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*To activate hyperlink, simultaneously press Control Key and click the mouse.

STUDENT LEARNING OBJECTIVES & RELATED ASSIGNMENT MATERIALS (CHART A)

LO#	*Student Learning Objective*	*Textbook Coverage (Page Ref.)*	*Mini-Exercise*	*Exercises*	*Coached Problems*	*Problems (Groups A & B)*	*Skills Development Cases*	*Continuing Case***	*Reserved*
LO1-1	Describe various organizational forms and business decision makers.	3 – 7	2				1, 2, 3		
LO1-2	Describe the purpose, structure, and content of the four basic financial statements.	7 – 16	2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12, 13, 14, 15, 16	1, 2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 12	1, 3	A: 1, 3 B: 1, 3	1, 2, 3, 4, 6, 7	1	
LO1-3	Explain how financial statements are used by decision makers.	16	16	3, 4, 6, 9, 10	2, 4	A: 2, 4 B: 2, 4	1, 2, 3, 4, 6	1	
LO1-4	Describe factors that contribute to useful financial information.	16 - 19	1, 2, 3				4, 5, 6		
LO1-S1	Describe the decision to become a public company and explain the implications for accounting.	20 - 22							
LO1-S2	Choose data visualizations appropriate for answering different question types.	22 - 26							
	**Continuous case assignment relates to entrepreneur Nicole Mackisey and is extended to each future chapter.								

STUDENT LEARNING OBJECTIVES & RELATED TECHNOLOGY ASSIGNMENT MATERIALS (CHART B)

LO#	***Student Learning Objective***	***Integrated Excel***	***Data Analytics (Tableau & Data Visualization)***
LO1-1	Describe various organizational forms and business decision makers.		
LO1-2	Describe the purpose, structure, and content of the four basic financial statements.	*Mini-Exercise M1-16* *Coached Problem CP1-1* *Problem PA1-1*	TDA 1-1, 1-3
LO1-3	Explain how financial statements are used by decision makers.	*Mini-Exercise M1-16*	TDA 1-3
LO1-4	Describe factors that contribute to useful financial information.		
LO1-S1	Describe the decision to become a public company and explain the implications for accounting.		TDA 1-2
LO1-S2	Choose data visualizations appropriate for answering different question types.		DV 1-1

STUDENT LEARNING OBJECTIVES & RELATED INSTRUCTOR MATERIALS / ONLINE DELIVERY (CHART C)

LO#	***Student Learning Objective***	***Textbook Coverage (Page Ref.)***	***Textbook Exhibit***	***Concept Overview Video******	***PowerPoint Slide #***	***PowerPoint Animated Builds & Solutions***	***PowerPoint Animated Slide #***
LO1-1	Describe various organizational forms and business decision makers.	3 – 7	1, 2	3 videos	2 - 5		
LO1-2	Describe the purpose, structure, and content of the four basic financial statements.	7 – 16	3, 4, 5, 6, 7, 8	9 videos	6 - 21	Mini-Exercise M1-12 Exercise E1-3, 1-6, 1-8 Skills Development Case S1-6 (Requirement 1)	41 - 42 43 - 50 51 - 53
LO1-3	Explain how financial statements are used by decision makers.	16		3 videos	22, 23	Exercise E1-3, 1-6 Skills Development Case S1-6 (Requirement 1)	43 - 48 51 - 53
LO1-4	Describe factors that contribute to useful financial information.	16 - 19	9	2 videos	24 - 27	Skills Development Case S1-6 (Requirement 1)	51 - 53
LO1-S1	Describe the decision to become a public company and explain the implications for accounting.	20 - 22	1A.1, 1A.2		28 – 32		
LO1-S2	Choose data visual-izations appropriate for answering different question types.	22 - 26			33 - 39		
	***Individual videos are available for viewing and assignment in Connect						

CHAPTER ONE
BUSINESS DECISIONS AND FINANCIAL ACCOUNTING

OVERVIEW

A real entrepreneur meets with his local CPA, who walks him through the decisions he must make when planning his business. Students discover the role of accounting, with an emphasis on financial statement reporting and use.

