

Quick Question On Cash Flows Part I

Prepare a statement of cash flows using the direct method for the ABC Company. Income was \$40,000 in 1995 and depreciation expense was \$20,000. Analyze the results.

ABC Company
Partial Balance Sheet
December 31, 1995

Assets	12/95	12/94	ANALYSIS: See bottom of page
Cash	\$ 48,000	\$ 20,000	
Accounts Receivable	112,000	82,000	
Inventory	85,000	53,000	
Depreciable Assets (NET)	<u>230,000</u>	<u>250,000</u>	
Total Assets	<u>\$475,000</u>	<u>\$405,000</u>	
Liabilities			
Accounts Payable	\$ 90,000	\$ 70,000	
Notes Payable	<u>135,000</u>	<u>135,000</u>	
Total Liabilities	\$225,000	\$205,000	
Owner's Equity			
Common Stock	\$200,000	\$190,000	
Retained Earnings	<u>50,000</u>	<u>10,000</u>	
Total Owner's Equity	\$250,000	\$200,000	
Total Liabilities and Owner's Equity	<u>\$475,000</u>	<u>\$405,000</u>	

ABC Company
Partial Balance Sheet
December 31, 1995

CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income		\$40,000
Accounts Receivable Increased	(\$30,000)	
Inventory Increased	(32,000)	
Depreciation, a Noncash Expense	20,000	
Accounts Payable Increased	20,000	<u>(22,000)</u>
Cash Flows From Operating Activities		\$18,000
CASH FLOWS FROM FINANCING ACTIVITIES		
Sold Stock		<u>10,000</u>
Net Increase (Decrease)		\$28,000
Cash Beginning of Period		<u>20,000</u>
Cash End of Period		\$48,000

ANALYSIS:

Increases in Accounts Receivable and Inventory were not offset by increases in Accumulated Depreciation and Accounts Payable and as a result, cash flows from operating activity were less than Net Income. Cash increased by an additional \$10,000 because of a sale of Common Stock. A dividend was not paid as indicated by the fact that the change in Retained Earnings equaled income. Depreciable assets were not bought or sold as the decrease in net assets equaled depreciation expense.