Should we recognize the asset?

Assets arise from transactions and events

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- A well-known scientist is hired to manage the R&D function for 480K a year. Employment starts next month.
- The firm receives an order for $15K in products.
- The firm writes a check for $1M to obtain an option to purchase a tract of land.
- A firm receives notice from a supplier that it has shipped raw materials of $200K. The firm has title to the goods while in transit.
- The firm purchases a patent from its creator for $1.2M

Should we recognize the liability?

Liabilities arise from transactions and events

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- The firm owes its attorneys $50K in legal expenses.
- The firm provides warranties on its products.
- The firm borrows $60K from the bank for a 90-day period.

Emily's Bakery

(1) Emily contributes $10,000 in cash

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- Assets = Liabilities + Owners' Equity
- Cash Contributed Capital
- +$10,000 +$10,000

Transactions and the Accounting Equation

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Cash +	A/R +	Equip. =	L/P +	C. Cap.+	R/E
+10,000				+10,000	
+ 3,000			+ 3,000		
- 5,000		+ 5,000			
+ 8,000	+ 4,000				+12,000
- 9,000					- 9,000

Summary

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- Balance sheet
  - Listing of
    - Resources owned by a firm (assets or investments)
    - Financing of the assets through obligations to external parties (liabilities)
    - Financing of the investments through residual claimants (shareholders' equity)
  - Preparing a balance sheet (and other financial statements) using transaction history

Initial Balance Sheet

Starting a Company

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- (5) Returns defective raw materials purchased in (4) and costing $900 to the supplier. The account has not yet been paid.
- (6) Pays the supplier in (4) and (5) the amount due, less a 2-percent discount for prompt payment. The firm treats cash discount as a reduction in the acquisition cost of raw materials.
- (7) Obtains a fire insurance policy providing $500,000 coverage beginning next month. It pays the 1-year premium of $4,950.

Initial Balance Sheet

Starting a Company

- (8) Issues a check for $1,800 for 3 months rent in advance for office space.
- (9) Purchases a patent on a machine process for $90,000 cash.
- (10) Purchases office equipment for $2,700, making a down payment of $250 and agreeing to pay the balance in 30 days.
- (11) Pays $825 to Express Trucking Company for delivering the equipment purchased in (3).

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