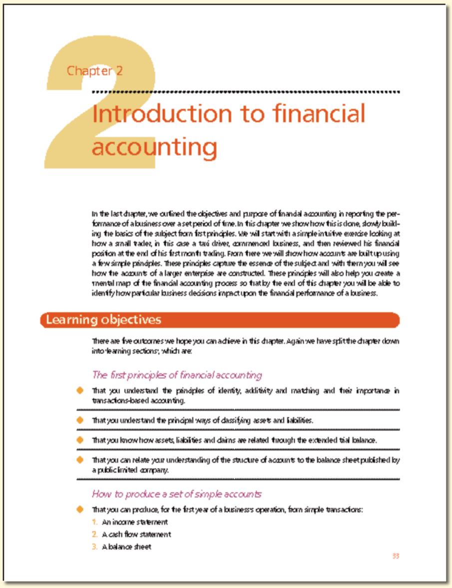
Walk-through tour


Chapter 2

Introduction to financial accounting

In the last chapter, we outlined the objectives and purpose of financial accounting in reporting the performance of a business over a set period of time. In this chapter we show how this is done, slowly building the basis of the subject from first principles. We will start with a simple intuitive exercise looking at how a small trader, in this case a taxi driver, commenced business, and then reviewed his financial position at the end of his first month trading. From there we will show how accounts are built up using a few simple principles. These principles capture the essence of the subject and with them you will see how the accounts of a larger enterprise are constructed. These principles will also help you create a mental map of the financial accounting process so that by the end of this chapter you will be able to identify how particular business decisions impact upon the financial performance of a business.

Learning objectives

There are five outcomes we hope you can achieve in this chapter. Again we have split the chapter down into learning sections, which are:

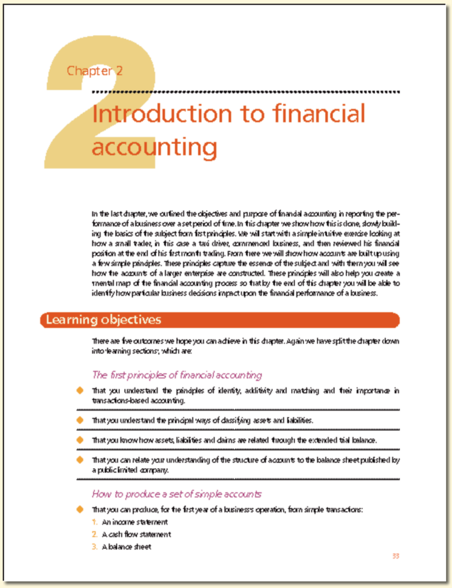
The first principles of financial accounting

- That you understand the principles of identity, additivity and matching and their importance in transactions-based accounting.
- That you understand the principal ways of classifying assets and liabilities.
- That you know how assets, liabilities and claims are related through the extended trial balance.
- That you can relate your understanding of the structure of accounts to the balance sheet published by a public limited company.

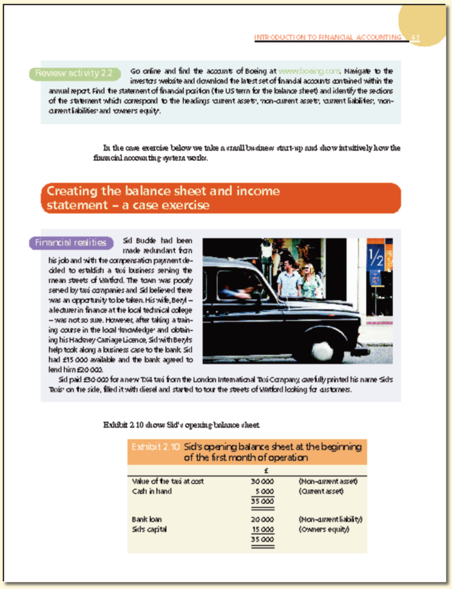
How to produce a set of simple accounts

- That you can produce, for the first year of a business's operation, from simple transactions:
  1. An income statement
  2. A cash flow statement
  3. A balance sheet

Introduction Brief overview of chapter with contextual comments linking to previous learning and concepts.



Learning objectives These are divided into sections and highlight the expected learning outcomes from each chapter. Success against these learning outcomes is assessed as the chapter proceeds.

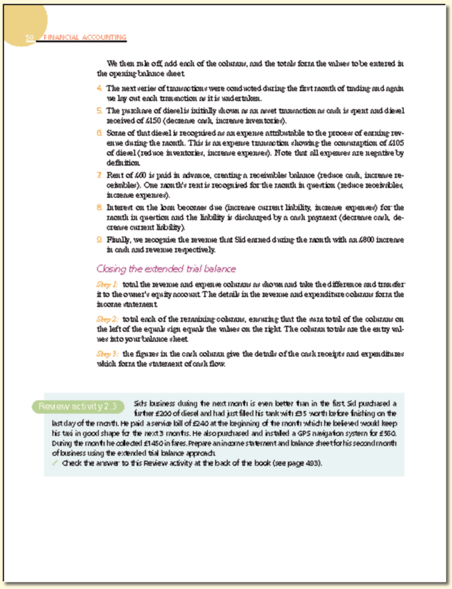

INTRODUCTION TO FINANCIAL ACCOUNTING

Creating the balance sheet and income statement – a case exercise

Exhibit 2.10 Sid's opening balance sheet at the beginning of the first month of operation

