

# Accounting Primer

VBA School of Bank Management

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# Agenda & Goals

Approach Accounting with Confidence



# Class Format

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## Section I

Accounting Overview  
Financial Statements



## Break



## Section II

Asset Liability  
Management  
How do banks make  
money?  
Financial ratios



## Lunch Break



## Section III

Liquidity, Risks,  
Capital Adequacy  
Articulation of the  
Statements and  
Interrelationships



# Zoom Introductions



What was the first concert you ever attended?



What was your favorite childhood vacation spot?



What was your first vehicle?



What is your super power?



# Goals

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**BASIC ACCOUNTING  
FUNDAMENTALS**



**UNDERSTAND A BANK'S  
BALANCE SHEET AND INCOME  
STATEMENT**

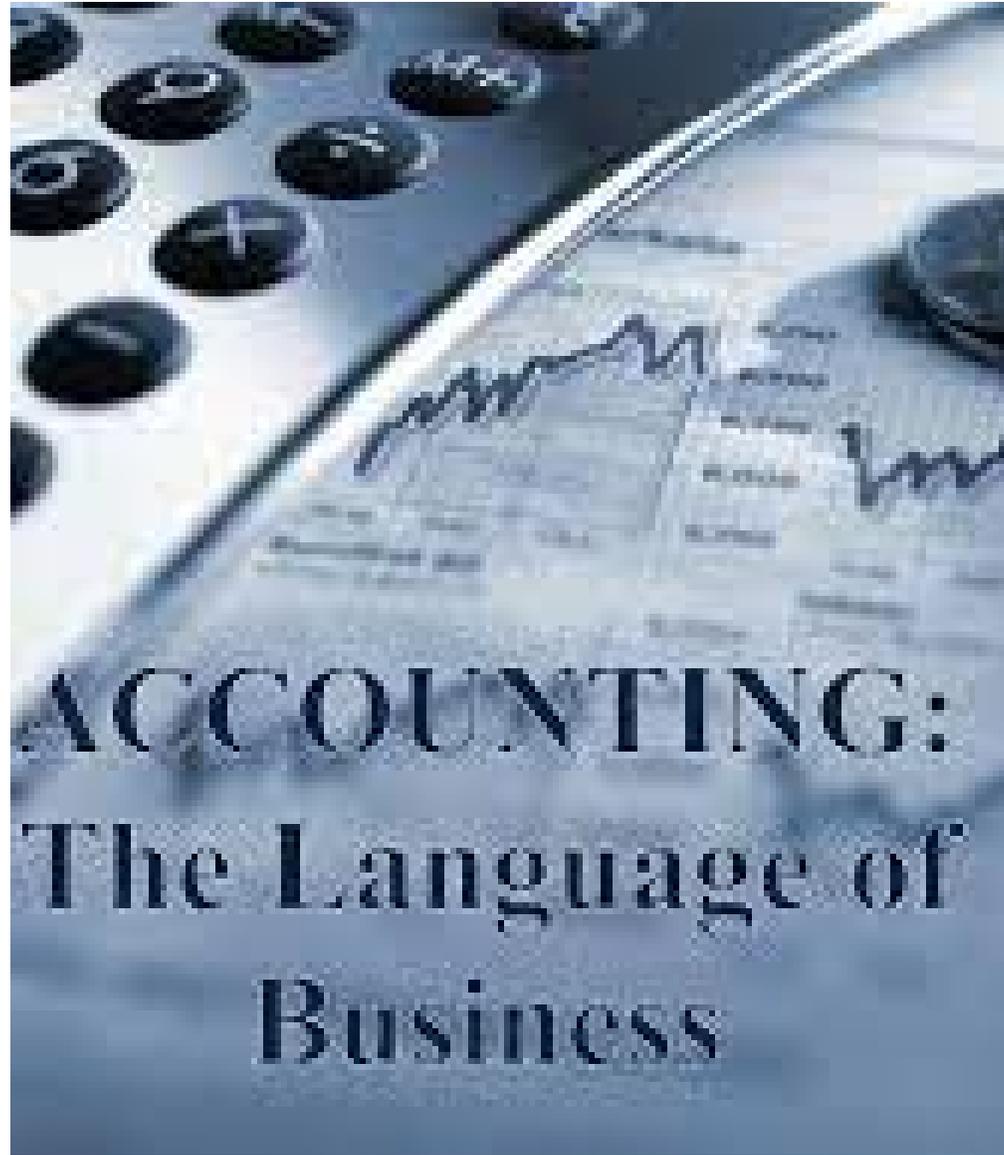


**UNDERSTAND HOW THEY  
RELATE TO LIQUIDITY,  
CAPITAL, AND PROFITABILITY**



# It's not just numbers.

- It tells your Bank's story!



# Financial Statements

Road Map telling us about the Bank's past, where it is now, and where it is headed in the future.



A blue marker is shown writing the words "Annual Report" in a cursive, handwritten style on a white notepad. The notepad has several horizontal lines. The background of the entire image is a light blue, textured surface.

Annual  
Report

## Who Uses The Information?

Shareholders

Regulators

Directors

Employees

Customers

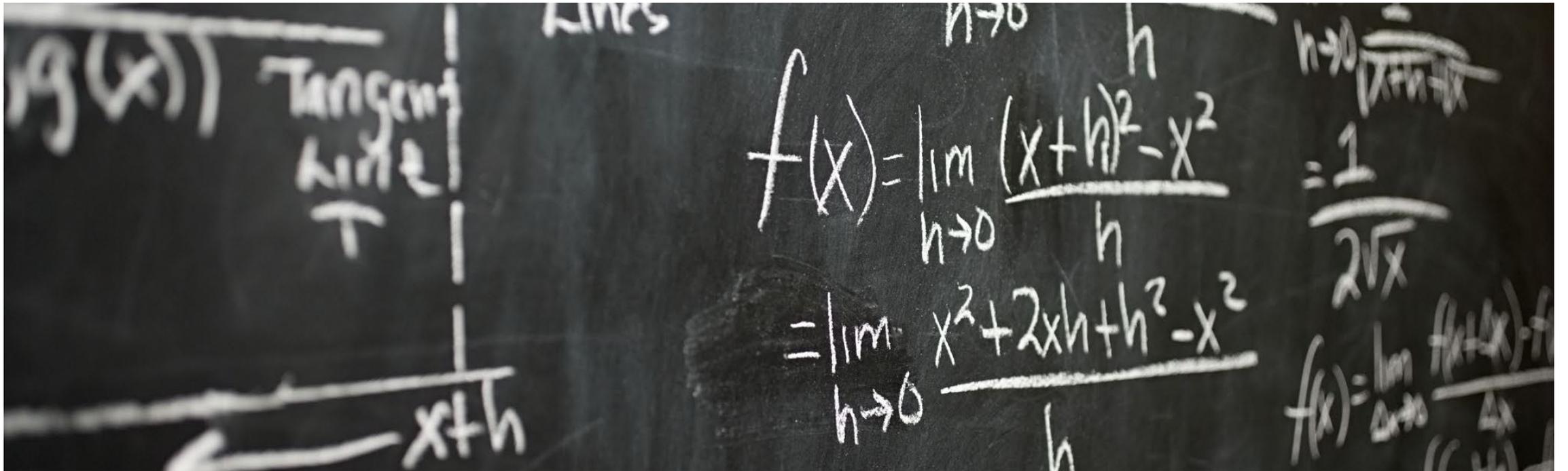




Report of Condition

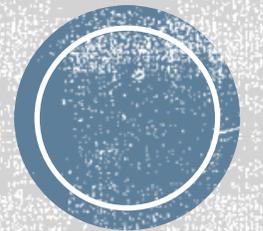
Balance Sheet

“Snapshot In Time”



# Assets = Liabilities + Equity

This is called the accounting equation.



