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**The Statement of Cash Flows—  
Direct Method**

**DEMONSTRATION PROBLEM**

The financial statements of Bolero Corporation follow.

**Bolero Corporation**  
**Income Statement**  
**For Year Ended June 30, 2005**

<i>Revenue from Sales:</i>				
<i>Sales</i>			\$570,960.00	
<i>Less Sales Returns and Allowances</i>			12,960.00	
<i>Net Sales</i>				\$558,000.00
<i>Cost of Good Sold:</i>				
<i>Merchandise Inventory, July 1, 2004</i>			\$163,200.00	
<i>Purchases</i>		\$372,720.00		
<i>Less: Purchases Returns and Allowances</i>	\$6,360.00			
<i>Purchases Discounts</i>	5,520.00	11,880.00		
<i>Net Purchases</i>		\$360,840.00		
<i>Add Freight In</i>		18,360.00		
<i>Delivered Cost of Purchases</i>			379,200.00	
<i>Cost of Goods Available for Sale</i>			\$542,400.00	
<i>Less Merchandise Inventory, June 30, 2005</i>			170,400.00	
<i>Cost of Good Sold</i>				372,000.00
<i>Gross Profit</i>				\$186,000.00
<i>Operating Expenses:</i>				
<i>Salary Expense</i>			\$ 88,200.00	
<i>Payroll Tax Expense</i>			9,780.00	
<i>Advertising Expense</i>			4,260.00	
<i>Depreciation Expense, Building</i>			14,400.00	
<i>Depreciation Expense, Equipment</i>			8,400.00	
<i>Supplies Expense</i>			1,920.00	
<i>Insurance Expense</i>			1,260.00	
<i>Miscellaneous Expense</i>			840.00	
<i>Total Operating Expenses</i>				129,060.00
<i>Income from Operations</i>				\$ 56,940.00
<i>Other Income:</i>				
<i>Interest Income</i>			\$ 840.00	
<i>Other Expenses:</i>				
<i>Interest Expense</i>			12,000.00	11,160.00
<i>Income Before Income Taxes</i>				\$ 45,780.00
<i>Income Tax Expense</i>				11,880.00
<i>Net Income</i>				\$ 33,900.00

**Bolero Corporation**  
**Statement of Retained Earnings**  
**For Year Ended June 30, 2005**

<i>Unappropriated Retained Earnings</i>			
<i>Unappropriated Retained Earnings,</i>			
<i>July 1, 2004</i>	<i>\$35,640.00</i>		
<i>Net Income for the Year</i>	<i>33,900.00</i>	<i>\$69,540.00</i>	
<i>Less: Cash Dividends Declared</i>	<i>\$15,600.00</i>		
<i>Transfer to Appropriations for Plant</i>			
<i>Expansion (see below)</i>	<i>6,000.00</i>	<i>21,600.00</i>	
<i>Unappropriated Retained Earnings,</i>			
<i>June 30, 2005</i>			<i>\$47,940.00</i>
<i>Appropriated Retained Earnings:</i>			
<i>Appropriated for Plant Expansion</i>			
<i>July 1, 2004</i>		<i>\$24,000.00</i>	
<i>Add Appropriation for the Year (see above)</i>		<i>6,000.00</i>	
<i>Retained Earnings Appropriated,</i>			
<i>June 30, 2005</i>			<i>30,000.00</i>
<i>Total Retained Earnings</i>			<i>\$77,940.00</i>

**Bolero Corporation**  
**Comparative Balance Sheet**  
**June 30, 2005 and June 30, 2004**

	2005	2004	Increase or (Decrease)
<i>Assets</i>			
Cash	\$ 29,820.00	\$ 22,020.00	\$ 7,800.00
Notes Receivable	0.00	10,800.00	( 10,800.00)
Accounts Receivable (net)	56,700.00	37,440.00	19,260.00
Subscriptions Receivable, Common Stock	28,860.00	0.00	28,860.00
Merchandise Inventory	170,400.00	163,200.00	7,200.00
Supplies	360.00	240.00	120.00
Prepaid Insurance	180.00	420.00	( 240.00)
Land	37,200.00	37,200.00	0.00
Building	264,000.00	264,000.00	0.00
Less Accumulated Depreciation	( 129,600.00)	( 115,200.00)	( 14,400.00)
Equipment	44,400.00	44,400.00	0.00
Less Accumulated Depreciation	( 25,200.00)	( 16,800.00)	( 8,400.00)
<b>Total Assets</b>	<b>\$477,120.00</b>	<b>\$447,720.00</b>	<b>\$29,400.00</b>
<i>Liabilities</i>			
Accounts Payable	\$ 35,220.00	\$ 51,360.00	(\$16,140.00)
Salaries Payable	2,520.00	2,940.00	( 420.00)
Income Tax Payable	1,140.00	840.00	300.00
Interest Payable	1,320.00	1,560.00	( 240.00)
Mortgage Payable	129,600.00	136,800.00	( 7,200.00)
<b>Total Liabilities</b>	<b>\$169,800.00</b>	<b>\$193,500.00</b>	<b>(\$23,700.00)</b>
<i>Stockholder's Equity</i>			
Common Stock	\$172,200.00	\$166,800.00	\$ 5,400.00
Common Stock Subscribed	25,860.00	0.00	25,860.00
Paid-in Capital in Excess of Par Value	31,320.00	27,780.00	3,540.00
Unappropriated Retained Earnings	47,940.00	35,640.00	12,300.00
Retained Earnings Appropriated for			
Plant Expansion	30,000.00	24,000.00	6,000.00
<b>Total Stockholders' Equity</b>	<b>\$307,320.00</b>	<b>\$254,220.00</b>	<b>\$53,100.00</b>
<b>Total Liabilities and Stockholders' Equity</b>	<b>\$477,120.00</b>	<b>\$447,720.00</b>	<b>\$29,400.00</b>

Transactions recorded:

- a. Paid \$7,200 on the principal plus \$12,000 interest on the mortgage.
- b. Collected note receivable, \$10,800, plus \$840 interest.
- c. Received subscription for common stock, \$34,800, having a par value of \$31,260.
- d. Received \$5,940 from subscribers of common stock, having a par value of \$5,400, and issued the stock.

