# Multiple Step Income Statement & Comprehensive Income

**Income Statements**
(In millions, except earnings per share)

| | Years Ended June 30 | |
|---|---|---|
| | 2013 | 2012 |
| **Income from Continuing Operations** | | |
| Sales revenue | $1,450.6 | $1,380.0 |
| Cost of goods sold | 832.6 | 800.4 |
| Gross profit | 618.0 | 579.6 |
| Operating expenses: | | |
| Selling | 123.5 | 110.5 |
| General and administrative | 147.8 | 139.1 |
| Research and development | 55.0 | 65.0 |
| Restructuring costs | 125.0 | — |
| Total operating expenses | 451.3 | 314.6 |
| Operating income | 166.7 | 265.0 |
| Non-OP items → Other income (expense): | | |
| Interest income | 12.4 | 11.1 |
| Interest expense | (25.9) | (24.8) |
| Gain on sale of investments | 18.0 | 19.0 |
| Income from continuing operations before income taxes and extraordinary item | 171.2 | 270.3 |
| Income tax expense | 59.9 | 94.6 |
| Income from continuing operations before extraordinary item | 111.3 | 175.7 |
| **Separately Reported Items** | | |
| Discontinued operations: | | |
| Loss from operations of discontinued component (including gain on disposal in 2013 of $47) | (7.6) | (45.7) |
| Income tax benefit | 2.0 | 13.0 |
| Loss on discontinued operations | (5.6) | (32.7) |
| Income before extraordinary item | 105.7 | 143.0 |
| Extraordinary gain, net of $11 in income tax expense | — | 22.0 |
| Net income | $ 105.7 | $ 165.0 |
| **Earnings per Share** | | |
| **Earnings per common share—basic:** | | |
| Income from continuing operations before extraordinary item | $ 2.14 | $ 3.38 |
| Discontinued operations | (.11) | (.62) |
| Extraordinary gain | — | .42 |
| Net income | $ 2.03 | $ 3.18 |
| **Earnings per common share—diluted:** | | |
| Income from continuing operations before extraordinary item | $ 2.06 | $ 3.25 |
| Discontinued operations | (.11) | (.62) |
| Extraordinary gain | — | .42 |
| Net income | $ 1.95 | $ 3.05 |

**An income statement for a hypothetical manufacturing co. that you can refer to as we proceed through the chapter.**

**Objective: to gain a general perspective of the items reported and classifications contained in corporate income statements.**

Note: Income Statement is also called Statement of Earnings

Dividend revenue: other income

# Operating versus Non-operating Income

**Operating Income**

**Includes revenues and expenses directly related to the principal revenue-generating activities of the company (e.g., gains or losses from selling equipment & other assets used in generating the revenue)**

**Non-operating Income**

**Includes certain gains and losses related to peripheral or incidental activities of the company (e.g., selling investment; special gains & losses that are infrequent or unusual, but not both.)**

# Income Statement (Single-Step)

Proper Heading

Revenues & Gains

Expenses & Losses

**MAXWELL GEAR CORPORATION**
**Income Statement**
**For the Year Ended December 31, 2013**

| | | |
|---|---|---|
| Revenues and gains: | | |
| Sales | | $573,522 |
| Interest and dividends | | 26,400 |
| Gain on sale of investments | | 5,500 |
| Total revenues and gains | | 605,422 |
| Expenses and losses: | | |
| Cost of goods sold | $302,371 | |
| Selling | 47,341 | |
| General and administrative | 24,888 | |
| Research and development | 16,300 | |
| Interest | 14,522 | |
| Total expenses and losses | | 405,422 |
| Income before income taxes | | 200,000 |
| Income tax expense | | 80,000 |
| Net income | | $120,000 |

# Income Statement (Multiple-Step)

Proper Heading

Gross Profit

Operating Expenses

Non-operating Items

**MAXWELL GEAR CORPORATION**
**Income Statement**
**For the Year Ended December 31, 2013**

| | | |
|---|---|---|
| Sales revenue | | $573,522 |
| Cost of goods sold | | 302,371 |
| Gross profit | | 271,151 |
| Operating expenses: | | |
| Selling | $47,341 | |
| General and administrative | 24,888 | |
| Research and development | 16,300 | |
| Total operating expenses | | 88,529 |
| Operating income | | 182,622 |
| Other income (expense): | | |
| Interest and dividend revenue | 26,400 | |
| Gain on sale of investments | 5,500 | |
| Interest expense | (14,522) | |
| Total other income, net | | 17,378 |
| Income before income taxes | | 200,000 |
| Income tax expense | | 80,000 |
| Net income | | $120,000 |

**or, Provision for income tax (T)**
**Current**
**Deferred**

**next item: Income from Cont OP**

**After that: Gain(loss) from Disc OP (prior to Net income). After Net income: OCI & then EPS, see PPT 1**

# U. S. GAAP vs. IFRS

**There are more similarities than differences between income statements prepared according to U.S. GAAP and those prepared applying IFRS.**
**Some differences are highlighted below.**

- Has no minimum requirements.
- SEC requires that **expenses** be classified by **function** (cost of goods sold, general & admin…).
- "Bottom line" called **net income or net loss.**
- Report **extraordinary items** **separately**.