Balance Sheet Must Balance!

# Balance Sheet

## Assets = OWN

- Loans are Assets
- Assets are USES of funds
- Usually carried at original cost

## Liabilities = OWED

- Debts or obligations
- Deposits are Liabilities
- Liabilities are SOURCES of funds

# Stockholders' Equity or Capital: Owners

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Common Stock

Paid in Capital

Retained Earnings (Undivided Profits)

Accumulated Other Comprehensive Income



**ILLUSTRATIVE  
BALANCE  
SHEET**

# Cash Assets

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Account is Called Cash and Due From Banks

Includes:

- Vault Cash
- Deposits with Other Banks (Correspondent Deposits)
- Cash Items in Process of Collection
- Reserve Account with the Federal Reserve

Sometimes Called Primary Reserves



# Cash Assets

Designed to meet the bank's need for liquidity.

This includes customer withdrawals, demand for loans, or other unexpected needs.



# GOAL: Balancing Act

To keep cash balance as low enough, because cash balances earn little or no interest income, and high enough to meet customer demands.

# Federal Funds Sold

## Fed Funds Sold are Overnight Loans

- Banks loan excess liquidity to other banks
- Earn fed funds rate

# Investment Securities

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Often Called Secondary Reserves

Back-up Source of Liquidity



Satisfy Pledging Requirement



Source of Income

Earn more than cash but less than loans  
Less risky. Less reward.

# Investment Securities

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## Taxable Securities

- U.S. Government Treasury Bills and Bonds
- Government Agency Securities
  - Federal Home Loan Bank, Federal Farm Credit Bank
- Corporate Bonds
  - Commercial Paper

## Tax-Exempt Securities

- Municipal Bonds



# **What's the Accumulated Other Comprehensive Loss related to investments about?**

Silicon Valley Bank Failure

A dark, semi-transparent background image showing a group of business professionals in a meeting. One person is pointing at a document on a table, while others look on attentively. The overall tone is professional and focused.

# Loans & Allowance

Types of Loans

Why does a bank need an allowance for credit losses?

# Types of Loans

## Real Estate Secured Loans

- 1-4 Family
- Multi-Family
- Home Equity Line/loans
- Construction and Development
- Commercial Real Estate

## Commercial and Industrial

## Consumer Loans

## Credit Cards

## Overdrawn Deposit Accounts



# Allowance for Credit Losses “ACL”

- Estimate determined by management under “CECL” (Current Expected Credit Losses)
- Calculation to determine an appropriate amount to set aside in case loans default
- Expected losses on loans over lifetime
- Reserve for HTM investment securities
- Liability for unfunded commitments



# Allowance for Credit Losses

Calculation:

Beginning Allowance for Credit Losses Balance

+ Provision for ACL (Expense from Income Statement)

- Actual Loan Charge-Offs

+ Recoveries from Previous Charged-Off Loans

= Ending Allowance for Credit Losses

# Allowance for Credit Losses

Exercise

**ILLUSTRATIVE  
BALANCE  
SHEET**

# Liabilities: Deposit Accounts

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**Non interest-bearing**  
Demand Deposits - Checking



**Interest Bearing Deposits**

Savings Deposits  
Interest Checking  
Money Market Deposit Accounts  
(MMDA)  
Time Deposits (Certificates of  
Deposits)

