

MODULE 8 FINANCIAL STATEMENTS | CHS 17, 18 & 19

Learning Objectives:		Topic*	Ch & Time
8.1	Describe the information provided in an income statement, and the purpose of an income statement.	F	Ch 17 3 hours
8.2	Prepare an income statement.	F	
8.3	Explain the difference in net income and income from continuing operations (discontinued operations).	F	
8.4	Define and calculate earnings per share.	F	
8.5	Describe the information provided in the statement of comprehensive income, statement of equity, and balance sheet and purpose of these statements.	F	Ch 18 3 hours
8.6	Prepare a statement of comprehensive income, statement of equity, and balance sheet.	F	
8.7	Describe the information provided in statement of cash flows, and the purpose of a statement of cash flows.	F	Ch 19 6 hours
8.8	Prepare a statement of cash flows using the direct method.	F	
Module 8 Total Hours = 12			

* F: Financial Accounting; M: Managerial Accounting; A: Financial Statement Analysis

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NOTES:

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LEARNING OBJECTIVE 8.1:

Describe the information provided in an income statement, and the purpose of an income statement.

LEARNING OBJECTIVE 8.2:

Prepare an income statement.

LEARNING OBJECTIVE 8.3:

Explain the difference in net income and income from continuing operations (discontinued operations).

Company Name	
INCOME STATEMENT	
For Year Ended (date)	
Sales	
Less cost of goods sold	
Gross Profit	
Less selling, general, & administrative expenses	
Operating Income (Loss)	
Other revenue and gains:	
Interest income	
Dividend income	
Other expenses and losses:	
Interest expense	
Loss on sale of equipment	
Income (Loss) from Continuing Operations Before Taxes	
Income tax expense	
Income (Loss) from Continuing Operations	
Discontinued operations:	
Income (Loss) from operations	
Gain (Loss) on disposal	
Net Income	
Earnings Per Share	

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Discontinued Operations

- Company sells or disposes of a component of an entity
- Report, net of tax:
 - Income (loss) of the component from the beginning of the accounting period to the date of sale or disposal, and
 - Gain (loss) on the sale or disposal of the component

LEARNING OBJECTIVE 8.4:

Define and calculate earnings per share.

Earnings Per Share

- Measure of operating performance on a per share basis
- EPS serves as an indicator of a company's profitability and growth

EPS Practice Problem 1

For the year ended December 31, 2017

Sales = \$1,000,000

Cost of Goods Sold \$600,000

SG&A expenses = \$150,000

Other income/(expense), net = (\$100,000)

Additional Information:

On January 1, 25,000 shares of common stock were outstanding. On July 1, 10,000 shares of common stock were issued.

$$\begin{aligned}
 \text{EPS} &= \frac{(\text{Net Income} - \text{Preferred Stock Dividends})}{\text{Weighted Average Number of Common Shares Outstanding}} \\
 &= \frac{\$150,000}{30,000*} \\
 &= \$5 \text{ per share}
 \end{aligned}$$

$$*30,000 = (25,000) + (10,000 \times 6/12)$$

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LEARNING OBJECTIVE 8.5:

Describe the information provided in the statement of comprehensive income, statement of equity, and balance sheet and purpose of these statements.

LEARNING OBJECTIVE 8.6:

Prepare a statement of comprehensive income, statement of equity, and balance sheet.

Company Name	
Statement of Comprehensive Income For Year Ended (date)	
Net Income	
Other Comprehensive Income:	
Unrealized Gain on Available-for-Sale Securities	
Total Comprehensive Income	

Comprehensive Income

- Comprehensive income is the sum of net income and other items that must bypass the income statement because they have not been realized, including items like an unrealized holding gain or loss from available for sale securities and foreign currency translation gains or losses.
- These items are not part of net income, yet are important enough to be included in comprehensive income, giving the user a bigger, more comprehensive picture of the organization as a whole.
- Items included in comprehensive income, but not net income are reported under the accumulated other comprehensive income section of shareholders' equity

Available for Sale Securities

- Management does not intend to sell in the next accounting year
- Reported on the balance sheet as a current asset, or a long-term asset in the investment section
- Change in cost (versus fair value) is reported as an unrealized gain/loss on the balance sheet in a separate section of stockholders' equity

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Trading Securities

- Management intends to sell in the near term
- Reported on the balance sheet as current asset
- Change in cost (versus fair value) is reported as an unrealized gain/loss on the income statement as part of "Other revenues and gains" or "Other expenses and losses"

