# COMM 217 Midterm Cheat Sheet

chapter 1. $\boxed{A = L + SE}$

Balance sheet -> statement of financial position
↳ measures a company's financial position at a specific time

Company name
Statement of financial position
As at ...
(all figures in $)

Assets
current assets (within 12 months)
Non-current assets (more than 12 months)

Liabilities and Shareholders' equity
Liabilities
Current liabilities (accounts payable, salaries payable, taxes payable, utilities payable)
Non-current liabilities (bank loan payable, notes payable, bonds payable)
Shareholders equity -> common shares (contributed capital)
retained earnings
Total liabilities and shareholders equity

retained earnings = beg. retained earnings + net income/loss (less dividends)

income statement -> statement of earnings
↳ measures the net income for a fiscal year

Company name
Statement of earnings
For the ~~month~~ period ended ...
(all figures in $)

| multi-step | single-step |
|---|---|
| Sales | Revenues & gains |
| Cost of goods sold | Expenses and losses |
| Gross profit | Net income. |
| Operating expenses | |
| Operating income | |
| Non-operating or other | |
| Net income | |

Ⓔ

- statement of cash flows → ~~measures~~ changes in cash 51
- Changes in equity

ch 2.

| DEA |  | CER |  |
|---|---|---|---|
| ↑ | ↓ | ↓ | ↑ |

(dividends
expenses
assets)

(liabilities
equities
revenues)

ch 3. accrual accounting → record entries when they are incurred.

vs cash basis accounting → record entries when cash exchanges hands.

In accrual accounting, your might have an expense that goes over different periods

↳ adjusting entries → putting entries in the right time

accrued revenues or expenses
↳ the event has happened but cash hasn't exchanged hands yet
↳ ex - phone bill
utilities

deffered revenues or expenses
↳ cash is exchanged before the revenue/expense is earned or incurred

defered revenue → liability
received money before providing goods or services

defered expenses → pay for something in advance eg 'rent'
is asset

## Ch 4. Closing entries:

↳ Closing temporary accounts to permanent accounts
↳ resetting the balance for expense and revenue accounts to 0 for the start of the next fiscal period.

Closing entries: 4 steps

1. Close revenues to income summary } closing balance sheet
2. Close expenses to income summary } = net earnings
3. Close income summary to retained earnings
4. Take dividends from retained earnings.

## Chapter 8 - reporting and interpreting cost of sales and inventory.

4 different types of inventory:

- raw materials → items acquired for the purpose of processing into products
- work in process → goods in the process of being manufactured
- finished goods → manufactured goods complete and available for sale
- merchandise → goods held for resale

FOB = freight on board

FOB shipping point = transfer of ownership when inventory leaves seller premises
FOB destination : transfer of ownership upon arrival of inventory at buyer premises.

Cost of Sales equation:

Beginning inventory
+ purchases
= Cost of goods available for sales (COGAS)
− Ending inventory
= Cost of goods sold (COGS)

Or

Beginning inventory
+ Purchases
= COGAS
− COGS
= ending inventory

Errors in measuring ending inventory:

↳ errors in measuring inventory will result in COGS, following year Beginning inventory, and following COGS being misstated. The error will correct itself after the second year.

Year 1: ending inventory overstated (ex: $100 more than it should be) → COGS understated ($100 less than it should be) → retained earnings overstated.

Year 2: beginning inventory overstated → COGS overstated. → net income goes down → retained earnings balance out

There are 2 inventory systems:

- Perpetual inventory system: records are maintained throughout the accounting period.
- Periodic inventory system: ending inventory and COGS are determined at the end of the period.

| | Perpetual | Periodic |
|---|---|---|
| Purchases | Debit inventory<br>Credit cash / AP | Debit Purchases<br>Credit Cash / AP |
| Time of sale | Debit cash / AR<br>Credit Sales revenue<br>Debit COGS<br>Credit inventory | Debit cash / AR<br>Credit sales revenue |
| End of period | No entry | Debit COGS<br>Credit inventory (beginning)<br>Credit purchases<br>Debit inventory (ending)<br>credit COGS. |

2 inventory costing methods to learn:

- FIFO (first in, first out)

+

- Weighted-average -> as you make purchases, you take the average of your per-unit inventory cost.

Each of these methods will result in different ending inventory and COGS.
FIFO will give the same results whether you use a perpetual or periodic system.

