

Example: Dave's Car Transport Service

- Dave starts a business to transport expensive cars
- On December 1, 2015
 - Receives \$50,000 cash from issuing common stock
 - Borrows \$80,000 from bank and buys \$100,000 truck
 - Will be used for 48 mos., with a \$4,000 salvage value
 - Pays \$12,000 cash upfront to rent office space for 1 year
- During December
 - Moves two cars, will get paid \$40,000 within 30 days
 - Pays employees \$10,000 of wages
- December 31: Bank wants to see financial statements

Did the company “make money” during December?

Cash Flows

Stock 50,000

Bank 80,000

Truck (100,000)

Rent (12,000)

Wages (10,000)

Customers 0

Cash 8,000

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Did the company “make money” during December?

Cash Flows

Operating

Rent (12,000)

Wages (10,000)

Customers 0

CFO (22,000)

Investing

Truck (100,000)

CFI (100,000)

Financing

Stock 50,000

Bank 80,000

CFF 130,000

Cash 8,000

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Statement of Cash Flows

Dec 2015 Cash Flows

Operating

Rent (12,000)

Wages (10,000)

Customers 0

CFO (22,000)

Investing

Truck (100,000)

CFI (100,000)

Financing

Stock 50,000

Bank 80,000

CFF 130,000

Cash 8,000

- Reports cash transactions *over a period of time*
- Operating Activities
 - Transactions related to the provision of goods or services and other normal business activities
- Investing Activities
 - Transactions related to the acquisition or disposal of long-lived productive assets
- Financing Activities
 - Transactions related to owners or creditors

Did the company “make money” during December?

Accounting Income

Revenue	40,000
Truck Expense	(2,000)
Rent Expense	(1,000)
Wages Expense	<u>(10,000)</u>
Net Income	27,000

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- Pays employees \$10,000 of wages

Notes: Truck expense

(“depreciation”) =
 $(100,000 - 4,000) / 48$

Rent expense is one month at
\$1000/mo.

Income Statement

Dec 2015 Accounting Income

Revenue	40,000
Truck Expense	(2,000)
Rent Expense	(1,000)
Wages Expense	<u>(10,000)</u>
Net Income	27,000

Notes: Truck expense

("depreciation") =
 $(100,000 - 4,000) / 48$

Rent expense is one month at
\$1000/mo.

- Reports results of operations over a period of time using accrual accounting
 - Recognition tied to business activities
 - Revenues
 - Increases in "owners' equity" from providing goods or services
 - Expenses
 - Decreases in "owners' equity" incurred in the process of generating revenues
 - Net Income (or Earnings or Net Profit)
 - = Revenues – Expenses
- => DOES NOT EQUAL CHANGE IN CASH!!!

Did the company “make money” during December?

Dec 2015 Cash Flows

Operating

Rent (12,000)

Wages (10,000)

Customers 0

CFO (22,000)

Investing

Truck (100,000)

CFI (100,000)

Financing

Stock 50,000

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Cash 8,000

Dec 2015 Accounting Income

Revenue 40,000

Truck Expense (2,000)

Rent Expense (1,000)

Wages Expense (10,000)

Net Income 27,000

Notes: Truck expense

(“depreciation”) =

$(100,000 - 4,000) / 48$

Rent expense is one month at
\$1000/mo.

What is financial position at end of the month?

Balance Sheet

Assets

Cash	8,000	(Cash in the bank on 12/31/2015)
Accounts Receivable	40,000	(Cash owed by customers on 12/31/2015)
Prepaid Rent	11,000	(Prepaid for 11 months of future space on 12/31/2015)
Truck	<u>98,000</u>	(100,000 original cost – 2,000 “depreciation”)
Total	157,000	

Liabilities & Stockholder's Equity

Bank Debt	80,000	(Cash owed to the bank on 12/31/2015)
Common Stock	50,000	(Stockholder investment as of 12/31/2015)
Retained Earnings	<u>27,000</u>	(Accounting Net income – Dividends as of 12/31/2015)
Total	157,000	

Balance Sheet

Dec 31, 2015 Balance Sheet

Assets

Cash	8,000
Accounts Receivable	40,000
Prepaid Rent	11,000
Truck	<u>98,000</u>
Total	157,000

Liabilities & Stockholder's Equity

Bank Debt	80,000
Common Stock	50,000
Retained Earnings	<u>27,000</u>
Total	157,000

- Reports financial position (resources and obligations) on a specific date
- Assets
 - Resources owned by a business that are expected to provide future economic benefits
- Liabilities
 - Claims on assets by “creditors” (non-owners) that represent an obligation to make future payment of cash, goods, or services
- Stockholders' Equity (Owners' Equity)
 - Claims on assets by owners of business
 - Contributed Capital (arises from sale of shares)
 - Retained Earnings (arises from operations)

Statement of Stockholders' Equity

- We'll get to this later...