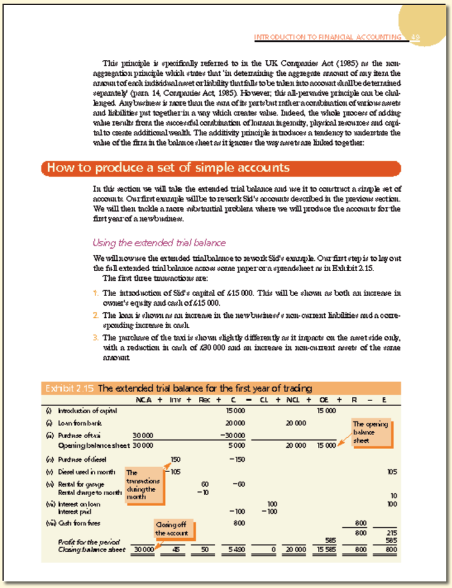
	£	
Value of the taxi at cost	30 000	(Non-current asset)
Cash in hand	5 000	(Current asset)
	35 000	
Bank loan	20 000	(Non-current liability)
Sid's capital	15 000	(Owners equity)
	35 000	

Financial realities These problems are fully explored in the text and provide a key component of the learning process.

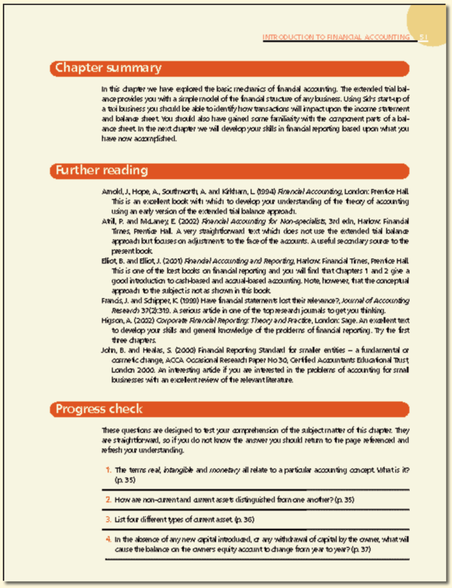

FINANCIAL ACCOUNTING

Closing the extended trial balance

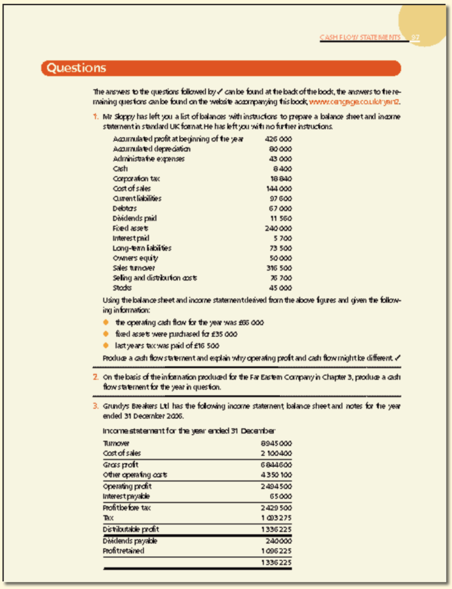
Review activities These short questions allow you to explore the learning you have just undertaken. They also include challenging issues which you may wish to use as the basis of discussion or further reading.



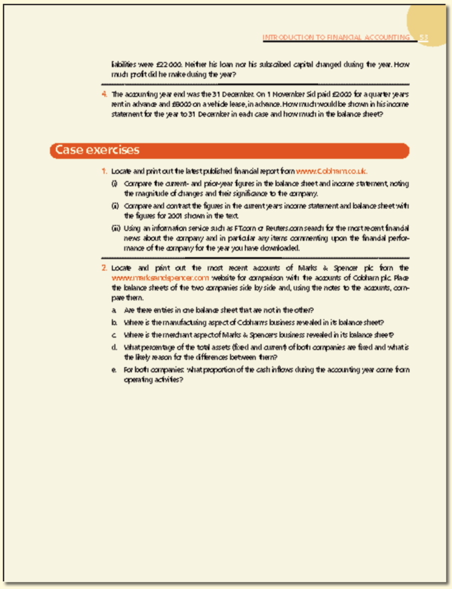
Exhibits These give a visual representation of key concepts or data. Look for 'Post-its' to guide you through the more complex analysis on spreadsheet exhibits.



Progress check At the end of each chapter there are a dozen or more brief questions which are designed to test your knowledge of the content of the chapter. These are very useful for bringing the subject together and preparing you to undertake the more substantial questions that follow.



Questions The questions are designed to test your achievement of the learning objectives specified at the beginning of each chapter. Each question should take between 30 and 45 minutes to complete.



Case exercises These are much more substantial pieces of work which will allow you to explore, using current materials and data, the methods and concepts in the text.