- Specifies certain minimum information to be reported on the face of the income statement.
- Allows **expenses** classified by **function** or **natural description** (salaries, rent…).
- "Bottom line" called **profit or loss**.
- **Prohibits** reporting **extraordinary items**.

# Reporting Irregular Items

**Irregular items** fall into 6 categories

1. Discontinued operations.
2. Extraordinary items.
3. Unusual gains and losses.
4. Changes in accounting principle.
5. Changes in estimates.
6. Corrections of errors.

*LO 4 Explain how to report irregular items.*

# Discontinued Operations

**As part of the continuing process to converge U.S. GAAP and international standards, the FASB and IASB have been working together to develop a common definition and a common set of disclosures for discontinued operations.**

**The proposed ASU (Accounting Standards Updates) defines a discontinued operation** as a **"component"** that **either (a) has been disposed of or (b) is classified as held for sale, & represents one of the following:**

**1. a separate major line of business or major geographical area of operations, or**

**2. part of a single coordinated plan to dispose** of **a separate major line of business** or **geographical area of operations, or**

**3. a business that meets the criteria to be classified as held for sale on acquisition.**

# Reporting Discontinued Operations

## Reporting for Components Sold

1. Income or loss from operations of the component from the beginning of the reporting period to the disposal date.

2. Gain or loss on the disposal of the component's assets.

## Reporting for Components Held For Sale

1. Income or loss from **operations** of the component from the beginning of the reporting period to the end of the reporting period.

2. An "**impairment loss**"
- if asset's **carrying value** (book value) **>** ("fair value - cost to sell", i.e., **net realizable value**).
- 1 & 2 can be combined **or** separately reported.
- If combined, the impairment loss must be disclosed.

# Reporting Discontinued Operations

**Example:** ABC Corporation had after tax income from continuing operations of $55,000,000 for the year. During the year, it disposed of its restaurant division at a pretax loss of $270,000. Prior to disposal, the division operated at a pretax loss of $450,000 for the year. Assume a tax rate of 30%. Prepare a partial income statement for ABC.

| | |
|---|---|
| Income from continuing operations | $55,000,000 |
| Discontinued operations: | |
| Loss from operations, net of $135,000 tax | 315,000 |
| Loss on disposal, net of $81,000 tax | 189,000 |
| Total loss on discontinued operations | 504,000 |
| Net income | $54,496,000 |

# Reporting Discontinued Operations

**Discontinued Operations** are reported after "Income from continuing operations."

| **Income Statement** (in thousands) | |
|---|---|
| **Sales** | $285,000 |
| Cost of goods sold | 149,000 |
| Gross profit | 136,000 |
| Interest expense | (21,000) |
| Total other | (4,000) |
| Income before taxes | 79,000 |
| Income tax expense | 24,000 |
| Income from continuing operations | 55,000 |
| Discontinued operations: | |
| Loss from operations, net of tax | **315** |
| Loss on disposal, net of tax | **189** |
| Total loss on discontinued operations | **504** |
| Net income | $ 54,496 |

Previously labeled as "Net Income".

Moved to

# Special Reporting Issues

## Comprehensive Income (covered in Section 2)

**Comprehensive Income:** is the changes in equity during a period from **nonowner sources**.

**Excludes**: those resulting from investments by owners and distributions to owners. It is a broader measure of the effects of all recognized changes except investments by and distributions to owners.

**Includes**: all gains and losses that **bypass net income** but **affect stockholders' equity**; i.e., other comprehensive income (e.g., unrealized gains or losses from Held-to-maturity Securities) .

Notes: Earnings or net income is a measure of entity performance, the extent to which asset inflows (revenues & gains) exceed asset outflows (expense & losses) during the period.

# Special Reporting Issues

## Comprehensive Income

| **Income Statement** (in thousands) | |
|---|---|
| **Sales** | $ 285,000 |
| Cost of goods sold | 149,000 |
| Gross profit | 136,000 |
| **Operating expenses:** | |
| Selling expenses | 10,000 |
| Administrative expenses | 43,000 |
| Total operating expense | 53,000 |
| **Income from operations** | 83,000 |
| **Other revenue (expense):** | |
| Interest revenue | 17,000 |
| Interest expense | (21,000) |
| Total other | (4,000) |
| Income before taxes | 79,000 |
| Income tax expense | 24,000 |
| **Net income** | $ 55,000 |

+

**Other Comprehensive Income**

- Unrealized gains and losses on available-for-sale securities.
- Translation gains and losses on foreign currency.
- Deferred gains & losses from derivatives
- Pension adjustments.

Reported in Stockholders' Equity

**PBO > Expected: Loss** **PBO < Expected: Gain**
**Return on Plan Assets > Expected: Gain** **Return on Plan Assets < Expected: Loss**
These Gains and Losses are **not** reported as "Pension Expense", instead, they **are** reported as **OCI**, a shareholder equity account.

