Balance Sheet
Approximately 60’

Slide 1  Introduction  3’

Click for slide and title;

T  Good….. (Morning, afternoon, evening).
   How are you today?

S  answers.

T  Thank you very much. Well today, we are speaking about financial positions and more precisely about balance sheets.

Click for title.
   Do you know what balance means?

S  The first meaning is equilibrium, you can say you keep or lose your balance.

T  What do you understand if I ask you: “What’s my balance?”

S  How much is there in your account?

T  What do you understand if I say: “the two sides have to balance out?”

S  answers

T  When speaking about accounting, we say balance sheet because the two sides balance out. This makes sense: a company has to pay for its assets by either borrowing money (liabilities) or getting it from shareholders (shareholders’ equity).
   Do you know of other financial statements?

S  The income statement and cash flow statement.

T  Right. They make up the cornerstone of any company’s financial statements. Let’s go to the heart of the matter…
What is meant exactly by the terms balance sheet? We’re going to try and answer this question… look at the word list.

Which of these words are related to balance sheet?

- Written statement
- Assets
- Point in time
- Financial state
- Liabilities
- Shareholders
- Creditors

Can you try to explain what a balance sheet is with the right words?

It’s a written statement for shareholders and creditors. It shows the financial state of the company at a particular time. It lists the company’s assets and the money owed, that is to say liabilities.

Company law in Britain and the Securities and Exchange Commission in the US require companies to publish annual balance sheets, is it the same in your country?

A balance sheet is divided into three sections, which are assets, liabilities and equity. A = L + E. The totals have to balance.

Can you describe the two major sides? What can you see on the document?

One half shows the business assets which can be material or immaterial. They list everything with a monetary value owned by the company: It can be money, like here cash in the bank. But it can be tangible assets, such as factories and machines that will bring future economic benefits. The other side shows the company liabilities. Liabilities are obligations to pay other organizations or people: money that the company owes or will owe at a future date.
These often include loans, taxes that will soon have to be paid, future pension payment to employees, and bills from suppliers that is to say companies which provide raw material, parts or services. Since assets are shown as debits (as the cash or capital account was debited to purchase them) and the total must correspond with the total sum of the credits, that is the liabilities and capital- assets equal liabilities plus capital or $A = L + E$. You can see that total value of the Assets ($50650) equals to the total value of Liabilities ($17900) and Equity ($32750).

T One question about a specific point: what about suppliers, what happens if the company was granted credit for buying goods?

S It has to be in the liabilities part.

Slide 3 Shareholders’ equity

Click for slide and title;

T What do you understand when I say “Statement of financial position”?

Click for boxes 1 & 2 ➔ 2clicks here;

S It’s the American equivalent for balance sheet.

T Are there any similarities between the British and American expressions?

S answers

T What is the lay out of a balance sheet in your country?

S answers

T OK. American and continental European companies put assets on the left and equity/capital and liabilities on the right. In Britain, this was traditionally the other way round, but nowadays most British companies use a vertical format, with assets at the top and liabilities and capital below.

Click for box 3;

T What about shareholders? What’s shareholder’s equity?
Shareholder’s equity consists of all the money belonging to shareholders. Part of this is share capital— the money the company raised by selling its shares.

What about retained earnings? Do you remember what retained earnings are? We talked about it when we discussed stocks and shares?

Instead of paying shareholders a dividend, the company turns the profit into capital by issuing new shares to existing shareholders, retained earnings are profits from previous years that have not been distributed as dividends. As a matter of fact, shareholders’ equity also includes retained earnings. Shareholders’ equity is the same as the company’s net assets, or assets minus liabilities.

What other type of information can I find on the balance sheet? Does it specify how much money a company has spent?

A balance sheet does not show how much money a company has spent or received during a year.

This information is given in other financial statements: the profit and loss account and the cash flow statement.

DISTRIBUTE PROFIT
GRANT CREDIT
OWE MONEY
PAY LIABILITIES
RETAIN EARNINGS
T  Now use the words you’ve just found to fill in the blanks.