**Instructions**

Prepare a statement of cash flows.

## SOLUTION

### Cash Receipts from Customers:

Net Sales		\$558,000
+ <u>Beginning Accounts Receivable</u>	+	<u>37,440</u>
= Total		\$595,440
- <u>Ending Accounts Receivable</u>	-	<u>56,700</u>
= Cash Receipts from Customers		<u>\$538,740</u>

### Cash Payments for Merchandise Purchases:

Delivered Cost of Purchases		\$379,200
+ <u>Beginning Accounts Payable</u>	+	<u>51,360</u>
= Total		\$430,560
- <u>Ending Accounts Payable</u>	-	<u>35,220</u>
= Cash Payments for Merchandise Purchases		<u>\$395,340</u>

### Cash Payments to Employees:

Salary Expense		\$ 88,200
+ <u>Beginning Salaries Payable</u>	+	<u>2,940</u>
= Total		\$ 91,140
- <u>Ending Salaries Payable</u>	-	<u>2,520</u>
= Cash Payments to Employees		<u>\$ 88,620</u>

### Cash Payments for Supplies:

Supplies Expense		\$ 1,920
+ <u>Ending Supplies</u>	+	<u>360</u>
= Total		\$ 2,280
- <u>Beginning Supplies</u>	-	<u>240</u>
= Cash Payments for Supplies		<u>\$ 2,040</u>

### Cash Payments for Insurance:

Insurance Expense		\$ 1,260
+ <u>Ending Prepaid Insurance</u>	+	<u>180</u>
= Total		\$ 1,440
- <u>Beginning Prepaid Insurance</u>	-	<u>420</u>
= Cash Payments for Insurance		<u>\$ 1,020</u>

### Cash Payments for Interest:

Interest Expense		\$ 12,000
+ <u>Beginning Interest Payable</u>	+	<u>1,560</u>
= Total		\$ 13,560
- <u>Ending Interest Payable</u>	-	<u>1,320</u>
= Cash Payments for Interest		<u>\$ 12,240</u>

### Cash Payments for Income Taxes:

Income Tax Expense		\$ 11,880
+ <u>Beginning Income Tax Payable</u>	+	<u>840</u>
= Total		\$ 12,720
- <u>Ending Income Tax Payable</u>	-	<u>1,140</u>
= Cash Payments for Income Taxes		<u>\$ 11,580</u>

**SOLUTION (continued)**

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	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	
1	2004					1
2	a.	<i>Mortgage Payable</i>		7,200.00		2
3		<i>Interest Expense</i>		12,000.00		3
4		<i>Cash</i>			19,200.00	4
5						5
6	b.	<i>Cash</i>		11,640.00		6
7		<i>Notes Receivable</i>			10,800.00	7
8		<i>Interest Income</i>			840.00	8
9						9
10	c.	<i>Subscriptions Receivable, Common Stock</i>		34,800.00		10
11		<i>Common Stock Subscribed</i>			31,260.00	11
12		<i>Paid-in Capital in Excess of Par Value</i>			3,540.00	12
13						13
14	d.	<i>Cash</i>		5,940.00		14
15		<i>Subscriptions Receivable, Common</i>				15
16		<i>Stock</i>			5,940.00	16
17						17
18		<i>Common Stock Subscribed</i>		5,400.00		18
19		<i>Common Stock</i>			5,400.00	19
20						20

**SOLUTION (continued)**

**Bolero Corporation**  
**Statement of Cash Flows**  
**For Year Ended June 30, 2005**

<i>Cash Flows from (used by) Operating Activities:</i>			
<i>Cash Receipts from:</i>			
<i>Customers</i>		\$538,740.00	
<i>Interest</i>		840.00	
<i>Total Cash Receipts</i>			\$539,580.00
<i>Cash Payments for:</i>			
<i>Merchandise Purchases</i>		\$395,340.00	
<i>Operating Expenses:</i>			
<i>Employees</i>	\$88,620.00		
<i>Payroll Taxes</i>	9,780.00		
<i>Advertising</i>	4,260.00		
<i>Supplies</i>	2,040.00		
<i>Insurance</i>	1,020.00		
<i>Miscellaneous</i>	840.00		
<i>Total</i>		106,560.00	
<i>Interest</i>		12,240.00	
<i>Income Taxes</i>		11,580.00	
<i>Total Cash Payments</i>			525,720.00
<i>Net Cash Flows from Operating Activities</i>			\$ 13,860.00
<i>Cash Flows from (used by) Investing Activities:</i>			
<i>Proceeds of Notes Receivable</i>		\$ 10,800.00	
<i>Net Cash Flows from Investing Activities</i>			10,800.00
<i>Cash Flows from (used by) Financing Activities:</i>			
<i>Repayment of Mortgage</i>		(\$ 7,200.00)	
<i>Issuance of Common Stock</i>		5,940.00	
<i>Payment of Dividends</i>		( 15,600.00)	
<i>Net Cash Flow used by Financing Activities</i>			( 16,860.00)
<i>Net Increase (Decrease) in Cash</i>			\$ 7,800.00