Reasons to choose different systems:

• Effect on Net earnings -> FIFO will result in lower COGS and a higher ending inventory (when prices are rising over time) -> use FIFO when managers want to show higher earnings.

• Effect on income taxes -> ~~Weighted~~ Weighted average will result in higher COGS and a lower ending inventory = lower net income = lower income taxes
↳ use ~~weighted~~ weighted average when managers want to defer paying taxes as long as possible

Inventory writedowns / LCNRV (lower of cost and net realizable value)
↳ we don't want to overstate our assets / revenues or understate liabilities / expenses
↳ which is why we choose the lower of cost and net realizable value (NRV) when determining the value of our inventory.

Journal entries for a write-down of inventory:

| | | |
|---|---|---|
| COGS | xxx | |
| inventory | | xxx |

▷ -> (# of units × (cost - Net realizable value)) = xxx

(6)

## ch7: Receivables and bad debts

- Businesses will make sales to customers on account, despite the risk of non-payment.
- This is because they believe that the increased sales will make up for the bad debts
- At the end of each year, management must make an estimate on which debts will not be collected - this is the allowance for doubtful accounts (AFDA) as an adjusting entry

AFDA:

journal entries:

To record bad debt estimates (at year-end as adjusting entries):

| | | |
|---|---|---|
| Bad debt expense | xxx | |
| AFDA | | xxx |

To write off specific accounts (during the year):

| | | |
|---|---|---|
| AFDA | xxx | |
| accounts receivables | | xxx |

Recovery of an account previously written off:

| | | |
|---|---|---|
| Accounts receivables | xxx | |
| AFDA | | xxx |

| | | |
|---|---|---|
| Cash | ~~x~~ xxx | |
| Accounts receivables | | xxx |

On income statements:

Operating expenses

Bad debt expense (xxx)

On Balance sheet:

Current Assets

| | | |
|---|---|---|
| accounts receivable | xxx | → accounts receivable (net) |
| less: AFDA | (xxx) | xxx |

AFDA

| | |
|---|---|
| less: writeoffs | beg. AFDA<br>Bad debt adjustment (x) |
| | desired ending AFDA |

Bank reconciliations

| Ending cash balance on books | Ending cash balance on bank statement |
|---|---|
| Add: Collections by bank<br>less: NSF cheques (insufficient funds)<br>Service charges (bank fees)<br>+/- company errors | add: deposits in transit<br>(s bank delay<br>less: outstanding cheques<br>+/- bank errors |
| Ending cash balance correct = | ending correct cash balance. |

## Ratios:

Ch. 2

**Current Ratio** = Current Assets/Current Liabilities
Indicates a company's ability to meet its current obligations.

Ch. 3

**Total Asset Turnover Ratio** = Sales Revenue/Average Total Assets
Measures the sales generated per dollar of assets. Used to asses a company's effectiveness at controlling current and noncurrent assets.

**Return on Assets (ROA)** = Net Earnings + Interest Expense (net of tax)/Average Total Assets
Measures how much the firm earned for each dollar of investment. How well has management used total invested capital during the period.

Ch. 4

**Earnings Per Share (EPS)** = Net Earnings/Avg. number of common shares outstanding during the period
EPS is reported on the income statement. Used to evaluate the operating performance and profitability of a company.

**Net Profit Margin** = Net Earnings/Net Sales
Measures the amount of net earnings generated from every dollar of sales.

**Return on Equity (ROE)** = Net Earnings/Average Shareholders' Equity
Measures how much the firm earned for each dollar of shareholders' investment.

Ch. 7

**Gross Profit Percentage Ratio** = Gross Profit/Net Sales
Measures the percent of gross profit for each dollar of net sales.

**Receivables Turnover** = Net Sales/Average Net Trade Receivables
Measures how many times average receivables are recorded and collected for the year.

**Average Collection Period** = 365 days/Receivables Turnover
Measures the average time in days it takes a customer to pay its accounts.

Ch. 8

**Inventory Turnover** = Cost of Sales/Average Inventory
Measures how many times average inventory was produced and sold during this period. A higher number indicates that inventory moves more quickly, thus reducing storage and obsolescence costs.

**Average Days to Sell Inventory** = 365 days/Inventory Turnover.
Measures the average number of days it takes the company to sell inventory.