SYNOPSIS OF CHAPTER REVISIONS

Focus Company: Noodlecake Studios

- Updated chapter opener describing the latest developments at this private company and its development of award-winning video games
- New Supplement 1A to present a framework for choosing appropriate data visualization techniques
- Updated Spotlight on the World depicting IFRS acceptance around the world
- Updated Spotlight on Ethics to discuss Theranos case
- Updated demonstration case featuring WD-40 Company
- Reviewed and updated all end-of-chapter material, including financial data for Designer Brands, Garmin, ZipRecruiter, and others

LEARNING STRATEGY – GETTING STARTED

☑ Overview the textbook:

- Margin Boxes
- You Should Know
- Coach's Tip
- How's It Going? — Self Study Practice
- Review the Chapter — Demonstration Case
- Chapter Summary
- Key Terms
- Homework Helper
- Practice Material

☑ Highlight and demonstrate Connect:

  - SmartBook, Concept Overview Videos, PowerPoint slides, assignments, etc.

CHAPTER SUMMARY

LO 1-1 Describe various organizational forms and business decision makers.

- Sole proprietorships are owned by one individual, are relatively inexpensive to form, and are not treated legally as separate from their owners. Thus, all profits or losses become part of the taxable income to the owner, who is also responsible personally for all debts of the business.
- Partnerships are businesses legally similar to proprietorships, but with two or more owners.
- Corporations are separate legal entities (thus, corporations pay taxes) that issue shares of stock to investors (stockholders) and are more costly to establish. Stockholders cannot be held liable for more than their investment in the corporation. Private corporations issue stock to a few individuals while public corporations issue stock to many in the stock market.
- Business decision makers include creditors (banks, suppliers), investors (stockholders), directors, customers, governments, and other external users.

LO 1-2 Describe the purpose, structure, and content of the four basic financial statements.

- The *income statement* reports the net amount that a business earned (net income) over a period of time by subtracting the costs of running the business (expenses) from the total amount generated by selling its goods and services (revenues).
- The *statement of retained earnings* explains changes in the Retained Earnings account over a period of time by considering increases (from net income) and decreases (from net losses and dividends to stockholders).
- The *balance sheet* reports what the business owns (reported as assets) at a particular point in time and how much of the financing for these assets came from creditors (reported as liabilities) or stockholders (reported as stockholders' equity).
- The *statement of cash flows* explains changes in the cash account over a period of time by reporting inflows and outflows of cash from the business's operating, investing, and financing activities.

LO 1-3 Explain how financial statements are used by decision makers.

- Creditors are mainly interested in assessing whether the company (1) is generating enough cash to make payments on its loan and (2) has enough assets to cover its liabilities. Answers to these questions are indicated by the statement of cash flows and the balance sheet.

CHAPTER SUMMARY (continued):

- Investors look closely at the income statement for information about a company's ability to generate profits, and at the statement of retained earnings for information about a company's dividend distributions.

LO 1-4 Describe factors that contribute to useful financial information.

- Companies generate useful financial information by applying generally accepted accounting principles (GAAP) or International Financial Reporting Standards (IFRS) in an ethical business environment.
- To be useful, information must be relevant and a faithful representation of the economic substance of business activities. Information is more useful when it is timely, verifiable, comparable and understandable.

LO 1-S1 Describe the decision to become a public company and explain the implications for accounting.

- Going public provides a company with additional options for financing and creates additional reporting responsibilities (press releases, financial statement, SEC, etc.).

LO 1-S2 Choose data visualizations appropriate for answering different question types.

- Data visualizations are representations of data using visual displays such as charts, graphs, maps, and plots.
- They often are easily and quickly comprehended and can reveal business insights.

CHAPTER OUTLINE

I. Understand the Business

LO 1-1 Describe various organizational forms and business decision makers.

A. Organizational Forms:
   1. Sole proprietorship—A business owned (and usually operated) by one individual.
   2. Partnership—Similar to a sole proprietorship except that profits, taxes, and legal liability are the responsibility of two or more owners instead of just one.
   3. Corporation—A separate entity from both legal and accounting perspectives. The corporation, not its owners, is legally responsible for its own taxes and debts. Thus, owners cannot lose more than their investment in the corporation.
   Teaching Note: This textbook focuses on corporations.
   4. Other—Other organizational forms exist, such as a limited liability company (LLC), which combines characteristics of a partnership and a corporation.

