are the decrease in owner's equity caused by the company's revenue-producing operation. Like revenues, expenses represent flows of resources during a period of time, but expenses are outflows whereas revenue is inflows. In amount, the expense is equal to the value of goods or services used up in gaining revenue. Please note that a cash payment can be regarded as an expense only if it decreases owner's equity. Thus, purchasing supplies, which is an exchange of one asset for another asset, is not an expense. Worth also bearing in mind is that dividend payments and drawing are not expenses since they are not related to revenue-producing operations of a business.

1.2.6 Profit

Profit, often called net income, is also the increase in owner's equity resulting from profitable operation of a business. If revenues exceed expenses, the result is called net income or profit; if expenses exceed revenues, the difference is called net loss. Revenue is a "gross" concept, whereas profit is a "net" concept.

The last three accounting elements, i.e. revenue, expense and profit are temporary accounts because they are opened at beginning of an accounting period, and closed at the end of the period. In the accounting equation, they belong to owner's equity.



1.3 Accounting Equation

The accounting equation shows the basic relationship between the accounting elements, i.e. the balance position of assets on one side whereas liabilities and owner's equity on the other side. So the basic accounting equation is:

$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$$

This equation tells us that assets of an entity must equal to the total of its liabilities and owner's equity. This equation explains who supply the assets of the entity. Suppose a business, Scarlett's Bar, owns assets of \$31,755 and liabilities of \$7,500. According to the accounting equation, the owner's equity must be \$24,255 ($\$31,755 = \$7,500 + \$24,255$).

Since the accounting equation is in equality, it can be presented in another way:

$$\text{Owner's Equity} = \text{Assets} - \text{Liabilities}$$

At this point, we bring revenues and expenses into the equation, which is called expanded accounting equation. Since the revenues help increase equity and expenses decrease equity, the accounting equation may be expanded to include revenues and expenses as shown below:

$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity} + \text{Revenues} - \text{Expenses}$$

On the basis of the accounting equation, the financial position and the operating result of a business can be recorded to the interested users of accounting information.



1.4 Recording Transactions in the Accounting Equation

Any business event that alters the amount of assets, liabilities or owner's equity or that affects the accounting equation is called a transaction. To record transactions using the accounting equation, we assume that during the month of January, 2007, Scarlett's Bar had the following transactions:

January 4—Scarlett started her business and deposited \$14,000 into a bank account opened specially for her business Scarlett's Bar.

January 6—Bought equipment like refrigerators, tables and chairs, etc. for \$8,500.

January 7—Bought supplies such as tableware for \$2,000.

January 8—Bought beverages etc. for \$7,500 on account.

January 20—Borrowed \$5,000 from the bank for a duration of 3 months.

January 21—Paid \$5,000 owed on inventory.

January 28—Paid electricity and water bills for the month \$245.

January 31—Total monthly cash sales \$15,000.

January 31—Paid chefs salary for the month \$4,500.

Now let's see how the accountant makes a meaningful record of the series of transactions, reconciling step by step with the accounting equation.

January 4—Scarlett started her business and deposited \$14,000 into a bank account.

There are two accounts that are affected: the assets Cash is increased, and the Capital of the firm is increased by the same amount (Capital C is used in "Cash" and "Capital" to mean the titles of accounts).

	Assets	=	Liabilities + Owner's Equity
	Cash	=	Scarlett, Capital
4	+\$14,000	=	+\$14,000

January 6—Bought equipment like refrigerators, tables and chairs, etc. for \$8,500.

Here Scarlett is substituting one asset (cash) for another asset (equipment). She is

receiving (+) the asset Equipment and paying out (-) the asset Cash. Note that the capital of \$14,000 remains unchanged.

	Assets	=	Liabilities	+	Owner's Equity
	Cash + Equipment	=			Scarlett, Capital
	\$14,000				\$14,000
6	<u>-\$8,500 + \$8,500</u>				
	\$5,500 \$8,500				\$14,000

January 7—Bought supplies such as tableware for \$2,000.

In this case Scarlett again substitutes one asset Cash for another asset Supplies (Tableware is current assets which is grouped under the title Suppliers). She receives Supplies (+) and pays out Cash (-).

