

## Module 3.5: Creating Reports

Depending on the degree of detail that you have set up in our Chart of Accounts, there are a lot of reports that you can create with your accounting software to look at your business dynamics in different ways. The Financial Statements are used by investors, market analysts, and creditors to evaluate a company's financial health and earnings potential. The three major financial statement reports are the balance sheet, profit & loss (income) statement, and statement of cash flows.

- *The Balance Sheet* - provides an overview of assets, liabilities, and stockholders' equity as a snapshot in time
- *The Profit & Loss Statement (or Income Statement)* - primarily focuses on a company's revenues and expenses during a particular period. Once expenses are subtracted from revenues, the statement produces a company's profit figure called net income.
- *The Cash Flow Statement* - measures how well a company generates cash to pay its debt obligations, fund its operating expenses, and fund investments.

*I have added samples of these three reports in the download section, as well as the transcript, to help you follow along.*

### The Balance Sheet

The balance sheet provides an overview of a company's assets, liabilities, and stockholders' equity as a snapshot in time. The date at the top of the balance sheet tells you when the snapshot was taken, which is generally the end of the fiscal year.

### The Balance Sheet Formula

$$\text{Assets} = (\text{Liabilities} + \text{Owner's Equity})$$

This formula is fairly simple to understand. That's because a company has to pay for all the things it owns (assets) by either borrowing money (taking on liabilities) or taking it from investors (issuing shareholder equity). The two sides have to always balance, thus the name.

The balance sheet totals will be calculated already, but here's how you identify them.

- Locate total assets on the balance sheet for the period.
- Total all liabilities, which should be a separate listing on the balance sheet.
- Locate total shareholder's equity and add the number to total liabilities.
- Total assets should equal the total of liabilities and total equity.

The balance sheet identifies how assets are funded, either with liabilities, such as debt, or stockholders' equity, such as retained earnings and additional paid-in capital from the stockholders. Assets are listed on the balance sheet in order of liquidity (which is how fast they can be turned into cash).

The liabilities are listed in the order in which they will be paid. Short-term or current liabilities are expected to be paid within the year, while long-term or non-current liabilities are debts expected to be paid in over one year.

Some examples of items listed on the balance sheet are:

#### Assets

- Cash and cash equivalents are liquid assets, which may include Treasury bills and certificates of deposit.
- Accounts receivables are the amount of money owed to the company by its customers for the sale of its product and service.
- Inventory

#### Liabilities

- Debt including long-term debt
- Wages payable
- Dividends payable

#### Shareholders' Equity

- Shareholders' equity is a company's total assets minus its total liabilities. Shareholders' equity represents the amount of money that would be returned to shareholders if all of the assets were liquidated and all of the company's debt was paid off.
- [Retained earnings](#) are part of shareholders' equity and are the amount of net earnings that were not paid to shareholders as dividends. It is usually saved for future business needs.

### **Example of a Balance Sheet**

Here is a portion of Exxon Mobil Corporation's [\(XOM\) balance sheet](#) as of September 30, 2018.

As you can see,

- Total assets were \$354,628.
- Total liabilities were \$157,797.
- Total equity was \$196,831.

- Total liabilities and equity were \$354,628, which equals the total assets for the period.

<b>Exxon Mobil Corporation</b>	
<b>Condensed Consolidated Balance Sheet</b>	
<i>(million of dollars)</i>	
	<u>Sept. 30, 2018</u>
<b>Assets</b>	
<b>Current assets</b>	
Cash and cash equivalents	5,669
Notes and accounts receivable — net	27,880
Inventories	
Crude oil, products and merchandise	14,617
Materials and supplies	4,144
Other current assets	1,665
<b>Total current assets</b>	<u>53,975</u>
Investments, advances and long-term receivables	40,427
Property, plant and equipment — net	249,153
Other assets, including intangibles — net	11,073
<b>Total assets</b>	<u><u>354,628</u></u>
<b>Liabilities</b>	
<b>Current liabilities</b>	
Notes and loans payable	19,413
Accounts payable and accrued liabilities	41,714
Income taxes payable	4,161
<b>Total current liabilities</b>	<u>65,288</u>
Long-term debt	20,624
Postretirement benefits reserves	21,448
Deferred income tax liabilities	27,084
Long-term obligations to equity companies	4,625
Other long-term obligations	18,728
<b>Total liabilities</b>	<u><u>157,797</u></u>
<b>Commitments and contingencies (Note 3)</b>	
<b>Equity</b>	
Common stock without par value	
(9,000 million shares authorized, 8,019 million shares issued)	15,254
Earnings reinvested	419,155
Accumulated other comprehensive income	(18,370)
Common stock held in treasury	
(3,785 million shares at September 30, 2018 and	
3,780 million shares at December 31, 2017)	(225,674)
ExxonMobil share of equity	(190,365)
Noncontrolling interests	6,466
<b>Total equity</b>	<u>196,831</u>
<b>Total liabilities and equity</b>	<u><u>354,628</u></u>