B. Accounting for Business Decisions
   1. Most companies exist to earn profits for their stockholders; profits are earned by selling goods or services to customers for more than they cost to produce.
   2. **Accounting**—A system of analyzing, recording, and summarizing the results of a business's operating, investing, and financing activities and then reporting them to decision makers.
   3. Business people talk about their companies using accounting terms, making it the "language of business."
   4. Accountants assist in reporting financial information for decision making and to help its owners understand the financial effects of those business decisions.
   5. The accounting system produces two kinds of reports (*Illustrated in Text Exhibit 1.1, p. 1-5*):
      a. Managerial accounting reports—Include detailed financial plans and continually updated reports about the operating performance of the company. These reports are made available only to the company's employees (internal users) for making business decisions.
      b. Financial accounting reports, called **financial statements**—Reports that summarize the financial results of business activities.
         i. Prepared periodically to provide information to people not employed by the business (external users).
         ii. External financial statement users aren't given access to detailed internal records of the company, so they rely extensively on the financial statements.
   6. External users of financial information (*Illustrated in Text Exhibit 1.2, p. 1-6*):
      a. Creditors include suppliers, banks, and anyone to whom money is owed.

b. Investors include existing and potential future stockholders.

c. Directors is the short title for the members of a company's board of directors; elected by stockholders to oversee the company's managers.

d. Government agencies include the Securities and Exchange Commission and the Internal Revenue Service.

II. Study the Accounting Methods

LO 1-2 Describe the purpose, structure, and content of the four basic financial statements.

A. The **Basic Accounting Equation**

Assets = Liabilities + Stockholders' Equity

<u>Teaching Note</u>: "What a company owns must equal what a company owes to its creditors and stockholders."

1. **Separate entity assumption**—A business's financial reports include only the activities of the business and exclude the personal transactions of the owners.
2. Asset—A resource the company controls and expects to benefit from in the future.

<u>Teaching Note</u>: Does company own/have legal rights to it? If yes, will it have benefit beyond the end of the current month? If so, it's an asset.

3. Liabilities—Measurable amounts the company expects to give up in the future to settle what it presently owes to creditors.
4. Stockholders' Equity—Represents the owners' claims on the assets of the business after the creditors' claims have been fulfilled. Owners' claims arise from two sources:
   a. Paid-in capital—The owners have a claim for amounts they contributed directly to the business in exchange for its stock (Common Stock).
   b. Earned capital—The owners have a claim on profits the company has earned for them through its business operations (Retained Earnings).

   <u>Teaching Note</u>: Earned income is particularly important because a business can survive only if it is profitable.

   c. Profits are generated when the total amount earned from selling goods and services is greater than the costs incurred to generate those sales.
      i. Revenues—Earned by selling goods or services to customers.
      ii. Expenses—All costs of doing business that are necessary to earn revenues.

      <u>Teaching Note</u>: Expenses are "incurred" to generate revenues.

      iii. Net Income (preferred term in accounting for profit)—Calculated as revenues minus expenses (net loss if revenues are less than expenses); generating net income increases stockholders' equity.

iv. Dividends—Distribution of a company's profits to its stockholders; reported as a reduction in Retained Earnings.

Teaching Note: Dividends are not an expense "incurred" to generate earnings.

B. Financial Statements (*Summarized in Text Exhibit 1-8, p. 1-15)*

1. Accounting reports prepared at any time during year.
   a. Most commonly monthly, quarterly, and annually using calendar year or fiscal year (a 12-month period ending on a day other than December 31).
   b. Each financial statement has a heading (name of the business, title the report, and the time period covered).
   c. Each major caption has an underlined subtotal; "bottom line" amount has a double underline.
   d. A dollar sign appears only at the top and bottom of each column of numbers.
2. There are four financial statements *(IM Activity Handout 1-1)*:

a. b. **Income statement**—Reports the revenues less expenses of the accounting period; the first (in order) of the four financial statements to be prepared *(Illustrated in Text Exhibit 1.3, p. 1-10)*