	Assets	=	Liabilities	+	Owner's Equity
	Cash+ Supplies + Equipment	=			Scarlett, Capital
	\$5,500 \$8,500				\$14,000
7	<u>-\$2,000 + \$2,000</u>				
	\$3,500 + \$2,000 \$8,500				\$14,000

January 8—Bought beverage etc. for \$7,500 on account.

In this transaction, both sides of the accounting equation are affected: increase on the left side Assets (+) and increase on the right side Liabilities (+) by the same amount. So the accounting equation is still in balance. For Scarlett's Bar such goods beverages, pastry, refreshment, etc. are grouped under the title Inventories. She therefore is receiving the asset Inventories but is not paying for it with the asset Cash. Instead, she will owe the money. Thus she creates the liability Accounts Payable because she owes that much.

	Assets = Liabilities + Owner's Equity					
	Cash + Supplies + Inventories + Equipment = Accounts Payable + Scarlett, Capital					
	\$3,500	\$2,000	\$8,500	\$14,000		
8	<u>+\$7,500 + \$7,500</u>					
	\$3,500	\$2,000	\$7,500	\$8,500	\$7,500	\$14,000

January 20—Borrowed \$5,000 from the bank for a duration of 3 months.

Like creating Accounts Payable to purchase an asset, both sides of the accounting equation increase by the same amount, but the balancing condition is not impaired. In this case Scarlett is receiving Cash (+) and creating a current liability—Short-term Borrowings (+).

	Assets = Liabilities + Owner's Equity					
	Cash + Supplies + Inventories + Equipment = Short - term Borrowings + Accounts					

Payable + Scarlett, Capital

	\$3,500	\$2,000	\$7,500	\$8,500		\$7,500	+\$14,000
20	+ \$5,000 + \$5,000						
	\$8,500	\$2,000	\$7,500	\$8,500	\$5,000	\$7,500	\$14,000

January 21—Paid \$5,000 owed on inventory.

This transaction reduces Scarlett's asset Cash since she is paying out money by \$5,000(—). She also reduces her liability Accounts Payable, by \$5,000(—). Now she owes that much less.

Assets = Liabilities + Owner's Equity

Cash + Supplies + Inventories + Equipment = Short - term Borrowings + Accounts Payable + Scarlett, Capital

	\$8,500	\$2,000	\$7,500	\$8,500	\$5,000	\$7,500	\$14,000
21	-\$5,000 -\$5,000						
	\$3,500	\$2,000	\$7,500	\$8,500	\$5,000	\$2,500	\$14,000

January 28—Paid electricity and water bills for the month \$245.

Electricity and water bills constitute Utilities Expense. This transaction means a deduction from Cash. Incurrence of expense means a deduction of Capital.

Assets = Liabilities + Owner's Equity

Cash + Supplies + Inventories + Equipment = Short - term Borrowings + Accounts Payable + Scarlett, Capital

	\$3,500	\$2,000	\$7,500	\$8,500	\$5,000	\$2,500	\$14,000
28	-\$245 \$245 Utilities Ex.						
	\$3,255	\$2,000	\$7,500	\$8,500	\$5,000	\$2,500	\$13,755

January 31—Total monthly cash sales \$15,000.

In this transaction Scarlett is receiving cash. So Cash is increased (+), and her Capital is also increased by the same amount (+). It is important to note that she labels Sales Revenue under Capital to indicate revenue received from major operation of her business.

Assets = Liabilities + Owner's Equity

Cash + Supplies + Inventories + Equipment = Short - term Borrowings + Accounts Payable + Scarlett, Capital

	\$3,255	\$2,000	\$7,500	\$8,500	\$5,000	\$2,500	\$13,755
31	+\$15,000 + \$15,000 Sales Revenue						
	\$18,255	\$2,000	\$7,500	\$8,500	\$5,000	\$2,500	\$28,755

January 31—Paid chefs salary for the month \$4,500.