S  We RETAIN (click to unmask solution when correct answer given) a lot of our EARNINGS (click) because we don’t DISTRIBUTE (click) any of our PROFITS (click) to the shareholders.
Most businesses have customers who OWE MONEY (click) because they GRANT (click) them 30 or 60 days’ CREDIT (click). We have a lot of LIABILITIES (click) that we’ll have to PAY (click) later this year.

Slide 5  Training 6’

Click for slide and title;

T  Let’s take the example of Chris and her company, a little restaurant. What is she doing?

Click yellow caption + picture 1 + white caption ➜ 3 clicks here;

S  Chris goes to the bank and gets a small business loan. The bank gives her cash.

Click for brown arrow;

T  What are the consequences on the balance sheet?

Click for box 2;

S  This will result in an increase in the liabilities on her balance sheet. On the balance sheets, her liabilities will go up the size of the loan. Her assets increase by the same amount. The balance sheet remains in balance.

Click for picture 3;

T  What happens then if Chris uses the cash to buy a truck and start her own sushi delivery service?

S  This will cause the cash asset to decrease but that will be balanced by another increase in her other assets: a new truck!

T  Where is this recorded in the balance sheet?

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The profit is recorded in the balance sheet as retained earnings in the equity section of the balance sheet.

What happens when she makes a monthly payment to reimburse her loan. How does it balance?

She reduces her liabilities by the amount of the payment and her cash is reduced by the same amount.

What’s her business worth?

To find out her business’ worth Chris subtracts liabilities from her assets. This equals to net worth of her business.

There seems to be two sorts of assets: current assets refer to cash or liquidity and to other assets that may be expected to realize in cash or be sold or used within a period less or equal to one year. Current assets are assets that will probably be used by the business in the near future. They include cash, money in bank accounts, saving bonds, that is to say money available to spend immediately. It also includes debtors, that is to say companies or people who owe money they will have to pay in the near future, and stocks. Generally speaking the more cash on hand, the better.

Is it a sign that the company is strong?
There are some cases where cash on the balance sheet doesn't necessarily mean the company isn't weak. If a company doesn't generate enough profit, they may turn to a bank to borrow money. The money sitting on the balance sheet as current assets may be borrowed money. To find out you have to check liabilities.

What about non-current assets?

There are also non-current assets such as long-term investments; they are used by the company for a period longer than one year. These are for example buildings and equipment.

What happens if a company anticipates that a debt will not be paid?

The company and the right department in the company must take action. It will write off, or abandon, the sum as a debt, and make provisions by charging a corresponding amount against profits: that is, by deducting the amount of the debt from the year's profit.

What about raw materials? What about unfinished work?

Manufacturing companies generally have a stock of raw materials, and also work in progress, which means partially manufactured products as well as products ready for sale. There are various ways of valuing stock or inventory, but generally these are valued at the lower of cost market, that is whichever figure is lower.

How can you calculate the cost? The market price?

Their cost is the purchase price plus the value of any work done on the items.

Should you anticipate profit?
S  Even if the stock is expected to be sold at a profit, you should not anticipate profits.

Slide 7  Tangible and intangible assets

Click for slide and title;

T  Look at these words:

Click for box 1;

I’m going to ask you to classify them into three categories:

Current Assets / Fixed Assets and a new category: intangible assets. Let’s first clarify the notion of Tangible assets. Do you understand what it means?

S  Tangible assets are assets with a physical existence such as property, plant and equipment. Current assets are: cash in the bank, debtors, and stocks. Fixed assets are: buildings, land and investments.

T  Can you explain what intangible assets are?

Click for box 2;

S  Intangible assets do not exist physically but represent a cost or benefit to a company. Intangible assets are: name, human capital and reputation.

T  Very good. What about name?

S  They include brand names, legally protected names for a company’s product, patents, exclusive rights to produce a particular new product for a fixed period, and trade marks, that is names or symbols that are put on products and cannot be used by other companies.

T  What about people and reputation? What about the notion of loyalty?