Teaching Note: Also commonly referred to as Statement of Income, Statement of Profit and Loss, or Statement of Operations.

i. **Unit of measure assumption**—Financial results of a company's business activities should be measured and reported using a single monetary unit (i.e., US dollar).
ii. **Accounts**—A standardized format that organizations use to accumulate the dollar effects of transactions on each financial statement item.
iii. When listing the accounts on the income statement, revenues are on top, usually with largest, most relevant revenue listed first, then expenses are subtracted, again from largest to smallest, except that Income Tax Expense is the last expense listed.
iv. Net Income is difference between total revenues and total expenses.
v. Single-step income statement format groups revenues separately from expenses and reports a single measure of income.

Teaching Note: Other income statement formats are explained in Chapter 6.

b. **Statement of retained earnings**—Reports the way that net income and the distribution of dividends affected the financial position of the company during the accounting period; the second (in order) of the four financial statements to be prepared *(Illustrated in Text Exhibit 1.4, p. 1-11)*

i. Retained earnings are profits that have accumulated in the company over time.

ii. Retained earnings balance at the beginning of the period + Net income (or – Net loss) – Dividends = Retained earnings balance at end of the period.

c. Balance sheet—Reports the amount of assets, liabilities, and stockholders' equity of a business at a point in time; the third (in order) of the four financial statements to be prepared. *(Illustrated in Text Exhibit 1.5, p. 1-12; <u>IM Activity Handout 1-2</u>)*

<u>Teaching Note</u>: Also commonly referred to as Statement of Financial Position.

i. Assets = Liabilities + Stockholders' equity; the basic accounting equation reflects the business's financial position at a point in time

ii. Assets listed in order of how soon they are to be used or turned into cash. Liabilities listed in order of how soon each is to be paid or settled.

d. **Statement of cash flows**—Reports inflows and outflows of cash during the accounting period in the categories of operating, investing, and financing; the final (in order) of the four financial statements to be prepared. *(Illustrated in Text Exhibit 1.6, p. 1-13; <u>IM Activity Handout 1-3</u>)*

i. ii. iii. Operating—These cash flows arise directly from running the business to earn profit.

iv. Investing—These cash flows arise from buying and selling productive resources with long lives, purchasing investments, and lending to others.

v. Financing—These cash flows include borrowing from banks, repaying bank loans, receiving cash from stockholders for company stock, or paying dividends to stockholders.

e. Notes to the Financial Statements—Help financial statement users understand how the amounts were derived and what other information may affect their decisions.

3. Relationships among the Financial Statements—The four basic financial statements connect to one another: *(Illustrated in Text Exhibit 1.7, p. 1-14; <u>IM Activity Handout 1-4</u>)*

a. Net income, from the income statement, is a component in determining ending Retained Earnings on the statement of retained earnings.

b. Ending Retained Earnings is then reported on the balance sheet.

c. Cash on the balance sheet is equal to the ending Cash reported on the statement of cash flows.

III. Evaluate the Results

LO 1-3 Explain how financial statements are used by decision makers.

A. Using Financial Statements

1. Creditors—Mainly interested in assessing two things:

a. Is the company generating enough cash to pay what it owes? The statement of cash flows helps answer this question.
b. Does the company have enough assets to cover its liabilities? Answers to this question come from comparing assets and liabilities reported on the balance sheet.

2. Investors—Expect a return on their contribution to the company:
   a. Return may be immediate (through dividends) or long-term (through selling stock certificates at a price higher than their original cost).
   b. Investors look closely at the income statement (and statement of retained earnings) for information about the company's ability to generate profits (and distribute dividends).

LO 1-4 Describe factors that contribute to useful financial information.

B. Useful Financial Information

1. **Generally Accepted Accounting Principles (GAAP)**—The rules used in the United States to calculate and report information in the financial statements.
   a. Financial Accounting Standards Board (FASB)—Currently has primary responsibility for setting the underlying rules of accounting in the U.S.
   b. Accounting rules in U.S. are similar to those used elsewhere, with some important differences.

   <u>Teaching Note</u>*: The "Spotlight on the World" features are used to highlight these important differences.*

   c. FASB has been working with the International Accounting Standards Board (IASB) to eliminate differences so that investors can more easily compare the financial statements of companies from different countries.