In this transaction, another expense, Salary Expense, is created. Also, both Cash and Capital are reduced by \$4,500(—).

$$\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$$

Cash + Supplies + Inventories + Equipment = Short - term Borrowings + Accounts Payable + Scarlett, Capital

	\$18,255	\$2,000	\$7,500	\$8,500	\$5,000	\$2,500	\$28,755
31	<u>-\$4,500</u>	<u>-\$4,500</u>					
	\$13,755	\$2,000	\$7,500	\$8,500	\$5,000	\$2,500	\$24,255

At this point, the figures of the basic accounting equation are:

$$\begin{aligned} \text{Assets} &= \text{Liabilities} + \text{Owner's Equity} \\ \$31,755 &= \$7,500 + \$24,255 \end{aligned}$$



1.5 Double-entry System

Each transaction must affect two or more accounts to keep the basic accounting equation in balance. In other words, for each transaction, debits must equal credits in the accounts. The equality of debits and credits is the basis for the double-entry system of recording transactions. Under the double-entry system, the dual (two-side) effect of each transaction is recorded in appropriate accounts respectively. If every transaction is recorded with equal debits and credits, then the sum of all the debits to the accounts must equal the sum of all the credits.

In double-entry system, whether an account is to be debited or credited depends on the type of the accounting element. By convention, increases in assets and expenses are recorded as debits, whereas increases in liability, owner's equity, revenue and profit are recorded as credits. Asset and expense decreases are recorded as credits, whereas liability, owner's equity and profit decreases are recorded as debits.

Just keep in mind that in double-entry system there are equal debit and credit entries for every transaction. When only two accounts are affected, the debit and credit amounts must equal the total of the credit entries; when more than two accounts are affected, the total amount debited credit entries must equal the total amount credited.



1.6 Divisions of Accounting Profession

The field of accountants' work is divided into three broad areas: public accounting, accounting for private businesses, and accounting for governments and non-profit organization.

1.6.1 Public Accounting

Public accountants who are similar to doctors or lawyers can offer their accounting

services to the public on a fee basis. Public accounting firms are organizations in which public accountants mainly work. Most people in the public accounting firms are licensed as certified public accountants (CPAs). Thus, public accounting firms are often called CPA firms.

The primary services offered by CPA firms include auditing, income tax services, and management advisory services.

1.6.2 Accounting for Private Businesses

The accountants in a private business, large or small, must record transactions and prepare periodic financial statements from accounting records. The chief accounting officer in a medium-sized or large business is usually called the controller, who manages the work of the accounting staff. As a part of the top management team, the controller is charged with the task of running the business, setting its objectives, and seeing that the objectives are met.

The work of the accountants in a private business mainly includes design of the accounting system, cost accounting, internal control, internal auditing, etc.

1.6.3 Accounting for Governments and Non-profit Organizations

Many accountants work in government offices or for non-profit organizations. These two areas are often joined together under the term governmental accounting and non-profit accounting.

Most enterprises face government regulations. Government officials rely on information to help them direct the affairs of their agencies just as do the executives of corporations. For example, in the U.S., there are the Securities and Exchange Commission (SEC) and the Internal Revenue Service (IRS) to perform extensive accounting work.

Many governmental accounting problems are similar to those applicable to private business. In other respects, however, accounting for governmental affairs requires a somewhat different approach because the objective of earning a profit is absent from public affairs. Non-profit organizations include universities, hospitals, churches, and charitable organizations. Non-profit accounting follows a pattern of accounting that is similar to governmental accounting.



1.7 Ethics of the Accounting Profession

One characteristic frequently associated with any profession is that those practicing the profession acknowledge the importance of an ethical code. This is especially important in the accounting profession because so much of an accountant's work involves providing information to support the informed judgments and decisions made by users of accounting

information.

Both codes of conduct identify integrity and objectivity as two key elements of ethical behavior for a professional accountant. Having integrity means being honest and forthright in dealings and communications with others; objectivity means impartiality and freedom from conflict of interest. An accountant who lacks integrity and/or objectivity cannot be relied on to produce complete and relevant information with which to make an informed judgment or decision.

Other elements of ethical behavior include independence, competence, and acceptance of an obligation to serve the best interest of the employer, the client, and the public. Independence is related to objectivity and is especially important to the auditor, who must be independent both in appearance and in fact. Having competence means having the knowledge and professional skills to adequately perform the work assigned. Accountants should recognize that the nature of their work requires an understanding of the obligation to serve those who will use the information communicated by them.