# Borrowings

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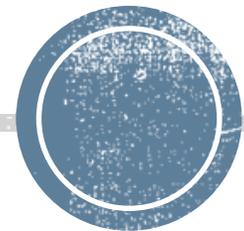
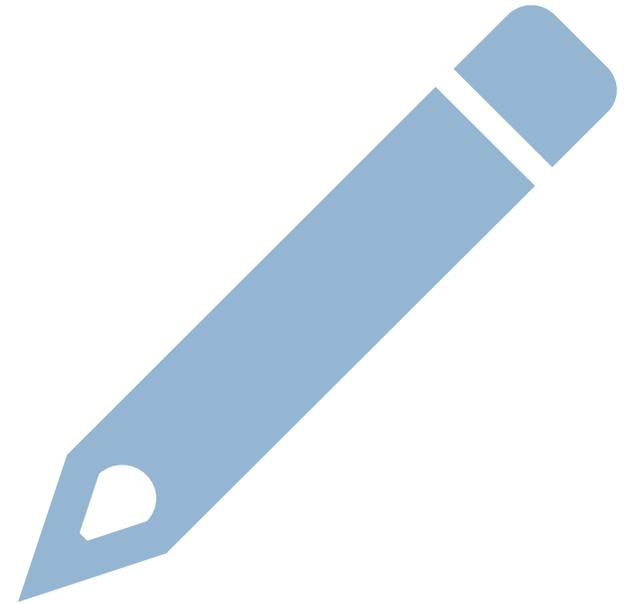
## Fed Funds Purchased

- Opposite of Fed Funds Sold
- Banks pay the fed funds rate to borrow liquidity from another bank overnight.

## Subordinated Debt

# In Class Exercise

Can you Balance a Balance Sheet?





Income Statement  
(Profit and Loss)

“Performance over  
a period of time”



# Income Statement

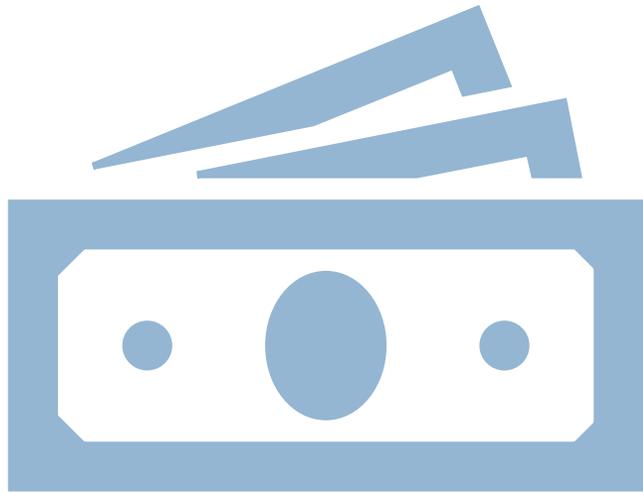
The income statement lists all categories of income and expenses. This statement details the financial performance and determines the amount of profit (loss).

+	Interest Income
-	Interest Expense
=	Net Interest Income
-	Credit Loss Expense
+	Non-interest income
-	Non-interest expense
=	Income before income taxes (pre-tax)
-	Income Taxes
=	Net income (loss)

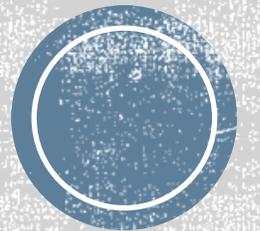
# Income Statement Components

Exercise to mark the components





# **Illustrative Income Statement**



**Net Interest Income =**

**Interest Income – Interest Expenses**

- Interest and Fees on Loans
- Federal Funds Sold
- Taxable Securities Revenue
- Tax-Exempt Securities Revenue
- Other Interest Income

- Deposit Interest Costs
- Interest on Short-Term Debt - Fed Funds Purchased
- Interest on Long-Term Debt or Other Borrowings

# + Non-interest Income

# – Non-interest Expenses

## Non-interest Income

- Service Charges on Deposit Accounts
- ATM/Debit Cards
- Mortgage origination fees
- Investment and Trust Fees
- Other Non-interest Income

## Non-interest Expenses

- Salaries and Employee Benefits
- Premises/Facilities/Occupancy and Equipment Expense
- Marketing Expense
- FDIC Insurance Expense
- ATM/Debit Card Expense
- Other Operating Expenses

# Service Charges on Deposit Accounts

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Checking Account Average Balance Fees

Overdraft Fees

Stop Payment Fees

# In Class Exercise

Can you calculate Net Income?



# In Class Exercise

Can you distinguish which accounts go on which statement?