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Company Name		
BALANCE SHEET		
(Date)		
Assets		
Current Assets:		
Cash		
Trading Securities		
Accounts Receivable		
Inventory		
Other Assets/Prepaid Expenses		
Investments:		
Investments accounted for using the Equity-method		
Available for Sale Securities		
Held to Maturity Debt		
Property, Plant and Equipment:		
Land		
Buildings		
Equipment		
Intangible Assets:		
Patents		
Trademarks		
Goodwill		
Liabilities		
Current Liabilities:		
Accounts Payable		
Accrued Expenses Payable		
Current portion of long-term debt		
Long-term Debt Securities:		
Notes Payable		
Bonds Payable		
Other Long-term Liabilities		
Owner's Equity		
Common Stock		
Preferred Stock		
Additional Paid-in Capital		
Retained Earnings		
Accumulated Other Comprehensive Income		
Treasury Stock		

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LEARNING OBJECTIVE 8.7:

Describe the information provided in statement of cash flows, and the purpose of a statement of cash flows.

LEARNING OBJECTIVE 8.8:

Prepare a statement of cash flows using the direct method.

The **income statement** and **balance sheet** follow the accrual basis of accounting, where revenues are recorded when earned (whether or not cash was received) and expenses are recorded when incurred (whether or not they have been paid).

The **cash flow statement** follows the **cash basis of accounting** where only actual cash inflows and outflows are recorded.

Operating activities

- Relating to the day-to-day operations of the business
- Inflows
 - Collections from customers
 - Collections of interest
 - Collections of dividends
- Outflows
 - Payments to suppliers of goods and services
 - Payments to employees
 - Payments for interest
 - Payments for taxes

Investing activities

- Buying and selling property, plant, and equipment and other long-term investments
- Inflows:
 - Proceeds from sales of long-term assets (PPE)
 - Collections of loans made to other entities
 - Proceeds from sales of short-term investments
- Outflows:
 - Purchases of long-term assets (PPE)
 - Loans made to other entities
 - Purchases of short-term investments

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Financing activities

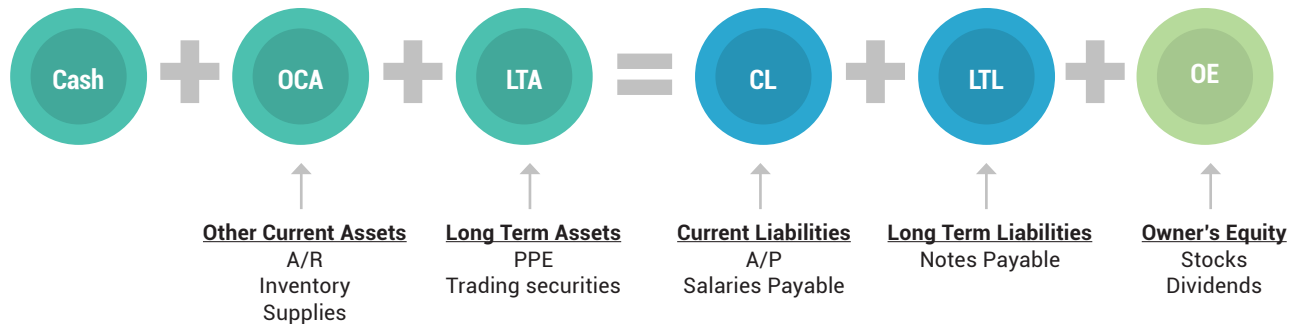
- Issuing and retiring debt, raising funds from owners and distributing dividends to owners
- Inflows:
 - Proceeds from issuance of debt
 - Proceeds from issuance of preferred and common stock
- Outflows
 - Payment of short and long-term debt
 - Purchase of treasury stock
 - Payment of cash dividends

Company Name Statement of Cash Flows For Period Ended _____		
Cash flows from operating activities		
Cash received from customers		
Cash received from renters		
Cash paid for inventory		
Cash paid for insurance		
Cash paid for wages		
Cash paid for miscellaneous expenses		
Cash paid for income taxes		
Cash paid for interest		
Net cash flows from operating activities		
Cash flows from investing activities		
Cash received from sale of trading securities		
Cash received from sale of equipment		
Cash paid for building		
Cash paid for equipment		
Net cash flows from investing activities		
Cash flows from financing activities		
Cash received from short-term note payable		
Cash received from bond issues		
Cash paid for treasury stock		
Cash paid for dividends		
Cash flows from financing activities		
Net change in cash during period		
Add beginning balance of cash		
Ending balance of cash		