Useful Words and Expressions

- | | |
|---|-------------------------------------|
| 1. classify
v. 分类; 分等 | 10. audit
v. & n. 审计 |
| 2. measure
v. 估量, 判定; 测量, 度量 | 11. budgetary
adj. 预算的 |
| 3. interpret
v. 解释, 说明, 口译 | 12. element
n. 要素 |
| 4. monetary
adj. 货币的; 财政的 | 13. asset
n. 资产; 优点 |
| 5. criterion
n. (批评判断的)标准; 准则; 规范;
准据 | 14. liability
n. 责任; 债务; 倾向 |
| 6. creditor
n. 债权人 | 15. revenue
n. 税收; 收益 |
| 7. investment
n. 投资; 投入 | 16. inventory
n. 存货 |
| 8. evaluation
n. 评价; 评估; 估价 | 17. liquidity
n. 流动性; 流动资产; 偿债能力 |
| 9. regulation
n. 管理; 规则 | 18. patent
n. 专利权 |
| | 19. copyright |

- | | | | |
|-----|------------------------------------|--|--|
| | <i>n.</i> 版权, 著作权 | | 财务状况 |
| 20. | license | | 34. financial accounting |
| | <i>n.</i> 执照, 许可证 | | 财务会计 |
| 21. | franchise | | 35. owner's equity |
| | <i>n.</i> 经销权 | | 所有者权益 |
| 22. | goodwill | | 36. management accounting |
| | <i>n.</i> 商誉 | | 管理会计 |
| 23. | mortgage | | 37. financial statement |
| | <i>vt.</i> 抵押 <i>n.</i> 抵押 | | 财务报表 |
| 24. | debit | | 38. current assets |
| | <i>vt.</i> 记入借方, 登入借方 <i>n.</i> 借方 | | 流动资产 |
| 25. | credit | | 39. intangible assets |
| | <i>vt.</i> 记入贷方, 登入贷方 <i>n.</i> 贷方 | | 无形资产 |
| 26. | ethics | | 40. accounts receivable |
| | <i>n.</i> 伦理学; 伦理观; 道德标准 | | 应收账款 |
| 27. | integrity | | 41. accounts payable |
| | <i>n.</i> 正直; 诚实; 廉正 | | 应付账款 |
| 28. | objectivity | | 42. accounting equation |
| | <i>n.</i> 客观; 客观性 | | 会计等式 |
| 29. | impartiality | | 43. double-entry system |
| | <i>n.</i> 公正, 公平 | | 复式记账法 |
| 30. | competence | | 44. certified public accountant (CPA) |
| | <i>n.</i> 能力, 胜任; 权限 | | 注册会计师 |
| 31. | obligation | | 45. the Securities and Exchange |
| | <i>n.</i> 义务; 职责; 债务 | | Commission (SEC) |
| 32. | information system | | (美) 证券交易委员会 |
| | 信息系统 | | 46. the Internal Revenue Service (IRS) |
| 33. | financial position | | (美) 国内收入署 |

Notes

1. Accounting is an information system that classifies, records, measures, summarizes, interprets and reports the economic activities of a business with monetary unit as its main criterion.

会计是一个信息系统, 是对一家企业的经济活动进行分类、记录、衡量、总结、解读和汇报, 通常以货币单位作为主要的标准。

2. As a result, a number of specialized fields of accounting have evolved in addition to financial accounting and management accounting, which include auditing, cost accounting, tax accounting, budgetary accounting, governmental and nonprofit accounting, human resources accounting, environmental accounting, social accounting, international accounting, etc.

因此，除了财务会计和管理会计之外，还演变出许多会计专业领域，包括审计、成本会计、税务会计、预算会计、政府与非营利组织会计、人力资源会计、环境会计、社会会计、国际会计等。

3. The accounting equation shows the basic relationship between the accounting elements, i.e. the balance position of assets on one side whereas liabilities and owner's equity on the other side.

会计等式表现会计要素的基本关系，即资产在等式的一端，而负债和所有者权益在等式的另一端，两者形成一种平衡关系。

4. Double-entry system

复式记账法。由意大利数学家卢卡·帕乔利（Luca Pacioli）于1494年首次提出，现在已经成为绝大多数国家会计记账的基本方法。复式记账法的基本规则是：每一项经济业务都具有双重影响，因此要在两个或两个以上的账户中记录和反映。

5. By convention, increases in assets and expenses are recorded as debits, whereas increases in liability, owner's equity, revenue and profit are recorded as credits.