Although the balance sheet is an invaluable piece of information for investors and analysts, there are some drawbacks. Since it is just a snapshot in time, it can only use the difference between this point and another single point in time in the past. This is why you need all three financial statements to get a clear view of how the business is doing.

## **The Profit & Loss or Income Statement**

Unlike the balance sheet, the profit & loss statement covers a range of time, which is a year for annual financial statements and a quarter for quarterly financial statements. The income statement provides an overview of revenues, expenses, net income and earnings per share. It usually provides two to three years of data for comparison.

### **Income Statement Formula and Calculation**

*Net Income=(Revenue-Expenses)*

- Total all revenue or sales for the period.
- Total all expenses and costs of operating the business.
- Subtract total expenses from revenue to achieve net income or the profit for the period.

So, how do we define revenue and expenses?

### **Types of Revenue**

There are three basis types of revenue. Operating revenue is the revenue earned by selling a company's products or services. For example, the operating revenue for an auto manufacturer would be realized through the production and sale of autos. Operating revenue is generated from the core business activities of a company.

Non-operating revenue is the income earned from non-core business activities. These revenues fall outside the primary function of the business. Some non-operating revenue examples include:

- Interest earned on cash in the bank
- Rental income from a property
- Income from strategic partnerships like royalty payment receipts
- Income from an advertisement display located on the company's property

Other income is the revenue earned from other activities. Other income could include gains from the sale of long-term assets such as land, vehicles, or a subsidiary.

### **Types of Expenses**

Primary expenses are incurred during the process of earning revenue from the primary activity of the business. Expenses include the cost of goods sold (COGS), selling, general and administrative expenses (SG&A), depreciation or amortization, and research and development (R&D). Typical expenses include employee wages, sales commissions, and utilities such as electricity and transportation.

Expenses that are linked to secondary activities include interest paid on loans or debt. Losses from the sale of an asset are also recorded as expenses.

The main purpose of the income statement (profit & loss statement) is to convey details of profitability and the financial results of business activities. However, it can be very effective in showing whether sales or revenue is increasing when compared over multiple periods. Investors can also see how well a company's management is controlling expenses to determine whether a company's efforts in reducing the cost of sales might boost profits over time. Less expenses mean more profit.

### Example of an Income Statement

Here is a portion of Exxon Mobil Corporation's (XOM) income statement as of September 30, 2018.

Exxon Mobil Corporation	
Condensed Consolidated Statement of Income	
<i>(million of dollars)</i>	
	Three months ending <u>Sept. 30, 2018</u>
Revenues and other income	
Sales and other operating revenue	74,187
Income from equity affiliates	1,960
Other income	458
<b>Total revenues and other income</b>	<u><b>76,605</b></u>
Costs and other deductions	
Crude oil and product purchases	41,776
Production and manufacturing expenses	9,097
Selling, general and administrative expenses	2,892
Depreciation and depletion	4,658
Exploration expenses, including dry holes	292
Non-service pension and postretirement benefit expense	307
Interest expense	200
Other taxes and duties	8,303
<b>Total costs and other deductions</b>	<u><b>67,525</b></u>
Income before income taxes	9,080
Income taxes	2,634
Net income including noncontrolling interests	6,446
Net income attributable to noncontrolling interests	206
<b>Net income attributable to ExxonMobil</b>	<u><b>6,240</b></u>

- Total revenues were \$76,605 for the period.
- Total costs were \$67,525.
- Net income or profit was \$6,240.

## **The Cash Flow Statement**

The cash flow statement (CFS) measures how well a company generates cash to pay its debt obligations, fund its operating expenses, and fund investments. The cash flow statement complements the balance sheet and profit & loss/income statement.