The "Spotlight on the World" feature (Text p. 1-17) discusses the IFRS.

2. Main goal of GAAP and IFRS is to ensure companies produce financial information that is useful to existing and potential investors, lenders, and other creditors in making decisions about providing resources to the companies.
3. For financial information to be judged useful, it must possess two fundamental characteristics:
   a. Relevance—Information is relevant if it makes a difference in decision making.
   b. Faithful representation—Information is a faithful representation if it fully depicts the economic substance of business activities.
4. Usefulness of financial information is enhanced when it is: *(Illustrated in Text Exhibit 1.9, p. 1-17).*
   a. Timely—It is available in time to influence decision makers.

b. Verifiable—When others, such as external auditors, reach similar values using similar methods.

c. Comparable—The same accounting principles are used over time and across companies.

d. Understandable—Reasonably informed users can comprehend and interpret.

5. To achieve these objectives, the FASB and IASB have developed a framework that outlines the financial elements to be measured and the main external users for whom the financial information is intended.
   a. A company's managers have primary responsibility for following GAAP.
   b. To provide additional assurance, some private companies and all public companies hire independent auditors to scrutinize their financial records.
      i. Following rules approved by the Public Company Accounting Oversight Board (PCAOB) and other accounting bodies, these auditors report whether, beyond reasonable doubt, the financial statements represent what they claim to represent and whether they comply with GAAP.
      ii. In a sense, GAAP is to auditors and accountants what the criminal code is to lawyers and the public.
6. Ethical Conduct
   a. **Ethics**—The standards of conduct for judging right from wrong, honest from dishonest, and fair from unfair.
   b. Intentional misreporting is both unethical and illegal.
   c. The American Institute of Certified Public Accountants (AICPA) requires all its members adhere to a Code of Professional Conduct to help ensure decisions are made in a professional and ethical manner.
   d. Despite this code of conduct, some individuals have been involved in accounting scandals and fraud. *The "Spotlight on Ethics" feature (Text p. 1-19) summarizes various accounting scandals*.
   e. **Sarbanes-Oxley Act (SOX)**—A set of laws established to strengthen corporate reporting in the United States; SOX requires top managers of public companies to:
      i. Sign a report certifying their responsibilities for the financial statements.
      ii. Maintain an audited system of internal controls to ensure accuracy in the accounting reports.
      iii. Maintain an independent committee to ensure that top management cooperates with auditors.
   f. Corporate executives face severe criminal and financial penalties if found guilty of committing accounting fraud.

g. Ethical conduct is just as important for small private businesses as it is for large public companies.
h. When faced with an ethical dilemma, follow a three-step process:
   i. Identify who will benefit from the situation (often the manager or employee) and those who will be harmed (other employees, the company's reputation, owners, creditors, and the public in general).
   ii. Identify and evaluate the alternative courses of action.
   ii. Choose the alternative that is the most ethical; that you would be proud to have reported in the news.

IV. Supplement 1A—Public Companies

LO 1-S1 Describe the decision to become a public company and explain the implications for accounting.

A. Going Public
1. When a company needs more financing than it can access privately, it may choose to issue shares to investors through an initial public offering (IPO) on a public stock exchange.
2. Going public offers many positive outcomes; the public company:
   a. Keeps the money it raises when issuing shares.
   b. Can more easily raise money in the future by issuing additional shares.
   c. Can pay employees using company shares not just cash.
   d. Gives founders and other stockholders a way to sell their shares.
   e. Can buy other companies by paying with shares rather than cash.
3. A company may also go public through a "direct listing" process, in which stockholders (not the company itself) exchange their shares of the company for cash provided by new investors.

B. Public Company Financial Reporting
1. There are downsides to being a public company:
   a. Greater public reporting of significant events affecting the company.
   b. Increased accounting disclosures.
   c. Greater risk of litigation for misstatements in and omissions from these reports.
   d. Required to give frequent updates about business through:
      i. Press Releases-A public company will announce annual (and quarterly) results sent to news agencies typically 3-5 weeks after the accounting period ends; many companies follow up with a conference call broadcast on the Internet allowing analysts to ask questions of senior executives.
      ii. Financial Statement Reports-Complete financial statements are released (several weeks after the press release) as part of an annual (or quarterly)

report posted at its investor relations website.

