

Operating Activities Analysis: Tolito Treats, Inc.

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This paper contains an operating activities analysis, explains cash flow statements, and prepares a statement of cash flows using the indirect method to create Tolito Treats, Inc.'s cash flow statement. A cash flow statement is a financial statement that shows how much cash a business generates and uses in each period. It is divided into operating, investing, and financing activities.

Interpret a cash flow statement to understand the meaning and impact of each section and the net cash flow of each section. Here are some tips:

- Operating activities show the cash inflows and outflows from the core business operations, such as selling goods or services and paying salaries, taxes, or interest. A positive net cash flow from operating activities means that the business is generating enough cash from its operations to cover its expenses and grow its business. A negative net cash flow from operating activities means that the business is spending more cash than it is earning from its operations, which may indicate a problem with its profitability or efficiency.
- Investing activities show the cash inflows and outflows from buying and selling long-term assets, such as property, plant, equipment, or investments. A positive net cash flow from investing activities means that the business is selling more assets than it is buying, which may indicate that it is downsizing, restructuring, or liquidating its assets. A negative net cash flow from investing activities means that the business is buying more assets than it is selling, which may indicate that it is expanding, upgrading, or diversifying its assets.

- Financing activities show the cash inflows and outflows from issuing and repaying debt and equity, such as bonds, loans, stocks, or dividends. A positive net cash flow from financing activities means that the business is raising more capital than it is paying back. This may indicate that it is growing, leveraging, or acquiring other businesses. A negative net cash flow from financing activities means the business is paying back more capital than it is raising. This may indicate that it is reducing its debt, increasing its equity, or distributing its profits to its owners or shareholders.

To get a complete picture of a business's cash flow, add the net cash flows from each section to get the net increase or decrease in cash for the period. Also, compare the net increase or decrease in cash with the change in cash balance from the balance sheet, which shows the cash balance at the beginning and end of the period. The net increase or decrease in cash should match the change in cash balance. Otherwise, there may be an error or a missing transaction in the cash flow statement. There are two methods for preparing a statement of cash flows: direct and indirect.

Direct method: The direct method is a cash-based method that reports cash inflows and outflows from operating activities. Under this method, each line item of the income statement is converted to its cash basis. This method is more accurate than the indirect method because it provides a detailed breakdown of cash inflows and outflows. However, it is more time-consuming and expensive to prepare.

Indirect method: The indirect method is an accrual-based method that starts with net income and makes adjustments based on changes in current assets, current liabilities, and non-cash charges. This method is less accurate than the direct method because it does not provide a

detailed breakdown of cash inflows and outflows. However, it is less time-consuming and less expensive to prepare. The figure below contains Toliyo Treats, Inc.'s balance sheet and income statement from 2013 to 2014.

Figure 1: Tolito Treats, Inc.'s Balance Sheet and Income Statement.

Tolito Treats, Inc. Balance Sheets as of December 31, 2013 and 2014		
<i>Current Aset</i>	2013	2014
Cash	\$ 34,000.00	\$ 34,000.00
Accounts receivable, Net	\$ 12,000.00	\$ 17,000.00
Inventory	\$ 16,000.00	\$ 14,000.00
Long term investment	\$ 6,000.00	-
Fixed Assets	\$ 80,000.00	\$ 93,000.00
Accumulated Depreciation	\$ (48,000.00)	\$ (39,000.00)
Total Assets	\$ 100,000.00	\$ 119,500.00
Account Payable	\$ 19,000.00	\$12,000
Bonds Payable	\$ 10,000.00	\$ 30,000.00
Common Stock	\$ 50,000.00	\$ 61,000.00
Retained Earning	\$ 21,000.00	\$ 28,000.00
Treasure Stock	-	\$ (11,500.00)
Total Liabilities and Equity	\$ 1,000,000.00	\$ 119,500.00
<i>Additional information for the period January 1, 2014 through December 31, 2014.</i>		
Sales on account	\$ 70,000.00	
Purchase on account	\$ 40,000.00	
Depreciation	\$ 5,000.00	
Expenses paid in cash (including \$4,000 of interest and \$6,000 in taxes.	\$ 18,000.00	
Decrease in inventory	\$ 2,000.00	
Sales of fixed assets for \$6,000 cash: cost \$21,000 and two-thirds depreciated (loss or gain is included in income)		
Purchase of fixed assets for cash	\$ 4,000.00	
Fixed Assets are exchanged for bonds payable of	\$ 30,000.00	
Sale of investments for for cash	\$ 9,000.00	
Purchase of treasury stock for cash	11,500.00	
Retire bonds payable by issuing common stock	\$ 10,000.00	
Collections on accounts receivable	\$ 65,000.00	
Sold unissued common stock for cash	\$ 1,000.00	

Figure 2: Tolito Treats, Inc.'s Cash flow statement(indirect methods).

