

# UNIT 10: FINANCIAL ACCOUNTING

**LO 2: PREPARE FINAL ACCOUNTS FOR SOLE TRADERS, PARTNERSHIPS AND LIMITED COAMpanies IN ACCORDANCE WITH APPROPRIATE PRINCIPLES, CONVENTIONS AND STANDARDS**

# UNIT 10: FINANCIAL ACCOUNTING

**D2: COMPARE THE ESSENTIAL FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT TO  
ANALYSE THE DIFFERENCES BETWEEN THEM IN TERMS PURPOSE, STRUCTURE AND CONTENT**

# OVERVIEW

- › Financial statements are the summary reports of a company's financial transactions. They report the end results of accounting activities during a given period of time. Financial statements provide the income or loss and financial position of a company.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › Companies produce a set of financial statements that reflect their business activities and profitability for each accounting period. The three main financial statements are the balance sheet, income statement, and statement of cash flows.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › The cash flow statement shows how well a company is managing its cash to fund its operations and any expansion efforts. In this article, we'll examine the differences between the balance sheet and the income statement.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › The balance sheet shows a company's assets, liabilities, and shareholders' equity. Total assets should equal the total of liabilities and shareholders' equity. The balance sheet shows how a company puts its assets to work and how those assets are financed as listed in the liabilities section.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › Shareholders' equity is the difference between assets and liabilities or the money left over for shareholders if all debts were repaid. Investors and creditors analyze the balance sheet to see how a company's management is putting its resources to work.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › **Current Assets**
- › The top section contains the current assets, which are short-term assets that are typically used up in less than one year.
- › **Long-term Assets**
- › Next on the balance sheet are the long-term assets.



# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › **Current Liabilities**
- › Current liabilities are short-term liabilities for a company that are due within one year.
- › **Long-term Liabilities**
- › Long-term debt consists of loans and financial obligations lasting over one year.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › Shareholders' equity
- › Shareholders' equity is equal to a firm's total assets minus its total liabilities and is helpful in calculating the financial health of a company. Shareholders' equity represents the net value or net worth of a company.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › A firm's revenues, gains, expenses and losses are listed on the **income statement**. Revenue is money earned from a company's normal business operations. The expenses on the income statement are the costs associated with earning the revenue.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › When a company sells one of its assets, it can experience a capital gain or loss. Revenues minus expenses, plus gains minus losses, equal net income or net loss. The dollar amount of net income listed on the income statement is also found on the cash flow statement under the operating activities section.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › The top section of an income statement includes total revenue or sales for the period.
- › Net sales: Revenue and sales are considered the top line for a company since they are located at the top of the income statement.
- › Cost of Goods Sold: COGS are direct costs and are only the expenses involved in the production process.
- › Selling, general, and administrative costs are the other expenditures not directly involved in production.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › Total costs or expenses.
- › Operating income is arrived at after subtracting total expenses from total revenues.
- › Net interest expense represents the cost of debt servicing.
- › Net income is often referred to as net profit or the bottom line since it's the final number and is located at the bottom of the income statement.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › The cash flow statement shows the amount of cash within a company. Items that affect the cash balance are listed on the statement. The first section of the cash flow statement is operating activities, which shows the cash flowing in and out of the company in relation to its business operation.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › The operating activities section also includes net income and the change in dollars of certain accounts listed on the balance sheet. The next section, investing activities, shows cash the company received and spent on a company's capital investments.



# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › The financing activities section shows the inflows and outflows of cash related to the company's issued financial securities, which is also listed on the balance sheet and statement of shareholders' equity

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › A statement of cash flows comprises of three sections:
- › Cash Flows from Operating Activities
- › This section includes cash flows from the principal revenue generation activities such as sale and purchase of goods and services. Cash flows from operating activities can be computed using two methods. One is the Direct Method and the other Indirect Method.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › Cash Flows from Investing Activities
- › Cash flows from investing activities are cash in-flows and out-flows related to activities that are intended to generate income and cash flows in future. This includes cash in-flows and out-flows from sale and purchase of long-term assets.

# FEATURES OF EACH FINANCIAL ACCOUNT STATEMENT

- › Cash Flows from Financing Activities
- › Cash flows from financing activities are the cash flows related to transactions with stockholders and creditors such as issuance of share capital, purchase of treasury stock, dividend payments etc.

# REFERENCES

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