S  Network of contacts, loyal customers, reputation, trained staff or human capital, and skilled management can also be considered as intangible assets. Because it is difficult to give an accurate value...
for any of these things, companies normally only record tangible assets.

T What is the best way to put the right worth on a going concern, that is to say a company that is expected to make good profits?

Click for box 3;

S A going concern should be worth more on the stock exchange than simply its net worth or net assets: assets minus liabilities.

T Imagine I want to buy a company above its net worth because of its intangible assets. How shall the price be calculated?

Click for box 4;

S The difference in price is recorded under assets in the balance sheet as goodwill; it’s the amount a buyer pays above a company’s asset.

T What happens to tangible asset’s value? What about depreciation charges?

Click for box 5 + banner;

S Tangible assets are generally recorded as their historical cost less accumulated depreciation charges, that is to say the amount of their cost that has already been deducted from profits. This gives their net book value.

T Think about the company you work for, what are the most valuable assets? Are they shown on the balance sheet?

S answers
T What do you know about depreciation charges in your country. Let’s take the computer we’re working with as an example.

S answers
T What about intangible assets?
S answers.
Now let’s speak about liabilities…

What type of liability do you know?

Generally there are two types of liabilities: the current and the long term liabilities.

What is that supposed to mean exactly?

Current liabilities are to be considered on the short term. They are expected to be paid within a year of the date of the balance sheet.

Could you be more specific? What do they include?

They include creditors, most of the time they are suppliers of goods, services, raw materials, parts or components. Most of the time they are not paid at the time of purchase. They also include planned dividends, and deferred taxes, that is to say money that will have to be paid as tax in the future, although the payment doesn’t have to be made now.

What about accrued expenses?

They are expenses that have accumulated during the accounting year but will not be paid until the following year after the date of the balance sheet. So accrued expenses are charged against income that is to say that it has to be deducted from profit even though the bills have not been received or the cash paid.

Now let’s see if you have understood… Imagine I am a trainee. Listen to my statements and say whether they are true or false. Are
you ready to start? Use the words appearing on the screen to answer. At least two out of three. Current liabilities are to be paid before the date of the balance sheet.

Click for line 1;

S  Current liabilities are expected to be paid within a year, If they are paid it’s no longer a liability and consequently it won’t appear on the balance sheet. So it’s false.

T  Accrued expenses can be compared to money an individual saves to pay bills in the future.

Click for line 2.

S  It’s true actually, accrued expenses are charged against profit, even though the bills or invoices have not yet been received.

Slide 9  Asking for trade references

Click for slide and title;

T  Now imagine, a new client, ABC Ltd who wants to open an account with your company, has just placed an order and has also requested three months’ credit. What is the first thing to be done?

Click for box 1;

S  I guess in this situation, I would enquire about the company’s status/standing and ask for trade references.

T  How could you do this?

S  I could address a company given as a referee. I could also address the company’s bank.

T  What would you write? Here are a few hints to help you. You can use the words in the box. For each step, say what you intend to write or say. Then try to make a correct sentence and please do not forget this is a request.
At first, I would state straight away the reason of my letter. Of course, I would add private and confidential.

Which expressions do you know to make requests?

ABC Ltd wishes to open an account with us and has given your name as a reference. We would be grateful if you would give us your opinion as to this company’s reliability.

Then I would explain the situation, giving a few details to justify my demand: not only has this company placed a big order with us but it also requires credit.

I would ask the question precisely. Could you give us your opinion as to the reliability of this company? We would be very grateful if you could tell us whether the quality of its work was up to standard? Could you supply us with information about the company’s standing.

What about confidentiality?

Of course, I’ll need to reassure the bank or the company saying the information will be treated in the strictest confidence. Finally I could offer my help. It goes without saying that any information you may supply will be treated in the strictest confidence. If we can help you in the future, please do not hesitate to contact us.
Imagine that your company receives a request for a reference. Please reply this letter, saying the company Turner & Oliver Ltd has a sound management and is trustworthy.

You can use the vocabulary below.

Click for word box

S  writes

Please help/rephrase/correct when necessary. Thank you

T  Thank you very much and see you next time!