**Income Statement Exercise: Creating Income Statements**

This exercise will help you to understand how to create an income statement and the difference between **cash-basis and accrual accounting**. The Farm Financial Guidelines recommends that farmers report income for tax purposes using cash-basis, but evaluate farm performance using “accrual adjustments.” This exercise demonstrates how to use information from the past and present period balance sheets to determine how to make accrual adjustments to the income statement.

1. Open the excel file entitled AEC465\_In-Class Assignment\_2
2. Find the worksheet “Balance Sheet” and calculate all necessary accrual adjustments needed. Note, adjustments are needed any time a change in value reflects an implicit change in income. For example, if the quantity of inventory of stored grain has gone up during the year, this suggests “unearned” income in terms of the grain that has been produced during the year but not yet sold.
3. Find the “Income Statement” worksheet and complete all necessary accounting entries to complete a two-column income statement in order to be able to compare cash-basis and accrual-adjusted reporting of income and expenses. The cash-basis income statement is provided, but accrual adjustments must be made, based on information from the balance sheet.

**Income Statement Exercise: Interpretation and Discussion**

In a separate Word document, answer the following two questions,

1. How does the "message" from the income statement change when going from cash basis to accrual-adjusted basis?
2. Interpret the ratios, in terms of liquidity, solvency and profitability

Save the excel file and the Word file using the following file name protocol, and then email your completed files to [jasterns@oregonstate.edu](mailto:jasterns@oregonstate.edu)

Excel file name: Hwk2\_yourlastname.xlsx

Word file name: Hwk2\_yourlastname.docs