按照惯例，资产和费用的增加作为借方被登记，而负债、所有者权益、收入和利润的增加作为贷方登记。

6. Certified Public Accountant (CPA)

注册会计师。他们是有资格执行审计业务的专业人员，一般需满足三个方面的条件才能获得这种资格：①接受过专业教育，通常要有本科学历，有的国家甚至要求更高的学历；②具有一定期限的会计或审计工作经验；③通过由专业会计团体举办的统一考试。注册会计师在英国及英联邦国家称为CA，即Chartered Accountant。

7. Both codes of conduct identify integrity and objectivity as two key elements of ethical behavior for a professional accountant.

在道德规范中，诚信和客观是职业会计师职业道德行为的两大要素。

8. Other elements of ethical behavior include independence, competence, and acceptance of an obligation to serve the best interest of the employer, the client, and the public.

职业道德行为的其他要素包括独立性、胜任能力及承担尽可能满足雇主、客户和公众利益的义务。



Exercises

I. Multiple choice.

1. Which of the following best describes accounting? ()
 - A. It records economic data but does not communicate the data to users according to any specific rules.
 - B. It is an information system that provides reports to stakeholders.
 - C. It is of no use by individuals outside of the business.
 - D. It is used only for filling out tax returns and for financial statements for various types of governmental reporting requirements.
2. Profit is the difference between _____. ()
 - A. assets and liabilities
 - B. the incoming cash and outgoing cash
 - C. the assets purchased with cash contributed by the owner and the cash spent to operate the business
 - D. the assets received for goods and services and the amounts used to provide the goods and services
3. The two most common specialized fields of accounting in practice are _____. ()
 - A. forensic accounting and financial accounting
 - B. managerial accounting and financial accounting
 - C. managerial accounting and environmental accounting
 - D. financial accounting and tax accounting
4. Public accountants are normally _____. ()
 - A. Certified Public Accountants
 - B. Forensic Accountants
 - C. Certified Internal Auditors
 - D. Certified Management Accountants
5. Which of the following is the best description of accounting's role in business? ()
 - A. Accounting provides stockholders with information regarding the market value of the company's stocks.
 - B. Accounting provides information to managers to operate the business and to other stockholders to make decisions regarding the economic condition of the company.
 - C. Accounting provides creditors and banks with information regarding the credit risk rating of the company.
 - D. Accounting is not responsible for providing any form of information to stockholders. That is the role of the information systems department.
6. Which of the following is not a role of accounting in business? ()

- A. To provide reports to stakeholders about the economic activities and conditions of the business.
- B. To personally guarantee loans of the business.
- C. To provide information to managers to use in operating the business.
- D. To provide information to other stakeholders to use in assessing the economic performance and condition of the business.
7. Owned resources of a business are referred to as _____. ()
- A. assets B. liabilities C. equities D. revenues
8. The accounting equation may be expressed as _____. ()
- A. Assets = Equities – Liabilities
- B. Assets + Liabilities = Owner’s equity
- C. Assets = Revenues – Liabilities
- D. Assets – Liabilities = Owner’s equity
9. The assets and liabilities of the company are \$ 155,000 and \$60,000 respectively. Owner’s equity should equal to _____. ()
- A. \$215,000 B. \$155,000 C. \$60,000 D. \$95,000
10. If total liabilities decreased by \$25,000 during a period of time and owner’s equity increased by \$30,000 during the same period, the amount and direction (increase or decrease) of the period’s change in total assets is _____. ()
- A. \$65,000 increase B. \$5,000 decrease
- C. \$5,000 increase D. \$65,000 decrease
11. Which of the following is not a true statement about the accounting equation and its element? ()
- A. The accounting equation is Assets = Liabilities – Owners’ Equity.
- B. Assets are the resources a business possesses.
- C. Liabilities represent debts of a business.
- D. Examples of assets are cash, land, buildings and equipment.
- E. Owners’ equity are the rights of the owners.
12. A business paid \$ 9,000 to a creditor in payment of an amount owed. The effect of the transaction on the accounting equation was to _____. ()
- A. increase one asset, decrease another asset
- B. increase an asset, decrease a liability
- C. decrease an asset, decrease a liability
- D. increase an asset, increase owner’s equity
13. A debit may signify _____. ()

