SOLUTIONS Learning Goal 16

Solutions to Discussion Questions

1. The purpose of the statement of cash flows is to explain the change in the cash balance between a current balance sheet and the prior sheet. The changes are classified into three main categories.
2. The statement of cash flows classifies the changes in cash into operating activities, investing activities, and financing activities.
3. Operating activities is considered to be the most important part of the statement of cash flows. Operating activities are the central and recurring activities of a business. Operating activities indicate the ability of a business to generate cash from ongoing future efforts.
4. $37,000. The simplest method is to use the following formula and solve for the missing item: beginning balance + positive items – negative items = ending balance.
5. Income statement, statement of owner's equity, balance sheet, statement of cash flows. The are usually prepared in the same order that see here.
6. The net income is needed to complete the statement of owner's equity.
7. The ending balance of owner's equity is needed to confirm the balance on the balance sheet.
8. The change in cash between the current and prior balance sheet is needed to confirm the change explained on the statement of cash flows.

LG 16-1.

	Statement of Cash Flows Activity Type	$ Effect on Cash Flow
a.	Financing	+ $15,000
b.	Investing	(10,000)
c.	Operating	+ 950
d.	Operating	(2,000)
e.	No change in cash	-0-
f.	Operating	+ 4,000
g.	No change in cash	-0-
h.	Operating	+ 500
i.	No change in cash	-0-
j.	Operating*	(500)
k.	Investing	+ 10,000
l.	Investing	(50,000)
m	Financing	+ 50,000
n.	No change in cash	-0-
o.	Investing	+ 15,000
p.	Financing	(5,000)

* Although it may seem that paying interest on a loan (which helps to finance a business) is a financing activity, all interest payments (and receipts) are required to be included as part of operating activities. However, the repayment of the principal of a loan is a financing activity item.

SOLUTIONS Learning Goal 16, continued

LG 16-2.

Murphys Company
Statement of Cash Flows
For the Month Ended November 30, 20XX

Cash flows from operating activities	
Receipts:	
Cash collections from customers	$24,900
Cash from interest received	700
Payments	
Payments for operating expenses	(18,300)
Payments for interest	(1,500)
Increase in cash from operating activities	5,800
Cash flows from investing activities	
Sale of equipment	1,000
Loan collection from customer	6,000
Loan to customer	(12,000)
Purchase of equipment	(10,000)
Decrease in cash from investing activities	(15,000)
Cash flows from financing activities	
Long-term borrowing	15,000
Owner investment	25,000
Owner withdrawals	(5,000)
Increase in cash from financing activities	35,000
Net increase in cash	25,800
Beginning cash balance, November 1	12,300
Ending cash balance, November 30	$38,100

Note: notice that items j, m, and n are non-cash events. Therefore, they would not appear on the statement of cash flows.

LG16-3

a. The revenues and expenses that make up net income do not always affect cash. In other words, there are frequently non-cash revenues and non-cash expenses. Example of non-cash revenue: revenue from a sale on account. Instead of cash increasing, accounts receivable increase. Example of non-cash expense: supplies expense when supplies are used up. Instead of the asset cash decreasing, supplies decrease.

b. As you might expect, both are important, but they focus on different things. Operating cash flow focuses on the ability to predictably generate cash that is used for paying recurring debts, accumulating cash necessary for acquiring assets, and building a cash reserve. Net income focuses on the larger issue of the entire change in the business wealth created for the owner, as a result of operating the business. In other words, net income includes non-cash assets as well as cash, so it affects the entire business wealth.