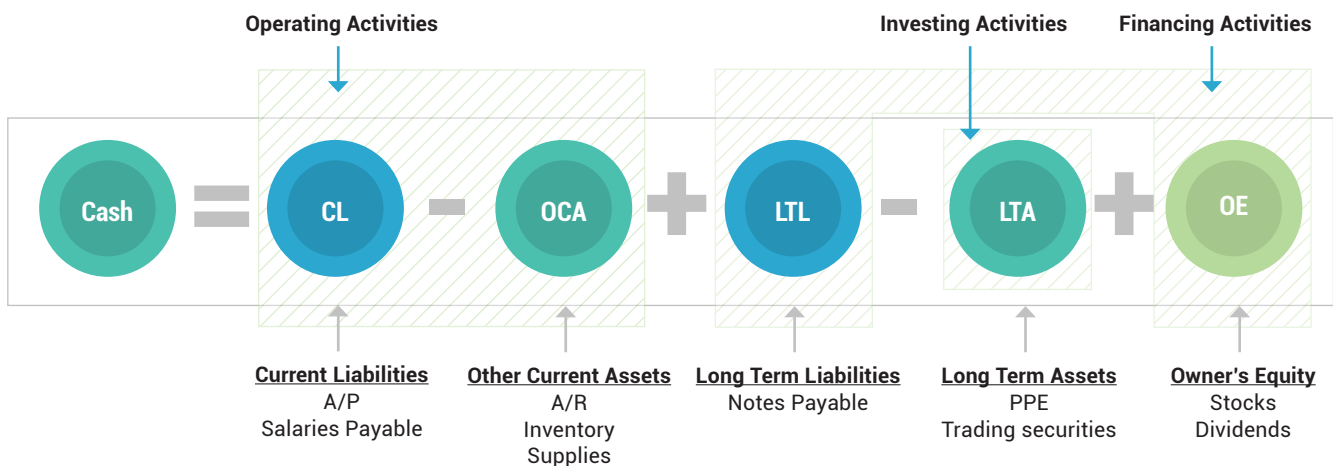
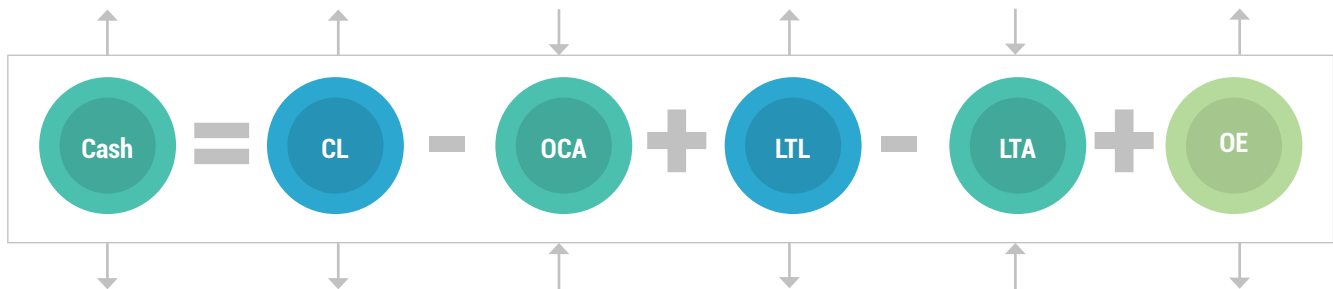
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Cash Flow

Identifying operating, investing, and financing activities



As cash flows in or out, what is the movement of the other classifications?



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Calculating cash flows from operating activities:***Revenues, Current Assets and Cash Inflows***

Cash received from customers:

Accounts Receivable	
Beginning balance	
Sales on account	Cash received
Ending balance	

Beginning Balance of Accounts Receivable
 +Net Sales on account during the period
-Cash collections from customers
 =Ending balance of Accounts Receivable

Related transactions:

(To record sale to customer on account)
 Accounts Receivable
 Sales

(To record cash collected from customer on account)
 Cash
 Accounts Receivable

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Expenses, Current Assets and Cash Outflows

Cash paid for prepaid expenses such as insurance, prepaid rent and supplies:

Prepaid Insurance (Prepaid Rent, or Supplies)	
Beginning balance	
Cash paid to purchase insurance	Expense (insurance, rent, supplies)
Ending balance	