- A. an increase in an asset account
 - B. a decrease in an asset account
 - C. an increase in a liability account
 - D. an increase in the capital stock account
14. The receipt of cash from customers in payment of their accounts would be recorded by a _____. ()
- A. debit to cash, credit to accounts receivable
 - B. debit to accounts receivable, credit to cash
 - C. debit to cash, credit to accounts payable
 - D. debit to accounts payable, credit to cash
15. As of December 31, 2017, Stoneland Corporation has assets of \$3,500 and stockholders' equity of \$2,000. What are the liabilities for Stoneland Corporation as of December 31, 2017? ()
- A. \$1,500 B. \$1,000 C. \$2,500 D. \$2,000
16. The effect on the basic accounting equation of performing services for cash are to _____. ()
- A. increase assets and decrease stockholders' equity
 - B. increase assets and increase stockholders' equity
 - C. increase assets and increase liabilities
 - D. increase liabilities and increase stockholders' equity
17. Which of the following accounts is an owner's equity account? ()
- A. Cash
 - B. Accounts Payable
 - C. Prepaid Insurance
 - D. Julia Davis, Capital
18. The gross increase in owner's equity attributable to business activities are called _____. ()
- A. assets B. liabilities C. revenues D. net income
19. The debit side of an account _____.
- A. depends on whether the account is an asset, liability or owner's equity
 - B. can be either side of the account depending on how the accountant set up the system
 - C. is the right side of the account
 - D. is the left side of the account
20. Which of the following describes the classification and normal balance of the fees earned account? _____
- A. Asset, credit
 - B. Liability, credit

C. Owner's equity

D. Revenue, credit

II. Translate the following into Chinese.

1. Financial accounting is primarily concerned with the recording and reporting of economic data and activities for a business. Although such reports provide useful information for managers, they are the primary reports for owners, creditors, governmental agencies and the public.

Managerial accounting uses both financial accounting and estimated data to aid management in running day-to-day operations and in planning future operations. Management accountants gather and report information that is relevant and timely to the decision-making needs of management.

2. The sum of the debits is always equal to the sum of the credits for each journal entry. This equality of debits and credits for each transaction is built into the accounting equation: $\text{Assets} = \text{Liabilities} + \text{Owner's Equity}$. Because of this double equality, this system of recording transactions is called the double entry accounting system.

III. Finish the following tasks.

1. Select accounts from the ledger of Hughes Company appear below. For each account, indicate the following:

(1) In the first column at the right, indicate the nature of each account, using the following abbreviations.

Asset—A Revenue—R Liability—L Expense—E None of the above—N

(2) In the second column, indicate the increase side of each account by inserting Dr. or Cr.

Account	(1) Type of Account	(2) Increase Side
Supplies		
Notes Receivable		
Fees Earned		
Philips, Drawing		
Accounts Payable		
Salaries Expense		
Hughes, Capital		
Accounts Receivable		
Equipment		
Notes Payable		

2. Analyze the following transactions as to their effect on the accounting equation.

- (1) The company paid \$225 to a vendor for supplies purchased previously on account.
- (2) The company performed \$1,050 of services and billed the customer.
- (3) The company received a utility billed for \$ 195 and will pay it next month.

(4) The owner of the company withdrew \$ 50 of supplies for personal use.

(5) The company paid \$ 305 in salaries to its employees.

(6) The company collected \$ 725 of cash from its customers on account.

Some of the possible effects of a transaction on the accounting equation are listed below:

- ① Assets, Dr. ; Assets, Cr.
- ② Assets, Dr.; Owner's Equity, Cr.
- ③ Assets, Dr.; Liability, Cr.
- ④ Assets, Dr.; Revenue, Cr.
- ⑤ Liability, Dr.; Assets, Cr.
- ⑥ Drawing, Dr.; Assets, Cr.
- ⑦ Expense, Dr.; Assets, Cr.
- ⑧ Expense, Dr.; Liability, Cr.

Put the appropriate letter next to each transaction.