Cash Flow Statement for the Year Ended December 31, 2014	
Cash Flows from Operating Activities	2014
Net Income	\$ 7,000.00
Depreciation Expense	\$ 5,000.00
Changes in Accrued Liability (Expenses)	\$ 4,000.00
Changes in Accounts Recivable	\$ 5,000.00
Changes in Inventory	\$ 2,000.00
Changes in Accounts Payable	\$ (7,000.00)
Loss on Sales of Fixed Assets	\$ 6,000.00
Gain on Sale of Investments	
Purchase of Treasury Stock	\$ (11,500.00)
Collection of Account Receivable	\$ 65,000.00
Net Cash Flow from Operating Activities	\$ 84,500.00
Cash Flows from Investing Activities	
Sales of Fixed Assets	\$ 6,000.00
Purchase of Fixed Assets	\$ (4,000.00)
Sales of Investment	\$ 9,000.00
Net cash Used in Investing Activities	\$ 11,000.00
Cash Flows from Financing Activities	
Purchase of Treasure Stock	\$ (11,500.00)
Insurance of Common Stock for Bonds	
Retirement of Bonds by Issuing Common Stock	\$ 10,000.00
Net Cash Used in Financial Activities	\$ (1,500.00)
Cash Flow Statement for the Year Ended December 31, 2014	
Net Cash Flow from Financing Activities	
Net Change in Cash	\$ 72,000.00
Cash at Beginning of Period (given)	\$ 34,500.00
Cash at End of Period	\$106,500.00

Figure 3: Tolioto Treats, Inc.'s side-by-side comparative statement.

Create a side-by-side comparative statement contrasting two bases of reporting		
Items	Net Income Basis	Cash Flows from Operation Basis
Cash at Beginning	\$ 34,500.00	\$ 34,500.00
Net Cash Provided by Operating Activities	\$ 7,000.00	\$ 84,500.00
Net Cash Used in Investing Activities	-	\$ (11,000.00)
Net Cash Used in Financing Activities	-	\$ (1,500.00)
Net Change in Cash	-	\$ 72,000.00
Cash at End	-	\$ 106,500.00

Explanation:

In 2014, Tolito Treats, Inc. experienced a net increase in cash of \$72,000, as calculated through the indirect method for the Statement of Cash Flows. This significant positive cash flow was primarily driven by operational activities, with net cash provided by operating activities of \$84,500. The company's operating activities included sales, purchases, depreciation, expenses paid in cash, changes in inventory and accounts receivable, sale of fixed assets, and collections on accounts receivable. Investing activities reflected a net cash outflow of \$11,000, primarily due to the sale of fixed assets and the purchase of new assets. On the financing side, a net cash outflow of \$1,500 was recorded, primarily attributed to the purchase of treasury stock and the retirement of bonds through the issuance of common stock.

The side-by-side comparative statement contrasts the outcomes under two bases of reporting: the traditional net income basis and the cash flows from operations basis. While the net income basis focuses on profitability derived from sales, expenses, and other accounting measures, the cash flows from the operations basis emphasize actual cash movements. The comparative statement highlights the importance of considering non-cash items like depreciation and changes in working capital to provide a more accurate representation of a company's liquidity and ability to

generate cash. In Tolito Treats, the positive net income of \$7,000 contrasts with the robust cash flows from operations of \$84,500, showcasing the impact of non-cash adjustments and the significance of cash management in evaluating financial health.

This analysis underscores the necessity of understanding both financial reporting perspectives. It helps stakeholders, such as investors and management, gain insights into how operational activities contribute to the company's overall cash position. Additionally, it provides a clearer picture of the company's financial health by highlighting the nuances between net income and cash flows from operations, enabling more informed decision-making and strategic planning.

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