### **Data From the Cash Flow Statement**

The CFS allows investors to understand how a company's operations are running, where its money is coming from, and how money is being spent. It also provides insight as to whether a company is on a solid financial footing.

There is no formula, per se, for calculating a cash flow statement. Instead, it contains three sections that report cash flow for the various activities for which a company uses its cash. Those three components are operating, investing and financing activities.

### **Operating Activities**

The operating activities on the Cash Flow Statement include any sources and uses of cash from running the business and selling its products or services. Cash from operations includes any changes made in cash, accounts receivable, depreciation, inventory, and accounts payable. These transactions also include wages, income tax payments, interest payments, rent, and cash receipts from the sale of a product or service.

### **Investing Activities**

Investing activities include any sources and uses of cash from a company's investments into the long-term future of the company. A purchase or sale of an asset, loans made to vendors or received from customers or any payments related to a merger or acquisition is included in this category.

Also, purchases of fixed assets such as property, plant, and equipment (PPE) are included in this section. In short, changes in your equipment, assets, or investments relate to cash from investing.

### **Financing Activities**

Cash from financing activities include the sources of cash from investors or banks, as well as the uses of cash paid to shareholders. Financing activities include debt issuance, equity issuance, stock repurchases, loans, dividends paid, and repayments of debt.

The cash flow statement essentially reconciles the income statement with the balance sheet in three major business activities.

## Example of a Cash Flow Statement

Here is a portion of Exxon Mobil Corporation's ([XOM](#)) cash flow statement as of September 30, 2018. We can see the three areas of the cash flow statement and their results.

Exxon Mobil Corporation Condensed Consolidated Statement of Cash Flows <i>(million of dollars)</i>		Nine months ending Sept. 30, 2018
Cash flow from operating activities		
Net income including noncontrolling interests		15,215
Depreciation and depletion		13,717
Changes in operational working capital, excluding cash and debt		(25)
All other items — net		(1,500)
<b>Net cash provided by operating activities</b>		<b>27,407</b>
Cash flows from investing activities		
Additions to property, plant and equipment		(13,480)
Proceeds associated with sales of subsidiaries, property, plant and equipment, and sales and returns of investments		3,239
Additional investments and advances		(1,113)
Other investing activities including collections of advances		492
<b>Net cash used in investing activities</b>		<b>(10,862)</b>
Cash flows from financing activities		
Additions to long-term debt		-
Additions to short-term debt		-
Reductions in short-term debt		(4,279)
Additions/(reductions) in commercial paper, and debt with three months or less maturity <i>(1)</i>		1,626
Cash dividends to ExxonMobil shareholders		(10,296)
Cash dividends to noncontrolling interests		(192)
Changes in noncontrolling interests		(374)
Common stock acquired		(430)
<b>Net cash used in financing activities</b>		<b>(13,945)</b>
Effects of exchange rate changes on cash		(108)
Increase/(decrease) in cash and cash equivalents		2,492
Cash and cash equivalents at beginning of period		3,177
Cash and cash equivalents at end of period		5,669

- Operating activities generated a positive cash flow of \$27,407 for the period.
- Investing activities generated negative cash flow or cash outflows of -\$10,862 for the period. Additions to property, plant, and equipment made up the majority of cash outflows, which means the company invested in new fixed assets.
- Financing activities generated negative cash flow or cash outflows of -\$13,945 for the period. Reductions in short-term debt and dividends paid out made up the majority of the cash outflows.

By reviewing your financial reports on a monthly, quarterly and annual basis, it will give you the data you need to make adjustments to your business before you lose any profits you have worked so hard to achieve.

And when it comes to tax preparation time, printing out a *detailed* profit & loss/income statement will list the totals of all of your active accounts and make it a whole lot easier to prepare an accurate return and pay the least amount of legal tax obligations.

Finally, although financial statements provide a wealth of information on a company, they do have limitations. The statements are open to interpretation, and as a result, investors often draw vastly different conclusions about a company's financial performance.

For example, some investors might want stock repurchases while other investors might prefer to see that money invested in long-term assets. A company's debt level might be fine for one investor while another might have concerns about the level of debt for the company. When analyzing financial statements, it's important to compare multiple periods to determine if there are any trends as well as compare the company's results its peers in the same industry.

While these reports may not seem important when you are just starting out your company, they can give you vital information when it starts growing. That's why I always recommend getting comfortable with them now, so you don't miss something later.