

What is the Accounting Equation?

Worksheet

The accounting equation states that $\text{Assets} = \text{Liabilities} + \text{Equity}$ - a company's resources always equal the claims against them from creditors and owners.

$$A = L + E$$

Questions

1. If $\text{Assets} = \$200,000$ and $\text{Liabilities} = \$75,000$, what is Equity ?

- A) \$275,000
- B) \$125,000
- C) \$75,000
- D) \$200,000

2. The accounting equation is the basis for which financial statement?

- A) Income statement
- B) Balance sheet
- C) Cash flow statement
- D) Statement of retained earnings

3. A company takes out a \$10,000 loan to buy equipment. What happens?

- A) Assets and liabilities both rise by \$10,000
- B) Equity rises by \$10,000
- C) Assets fall by \$10,000
- D) Liabilities fall by \$10,000

4. If $\text{Liabilities} = \$50,000$ and $\text{Equity} = \$150,000$, $\text{Assets} = ?$

- A) \$100,000
- B) \$200,000
- C) \$50,000
- D) \$150,000

5. A bakery has \$45,000 in cash, \$15,000 in equipment, and owes \$20,000 to a supplier. Find the owner's equity.

6. A startup has \$80,000 in liabilities and \$120,000 in equity. What are its total assets?

7. A shop's assets are \$150,000 and liabilities are \$55,000. Find equity.

8. Define: What is the accounting equation?

9. Define: Why must the equation always balance?

10. Define: What happens to equity if assets increase but liabilities stay the same?

Answer Key

1. B) $\$125,000 - E = A \quad L = 200,000 \quad 75,000 = 125,000$.
2. B) Balance sheet - The balance sheet lists assets, liabilities and equity in this equation.
3. A) Assets and liabilities both rise by $\$10,000$ - Cash/equipment (asset) and loan (liability) both increase by $\$10,000$, keeping the equation balanced.
4. B) $\$200,000 - A = L + E = 50,000 + 150,000 = 200,000$.
5. $A = 45,000 + 15,000 = 60,000 \quad L = 20,000 \quad E = A \quad L = 60,000 \quad 20,000 = 40,000$
6. $A = L + E \quad A = 80,000 + 120,000 = 200,000$
7. $E = A \quad L \quad E = 150,000 \quad 55,000 = 95,000$
8. Assets = Liabilities + Equity - the foundation of the balance sheet and double-entry bookkeeping.
9. Because every transaction has two sides (debit and credit) that keep assets equal to liabilities plus equity.
10. Equity increases by the same amount, since $E = A - L$.

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