

Improving Your Small Business Skills

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Information to Increase both the Wealth and Lifestyle of Your Family

How To Improve Your Understanding of the Balance Sheet

For many businesses, this financial area is probably the least understood, but one of the most important to fully comprehend.

While the profit-and-loss statement shows the business's yearly trading results, the balance sheet shows the financial strengths and weaknesses of the business on a particular day, normally June 30th.

Terms Explained:

Assets: Are what you own and use to run and produce your business' income.

Current Assets: Are in cash form or are likely to be converted to cash within 12 months.

Non-Current Assets: Not likely to be converted to cash form within 12 months and are to be used in the business operations for more than 12 months.

Liabilities: What the business owes to non-owners.

Current Liabilities: Monies due to be repaid within 12 months.

Non-Current Liabilities: Monies due to be repaid after 12 months.

Net Assets: Is the difference between what is owned (Assets) and what is owed (Liabilities).

Owner's Equity: Is what the net assets are represented by. It represents the total profits of the business since commencement less distribution made to the owners.

Connection between Balance Sheet and Profit and Loss Statement

1. Total Assets Minus Total Liabilities Equals Owner's Equity. The above business has \$130,000 in owner's equity. The business is profitable.
2. When Total Liabilities Exceed Total Assets the business is **NOT** profitable.
3. The company is, generally, able to pay its debts when they fall due if Current Assets Exceed Current Liabilities. With current assets, the higher the cash component the better. Lack of planning and management in this area has caused many businesses to fail.

BALANCE SHEET

ASSETS	
Current Assets	
- Trade Debtors	50,000
- Cash at Bank	10,000
- Term Deposit	50,000
- Inventory	60,000
<u>Total Current Assets</u>	<u>\$170,000</u>
Non-Current Assets	
- Plant & Equipment	100,000
<u>Total Non-Current Assets</u>	<u>100,000</u>
<u>TOTAL ASSETS</u>	<u>\$270,000</u>
LESS: LIABILITIES	
Current Liabilities	
- Trade Creditors	40,000
- Bank Loan	20,000
<u>Total Current Liabilities</u>	<u>60,000</u>
Non-Current Liabilities	
- Bank Loan	80,000
<u>Total N/Current Liabilities</u>	<u>80,000</u>
<u>TOTAL LIABILITIES</u>	<u>\$140,000</u>
NET ASSETS	<u>\$130,000</u>
Represented by:	
OWNER'S EQUITY	\$130,000

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