# Practice Problems – Statement of Cash Flows

**Requirement 1**

Use the following information to prepare the cash flow from operating activities section of the cash flow statement for Bridgewood, Ltd. for 2011, using both the direct and indirect methods. You can use the spreadsheet provided on the next page as a guide in preparing the direct method cash flow from operating activities.



**Cash flow from operating activities (direct method)**

|  |  |  |  |
| --- | --- | --- | --- |
| **Revenue/Expense line item** | **Amount** | **Adjustment to arrive at corresponding cash flow** | **Corresponding cash inflow/outflow** |
| Sales | 850 |  |  |
| Cost of goods sold | (610) |  |  |
| Rent expense | (56) |  |  |
| Depreciation | (22) |  |  |
| Interest expense | (30) |  |  |
| Gain from sale of noncurrent assets | 14 |  |  |
| Tax expense | (41) |  |  |
| Net income | 105 |  |  |

**Requirement 2**

1. Please state the effect of each of the following transactions on the firm’s current-period cash flow from operating, investing, and financing activities. Ignore any effect that the transactions might have on the firm’s tax payments.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
|  |  | CFO | CFI | CFF |
|  | The firm sells equipment for $50,000 this period. The equipment had an original cost of $100,000 and accumulated depreciation of $80,000. |  |  |  |
|  | The firm sells goods to customers for $40,000. The goods that were sold cost the firm $25,000 and were paid for in a prior period. All sales are on account and will be paid next period. |  |  |  |
|  | The firm purchases a building for $2,000,000 this period. The seller provides the financing for the purchase. No payments on the loan are made this period. |  |  |  |
|  | Wage expense of $30,000 is incurred this period. Payments to workers this period totaled $25,000. |  |  |  |
|  | A bank loan for $100,000 was taken out this period. No payments were made on the loan this period. |  |  |  |
|  | Interest of $2,000 and dividends of $1,000 were paid by the firm during the period. |  |  |  |
|  | Customers placed orders for $7,000 of goods to be delivered next period. No payments are made this period. |  |  |  |

1. Ignoring the impact of taxes, is depreciation a source of cash?
2. Do accounting policies affect total cash flows?

### Requirement 3: The following excerpts are from Endo Pharmaceutical’s 2010 10-K:



1. How much cash was collected from customers during 2010? Please use the changes in operating assets and liabilities as listed on the cash flow statement in your calculations. How much different would your answer be in you instead used the changes as given on the balance sheet?
2. Which of these two methods is the correct one to use in calculating cash collected from customers?
3. How much cash was paid to suppliers for inventory? In your calculations, assume that all accounts payable pertain to inventory. Please use the changes in assets and liabilities as given on the cash flow statement, rather than those from the balance sheet.

**Requirement 4**

**Example: Cherokee Inc.**

Use the following information to prepare the operating section of the statement of cash flows for Cherokee, Inc. (NASDAQ: CHKE). The “Related to” column shows the section of the cash flow statement associated with each B/S or I/S line. Assume that there were no sales of either PP&E or trademarks during fiscal 2011.

Please prepare the CFO section using bot he direct and indirect method.

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **CHEROKEE INC - BALANCE SHEET (10-K)** | | |  |  |
|  |  |  |  |  |  |  |
| ($1000s) | **Jan 29, 2011** | **Jan 30, 2010** |  | **Change** |  | **Related to** |
| Current assets: |  |  |  |  |  |  |
| Cash and cash equivalents | $ 9,587 | $ 9,419 |  | $ 168 |  |  |
| Receivables | 6,644 | 6,939 |  | (295) |  | CFO |
| Other current assets | 94 | 101 |  | (7) |  | CFO |
| Deferred tax asset | 2,618 | 2,011 |  | 607 |  | CFO |
| Total current assets | 18,943 | 18,470 |  | 473 |  |  |
| Deferred tax asset | 1,358 | 644 |  | 714 |  | CFO |
| Property and equipment, net | 173 | 185 |  | (12) |  | CFI |
| Trademarks, net | 6,709 | 7,866 |  | (1,157) |  | CFI |
| Total assets | $ 27,183 | $ 27,165 |  | $ 18 |  |  |
|  |  |  |  |  |  |  |
| Current liabilities: |  |  |  |  |  |  |
| Accounts payable | $ 1,867 | $ 967 |  | $ 900 |  | CFO |
| Accrued expenses | 5,298 | 2,536 |  | 2,762 |  | CFO |
| Income taxes payable | 1,857 | 1,260 |  | 597 |  | CFO |
| Accrued dividends | 1,699 | 3,349 |  | (1,650) |  | CFF |
| Promissory note | 7,260 | - |  | 7,260 |  | CFF |
| Total liabilities | 17,981 | 8,112 |  | 9,869 |  |  |
|  |  |  |  |  |  |  |
| Stockholders' Equity |  |  |  |  |  |  |
| Common stock | 177 | 176 |  | 1 |  | CFF |
| Additional paid-in capital | 16,686 | 15,187 |  | 1,499 |  | CFF |
| Retained earnings (deficit) | (401) | 3,690 |  | (4,091) |  | CFO/CFF |
| Less: Treasury stock | (7,260) | - |  | (7,260) |  | CFF |
| Total stockholders' equity | 9,202 | 19,053 |  | (9,851) |  |  |
| Total liabilities and stockholders' equity | 27,183 | 27,165 |  | 18 |  |  |

|  |  |  |
| --- | --- | --- |
| **CHEROKEE INC -INCOME STATEMENT** | |  |
|  |  |  |
|  | **Year ended** |  |
| ($1000s) | **Jan 29, 2011** | **Related to** |
| Royalty revenues | $ 30,777 | Cash from customers |
| SG&A Expenses | 16,322 | Cash to suppliers/employees |
| Depreciation | 75 | Non-cash |
| Amortization of trademarks | 1,474 | Non-cash |
| Operating income | 12,906 |  |
| Interest and other income | 13 | Cash received for interest |
| Income before income taxes | 12,919 |  |
| Income tax provision | 5,200 | Cash paid for taxes |
| Net income | $ 7,719 |  |