

FINANCE AT A GLANCE

What are LIABILITIES?

Lesson 07

Recall from Lesson 1 the following illustration:

The company's resources:

Cash
Inventories
Equipment

EQUALS

How the company got its resources:

Credit given by suppliers
Funds borrowed from banks
Funds from business owners

The credit given by suppliers and the funds borrowed from banks constitute a company's liabilities. Liabilities, in accounting terminology, are obligations of a company to parties it owes money from, such as its suppliers and banks.

Liabilities can also be in the form of advance payments from clients who anticipate delivery of products and services. Such advance payments contribute to a company's financial means to acquire assets.

Salaries already earned by employees but are pending release to them, as well as tax obligations to government bodies already incurred but are pending settlement also comprise liabilities. How do salaries due and taxes due finance assets? Well, look at it this way: The funds that could have been used to pay the salaries and the taxes due were instead used (temporarily) to acquire some assets. Therefore, the salaries payable and the taxes payable are, in effect, financing the assets, in the same way that funds from banks, credit from suppliers and advances from clients do.

Let us now incorporate in the illustration these other liabilities that we have just discussed (as well as the other asset forms we discussed in Lessons 5 and 6).

The company's resources:

Cash
Short-term investments
Accounts receivable
Inventories
Prepaid expenses
Long-term investments
Net fixed assets (property, plant
and equipment net of depreciation)
Intangible assets
Other assets

EQUALS

How the company got its resources:

Credit given by suppliers
Advances from clients
Salaries owed to employees
Taxes awaiting settlement
Funds borrowed from banks

Funds from business owners

We shall look into liabilities and equity in the coming lessons.

Until then, thank you for your continued interest in Finance At A Glance.

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