A typical annual report includes two parts:

(1) A letter to investors from the company's Chief Executive Officer (CEO) with glossy pictures and comments about the company's business.

(2) A financial section. (*The typical elements of the financial section are listed and described in Text Exhibit 1A.1, p. 1-21).*

(3) Securities and Exchange Commission (SEC) Filings-Include Form 10-K (annual) with disclosures, Form 10-Q (quarterly) and Form 8-k (significant business events). (*Timing of significant financial reporting events is shown in Text Exhibit 1A.2, p. 1-22).*

The "Spotlight on Financial Reporting" feature (Text p. 1-21) discusses the current event reporting of COVID-19.

To find SEC filings, click on "Company Filings Search" in the Filings tab at sec.gov.

V. Supplement 1B—Data Visualization

LO 1-S2 Choose data visualizations appropriate for answering different question types.

A. Data Visualizations-Representations of data using visual displays such as charts, graphs, maps, and plots.

1. Visualizations often are easily and quickly comprehended, and can reveal business insights by answering one of the following types of questions:
   a. Comparison-Asks "Is a particular item more (or less)?"
   b. Composition-Asks "What does the item include?"
   c. Association-Asks "Is one item connected to another?"
   d. Distribution-Asks "How are items spread out?"
2. Examples of commonly used data visualizations by question type:
   a. Comparison-Column, Bar, Line, Waterfall, and Deviation charts; *visuals, uses and limitations illustrated and discussed on Text pp. 1-22, 1-23.*
   b. Composition (part-to-whole)-Pie, Donut, Stacked Column, and Treemap charts; *visuals, uses, and limitations illustrated and discussed on Text pp. 1-23, 1-24*.
   c. Association-Scatter plot and Bubble chart; *visuals, uses and limitations illustrated and discussed on Text p. 1-24.*
   d. Distribution-Geospatial and Histogram; *visuals, uses and limitations illustrated and discussed on Text p. 1-25.*
3. A summary of data visualizations by question type and data characteristics is provided on Text p. 1-26.

SUPPLEMENTAL ACTIVITIES / HANDOUTS

The following handouts are suitable for individual or group in-class activities. Solutions are provided immediately following each handout master.

Activity handouts may also be assigned in Connect using the **file attachment assignment** option provided at the **+Add Assignment** tab. To do so, save the handout as a separate file and upload to the Connect assignment you have created. File attachment assignments require manual grading.

1. Handout 1–1
   Handout designed to review the classification of various accounts, elements, or transactions on the financial statements.
2. Handout 1–2
   Handout designed to review the classification of various accounts on the balance sheet.
3. Handout 1–3
   Handout designed to review various cash inflow and outflow transactions and related classifications on the statement of cash flows.
4. Handout 1–4
   Handout designed to review the individual financial statements and the relationships among the financial statements.

HANDOUT 1–1

COMPONENTS OF FINANCIAL STATEMENTS

Identify the financial statement(s) on which each account, element or transaction would be reported.

Account, Element or Transaction	Income Statement	Statement of Retained Earnings	Balance Sheet	Statement of Cash Flows
a. Service Revenue				
b. Cash				
c. Notes Payable				
d. Common Stock				
e. Supplies				
f. The amount of cash collected from customers				
g. Accounts Receivable				
h. Retained earnings				
i. Salaries and Wages Expense				
j. Equipment				
k. Dividends paid to stockholders				
l. Accounts Payable				

<u>HANDOUT 1–1 SOLUTION</u>

COMPONENTS OF FINANCIAL STATEMENTS

Identify the financial statement(s) on which each account, element or transaction would be reported.

Account, Element or Transaction	Income Statement	Statement of Retained Earnings	Balance Sheet	Statement of Cash Flows
a. Service Revenue	X			
b. Cash			X	X
c. Notes Payable			X	
d. Common Stock			X	
e. Supplies			X	
f. The amount of cash collected from customers				X
g. Accounts Receivable			X	
h. Retained earnings		X	X	
i. Salaries and Wages Expense	X			
j. Equipment			X	
k. Dividends paid to stockholders		X		X
l. Accounts Payable			X	

HANDOUT 1–2

BASIC BALANCE SHEET ELEMENTS

For each account, identify its proper classification on the balance sheet.