Beginning balance of Prepaid Insurance
+Cash paid for insurance during the period
 -Insurance expense during the period
 =Ending balance of Prepaid Insurance

Related transactions:

(To record purchase of insurance)

Prepaid Insurance
 Cash

(To record expired insurance adjustment)

Insurance Expense
 Prepaid Insurance

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Expenses, Current Liabilities and Cash Outflows

Cash paid for wages, taxes and interest:

Wages Payable (Interest or Taxes)	
	Beginning balance
Cash paid to employees	Wages Expense (interest or rent)
	Ending balance

Beginning balance of Wages Payable

-Cash paid to employees

+Wages Expense during the period

=Ending balance of Wages Payable

Related transactions:

(To record end of period wages expense)

Wages Expense

Wages Payable

(To record payment to employees)

Wages Payable

Cash

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Expenses, Current Assets and Cash Outflows

Cash paid to suppliers (for inventory):

Inventory	
Beginning balance	
Purchases of Inventory	COGS
Ending balance	

Accounts Payable	
	Beginning balance
Cash paid to suppliers	Purchases of inventory
	Ending balance

Beginning balance of Inventory

+Purchases of inventory

-Cost of Goods Sold

=Ending balance of Inventory

Beginning balance of Accounts Payable

+Purchases of inventory

-Cash paid to suppliers

=Ending balance of Accounts Payable

Related transactions:

(To record Cost of Goods Sold)

COGS

Inventory

(To record payment of Accounts Payable)

Accounts Payable

Cash

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Cash Flows from Operating Activities
DIRECT Method

Cash Receipts:

From Customers (a)

Cash Payments:

To Suppliers (b)

For Rent or Insurance (c)

To Employees (d)

For Interest expense (e)

For Income Taxes (f)

Net Cash provided by Operating Activities

(a) Accounts Receivables, Sales

(b) Accounts Payable, Inventory, Cost of Goods Sold

(c) Prepaid Rent or Prepaid Insurance, Rent Expense or Insurance Expense

(d) Wages or Salary Payable, Wages or Salary Expense

(e) Interest Payable, Interest Expense

(f) Income Taxes Payable, Income Tax Expense

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Selected Balance Sheet Accounts

	<u>Dec. 31, 2017</u>	<u>Dec. 31, 2016</u>
Cash	10,000	20,000
Accounts Receivable	110,000	190,000
Merchandise Inventory	100,000	60,000
Prepaid Rent	30,000	15,000
Accounts Payable	40,000	53,000
Salaries Payable	3,000	8,000
Income Taxes Payable	0	0

Income Statement (Dec. 31, 2017)

Sales	900,000
Cost of Goods Sold	500,000
Salary Expense	190,000
Depreciation Expense	60,000
Rent Expense	70,000
Income Taxes Expense	40,000

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1. Cash collections from customers for sales during 2017 was:
2. Cash payments for salaries during 2017 was:
3. Cash payments for rent during 2017 was:
4. Cash payments to suppliers for merchandise inventory during 2017 was:
5. Cash payments for depreciation during 2017 was:
6. Cash payments for income taxes during 2017 was:
7. Total cash collected was:
8. Total cash paid was:
9. Cash from operating activities was:
10. Net income was:

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Cash Flows: Operating Activities (Direct Method)**Selected Balance Sheet account balances as of December 31:**

	<u>2017</u>	<u>2016</u>
Cash	30,000	10,000
Accounts Receivable	120,000	150,000
Merchandise Inventory	35,000	50,000
Prepaid Insurance	25,000	20,000
Accounts Payable	30,000	40,000
Salaries Payable	6,000	1,000
Income Taxes Payable	2,000	1,000
Interest Payable	3,000	3,000

Selected Income Statement items for the year 2017 are:

Sales	970,000
Cost of Goods Sold	500,000
Salary Expense	200,000
Depreciation Expense	60,000
Insurance Expense	70,000
Income Taxes Expense	40,000
Interest Expense	10,000

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1. Cash payments to suppliers for merchandise inventory during 2017 amounted to:
2. Cash payments for salaries during 2017 amounted to:
3. Cash payments for depreciation during 2017 amounted to:
4. Cash payments for insurance during 2017 amounted to:
5. Cash payments for income taxes during 2017 amounted to:
6. Cash payments for interest during 2017 amounted to:
7. Cash collections from customers during 2017 amounted to:
8. Total cash payments during 2017 amounted to:
9. Cash from operating activities during 2017 amounted to:
10. Net income is: