

PRINCIPLES OF FINANCIAL AND MANAGERIAL ACCOUNTING II

Statement of Cash Flows

I. History of Statement of Cash Flows

A. Prior to 1971

studied "funds flow" and "cash flow" but not required to be reported

B. 1971 through July 8, 1988

Statement of Changes in Financial Position required for all published financial statements

1. working capital concept (most popular)
2. cash concept

C. July 31, 1988 to present Statement of Cash Flows

1. considered a principal financial statement
2. to be included whenever Balance Sheet and Income Statement information is presented

II. Questions the financial statements attempt to answer (according to ALEX #1 illustration of Horatio Algie's Tree Trimming Service in first semester)

A. Balance Sheet

Where does my business stand today?

B. Income Statement

How well did my business do this month (this year, etc.)?

C. Statement of Cash Flows

*From where did cash come, and where did it go?
(also mentioned in Chapter 1, pp. 4, 21, 22, 24)*



III. Categories of sources ("inflows") and applications/uses ("outflows") of cash

Cash	
<u>Sources</u> ("inflows"):	<u>Applications/Uses</u> ("outflows"):
1. _____	1. _____
2. _____	2. _____
3. _____	3. _____
4. _____	4. _____

IV. Grouping sources/applications for Statement presentation

- I. _____
- II. _____
- III. _____

V. Operating Activities

A. Preparer assumed to understand these underlying concepts:

- 1. Balance Sheet/income Statement interrelated
 - a. Chapter 1, Exercise E1-10, we found net income from balance sheet data
 - b. Chapters 3, 4, 5, and others every AJE effected the BS and the IS

2. Net Income \neq Cash

- a. Chapter 14, appropriations of retained earnings

_____ \neq Cash

_____ \neq Cash

_____ $=$ Cash

- b. Income Statement prepared under accrual basis
- c. Results of operations reported on the income statement may result in many balance sheet changes -- not limited to changes in cash.

BALANCE SHEET		
Current Assets		
Cash	x	
Receivables	x	
Inventory	x	
PrePd Exp	<u>x</u>	xxxx
LT Assets		
PP&E	xxx	
Acc Depr	<u>x</u>	<u>xx</u>
TOTAL ASSETS		<u><u>xxxxxx</u></u>
Current Liabilities		
Accts Pay	x	
Sal Pay	<u>x</u>	xx
LT Liabilities		
Bonds Payable		xx
Capital Stock	x	
Retained Earnings	<u>x</u>	<u>xx</u>
TOTAL LIAB & SE		<u><u>xxxxxx</u></u>

INCOME STATEMENT	
Sales	xxxxxxxxxx
Cost of Goods Sold	<u> xx</u>
Gross Profit	xxxxxxxxxx
Expenses:	
Advertising	x
Depreciation	x
Salaries	x
Rent	x
Insurance	x
Interest	x
Utilities	<u>x</u>
Total Expenses	<u> xxxxxxx</u>
NET INCOME	<u><u> x</u></u>

- d. If these positions are true for one current asset and one current liability, we can assume they would be the same for all current assets and all current liabilities, and, therefore, summarize as follows:

- B. "Cash Provided by Operations" can be determined in three phases by changing Net Income as follows:
1. add and deduct _____
(best example: _____)
 2. add and deduct _____

(exceptions: dividends payable, marketable securities)
 3. to avoid duplication, negate effect of loss (add) or gain (deduct) from sale of LT investing and financing activities (already in NI).

VI. *Investing Activities*

- A. Determine in/outflows (referring to list of 4 sources/uses) by examining "non-current" accounts.
- B. Current and "noncurrent" accounts
- | | |
|---------------------|-----------------------|
| 1. <u>Current</u> | <u>"Non-Current"</u> |
| Current Assets | Long-Term Assets |
| Current Liabilities | Long-Term Liabilities |
| | Capital Stock |
| | Retained Earnings |
| | Revenue |
| | Expenses |
2. since significant cash transactions have one current and one "non-current" effect, easier to find them by examining "non-current" accounts

VII. *Financing Activities*

As for investing activities, determine in/outflows (referring to list of 4 sources/uses) by examining "noncurrent" accounts.

VIII. Summary

- A. "Tools" needed
1. Comparative Balance Sheet (provided in textbook)
 2. Four categories of sources and uses of cash
 3. Cash Provided By Operations (CPBO) "Window"
 4. Data from "non-current" accounts (provided)
 5. "Pattern" to follow (textbook or other example)
- B. "Know-How" needed (steps in preparing statement)
1. from comparative balance sheet, prepare an "increase/decrease" column (this becomes a "check-list" for making sure all changes were considered)
 2. using "4 sources/4 uses" list, consider items of in/outflow
 - a. convert NI to CPBO (three phases)
 - b. use information from "noncurrent" accounts to find *investing* and *financing* in/outflows.

IX. Sample Problem

The comparative balance sheet for Resurrection Company at April 30 of the current and preceding year is presented at the top of the next page. Selected "non-current" accounts are provided for additional information.

Prepare a statement of cash flows.



RESURRECTION COMPANY
COMPARATIVE BALANCE SHEET

<u>ASSETS</u>	<u>4/30/x2</u>	<u>4/30/x1</u>	Increase (Decrease)	✓
Cash	\$ 30,000	\$ 4,000	\$ 26,000	_____
Accounts Receivable	21,000	10,000	11,000	_____
Merchandise Inventory	30,000	36,000	(6,000)	_____
Equipment	180,000	150,000	30,000	_____
Accumulated Depreciation	(36,000)	(30,000)	(6,000)	_____
Land	-0-	30,000	(30,000)	_____
Total Assets	<u>\$225,000</u>	<u>\$200,000</u>	<u>\$ 25,000</u>	_____
 <u>LIABILITIES AND STOCKHOLDERS' EQUITY</u>				
Accounts Payable	\$ 33,000	\$ 40,000	\$ (7,000)	_____
Salaries Payable	3,000	2,000	1,000	_____
Dividends Payable	3,000	3,000	-0-	_____
Bonds Payable	20,000	60,000	(40,000)	_____
Common Stock	80,000	50,000	30,000	_____
Paid in Cap. in Excess of Par--C. S.	39,000	15,000	24,000	_____
Retained Earnings	<u>47,000</u>	<u>30,000</u>	<u>17,000</u>	_____
Total Liab. and Stockholders' Equity	<u>\$225,000</u>	<u>\$200,000</u>	<u>\$ 25,000</u>	_____

Equipment			
5/1/x1 Balance	150,000	Purchased for cash	30,000
Accumulated Depreciation			
	5/1/x1 Balance		30,000
	4/30/x2 Depreciation Expense		6,000
Land			
5/1/x1 Balance	30,000	Sold for \$28,000	30,000
Bonds Payable			
retired at maturity	40,000	5/1/x1 Balance	60,000
Common Stock			
	5/1/x1 Balance		50,000
	Issued for cash		30,000
Paid in Capital in Excess of Par — Common Stock			
	5/1/x1 Balance		150,000
	Issued for cash		24,000
Retained Earnings			
Dividends declared	5,000	5/1/x1 Balance	30,000
		Net Income per I. Stmt.	22,000

RESURRECTION COMPANY
Statement of Cash Flows
For the Year Ended April 30, xxxx

Cash flows from ***operating activities***:

Net income, per income statement \$ _____

Add: _____ \$ _____

Deduct: _____ \$ _____

Net cash flow _____ *operating activities* \$ _____

Cash flows from ***investing activities***:

_____ \$ _____

Less: _____

Net cash flow _____ *investing activities* _____

Cash flows from ***financing activities***:

_____ \$ _____

Less: _____ \$ _____

Net cash flow _____ *financing activities* _____

_____ in cash \$ _____

Cash at the beginning of the year _____

Cash at the end of the year \$ _____