Account	Asset	Liability	Stockholders' Equity
a. Notes Payable			
b. Cash			
c. Common Stock			
d. Supplies			
e. Accounts Receivable			
f. Accounts Payable			
g. Equipment			
h. Land			
i. Retained Earnings			

HANDOUT 1–2 SOLUTION

BASIC BALANCE SHEET ELEMENTS

For each account, identify its proper classification on the balance sheet.

Account	Asset	Liability	Stockholders' Equity
a. Notes Payable		X	
b. Cash	X		
c. Common Stock			X
d. Supplies	X		
e. Accounts Receivable	X		
f. Accounts Payable		X	
g. Equipment	X		
h. Land	X		
i. Retained Earnings			X

HANDOUT 1–3

STATEMENT OF CASH FLOWS

For each activity, identify as a cash inflow or (outflow) and its proper classification on the statement of cash flows.

Activity	Inflow or (Outflow)	Operating	Investing	Financing
a. Cash paid to employees and suppliers				
b. Cash used to buy equipment and software				
c. Cash dividends paid to stockholders				
d. Cash received from customers				
e. Cash received from selling equipment				
f. Cash borrowed from the bank				
g. Cash from issuing stock				

HANDOUT 1–3 SOLUTION

STATEMENT OF CASH FLOWS

For each activity, identify as a cash inflow or (outflow) and its proper classification on the statement of cash flows.

Activity	Inflow or (Outflow)	Operating	Investing	Financing
a. Cash paid to employees and suppliers	Outflow	X		
b. Cash used to buy equipment and software	Outflow		X	
c. Cash dividends paid to stockholders	Outflow			X
d. Cash received from customers	Inflow	X		
e. Cash received from selling equipment	Inflow		X	
f. Cash borrowed from the bank	Inflow			X
g. Cash from issuing stock	Inflow			X

HANDOUT 1–4

OVERVIEW OF FINANCIAL STATEMENTS

Identify the purpose (i.e., what is measured/reported) and equation used to complete each of the financial statements.

Financial Statement	Purpose	Equation
Income Statement		
Statement of Retained Earnings		
Balance Sheet		
Statement of Cash Flows		

RELATIONSHIPS AMONG FINANCIAL STATEMENTS

Answer the following questions:

1. How does the income statement tie to the statement of retained earnings?

2. How does the statement of retained earnings tie to the balance sheet?

3. How does the balance sheet tie to the statement of cash flows?

HANDOUT 1–4 SOLUTION

OVERVIEW OF FINANCIAL STATEMENTS

Identify the purpose (i.e., what is measured/reported) and equation used to complete each of the financial statements.

Financial Statement	Purpose	Equation
Income Statement	The financial performance of the business during the current accounting period.	Revenues – Expenses = Net Income (Loss)
Statement of Retained Earnings	Earnings retained in the business during the current accounting period added to those of prior periods.	Beginning Retained Earnings + Net Income (this period) – Dividends (this period) = Ending Retained Earnings
Balance Sheet	The financial position of a business at a point in time.	Assets = Liabilities + Stockholders' Equity
Statement of Cash Flows	Activities that caused increases and decreases in cash during the current accounting period.	+/– Operating Cash Flows +/– Investing Cash Flows +/– Financing Cash Flows = Change in Cash + Beginning Cash = Ending Cash

RELATIONSHIPS AMONG FINANCIAL STATEMENTS

Answer the following questions:

1. How does the income statement tie to the statement of retained earnings?

   Net income, from the income statement, is a component in determining ending Retained Earnings on the statement of retained earnings.

2. How does the statement of retained earnings tie to the balance sheet?

   Ending Retained Earnings from the statement of retained earnings is reported on the balance sheet (in the stockholders' equity section).

3. How does the balance sheet tie to the statement of cash flows?

   Cash on the balance sheet is equal to the ending Cash reported on the statement of cash flows.