# Special Reporting Issues

## Review

Gains and losses that bypass net income but affect stockholders' equity are referred to as

a. comprehensive income.

b. other comprehensive income.

c. prior period income.

d. unusual gains and losses.

# Special Reporting Issues

Companies must display the components of other comprehensive income in one of three ways:

1. A 2nd separate income statement;
2. A combined income statement of comprehensive income; or
3. As part of the statement of stockholders' equity

# Special Reporting Issues

## Comprehensive Income

2nd income statement

**V. GILL INC.**
**INCOME STATEMENT**
**FOR THE YEAR ENDED DECEMBER 31, 2012**

| | |
|---|---|
| Sales revenue | $800,000 |
| Cost of goods sold | 600,000 |
| Gross profit | 200,000 |
| Operating expenses | 90,000 |
| Net income | $110,000 |

**V. GILL INC.**
**COMPREHENSIVE INCOME STATEMENT**
**FOR THE YEAR ENDED DECEMBER 31, 2012**

| | |
|---|---|
| Net income | $110,000 |
| Other comprehensive income | |
| Unrealized holding gain, net of tax | 30,000 |
| Comprehensive income | $140,000 |

# Special Reporting Issues

## Comprehensive Income

Combined statement

V. Gill Inc.

Combined Statement of Comprehensive Income

For the Year Ended December 31, 2012

| | |
|---|---|
| Sales revenue | $ 800,000 |
| Cost of goods sold | 600,000 |
| Gross profit | 200,000 |
| Operating expenses | 90,000 |
| Net income | 110,000 |
| Other comprehensive income → Unrealized holding gain, net of tax | 30,000 |
| Comprehensive income | $ 140,000 |

# Special Reporting Issues

**Comprehensive Income** – As part of

Statement of Stockholder's Equity

| | |
|---|---|
| **V. Gill Inc.** | |
| **Statement of Stockholders' Equity** | |
| **For the Year Ended December 31, 2012** | |
| | |
| **Retained Earning - Beginning balance** | **60,000** |
| **Net income** | **110,000** |
| **Dividend** | **-10,000** |
| **Retained Earning - Ending balance** | **160,000** |
| **Accumulated Other Comprehensive Income** | **90,000** |

NOT: Net of Taxes

(assuming $90,000 AOCI includes $30,000 OCI).

# Special Reporting Issues

## **Comprehensive Income** – Balance Sheet Presentation

**V. GILL INC.**
**BALANCE SHEET**
**AS OF DECEMBER 31, 2012**
**(STOCKHOLDERS' EQUITY SECTION)**

| | |
|---|---|
| Stockholders' equity | |
| Common stock | $300,000 |
| Retained earnings | 160,000 |
| Accumulated other comprehensive income | 90,000 |
| Total stockholders' equity | $550,000 |

Regardless of the display format used, the *accumulated other comprehensive income* of $90,000 is reported in the stockholders' equity section of the balance sheet.

# Other Comprehensive Income

**Comprehensive income includes traditional net income as well as following 4 additional gains and losses that change shareholders' equity:**

| | | ($ in millions) | |
|---|---|---|---|
| | Net income | | $xxx |
| | Other comprehensive income: | | |
| 3 N | Net unrealized holding gains (losses) on investments (net of tax)* | $x | |
| 2 E | Gains (losses) from and amendments to postretirement benefit plans (net of tax)† | (x) | |
| 1 D | Deferred gains (losses) from derivatives (net of tax)‡ | (x) | |
| 4 T | Gains (losses) from foreign currency translation (net of tax)§ | x | xx |
| | Comprehensive income | | $xxx |

*Changes in the market value of certain investments ().

†Gains and losses due to revising assumptions or market returns differing from expectations and prior service cost from amending the plan ().

‡When a derivative designated as a cash flow hedge is adjusted to fair value, the gain or loss is deferred as a component of comprehensive income and included in earnings later, at the same time as earnings are affected by the hedged transaction ().

§Gains or losses from changes in foreign currency exchange rates. The amount could be an addition to or reduction in shareholders' equity. ()

# U. S. GAAP vs. IFRS

Both U.S. GAAP and IFRS allow companies to report comprehensive income in either a single statement of comprehensive income or in two separate statements. Other comprehensive income items are similar under the two sets of standards.

- Includes four possible Other Comprehensive Income items.

- Includes same four.
- Includes a fifth possible item, changes in revaluation surplus, from the optional revaluation of property, plant, and equipment & intangible assets.

# Accumulated Other Comprehensive Income

**In addition to reporting comprehensive income that occurs in the current period, we must also report these amounts on a cumulative basis in the balance sheet as an additional component of shareholders' equity.**

This is consistent with the way we report net income that occurs in the current reporting period in the income statement and also report accumulated net income (that hasn't been distributed as dividends) in the balance sheet as retained earnings. Similarly, we report OCI as it occurs in the current reporting period and also report accumulated other comprehensive income (AOCI) in the balance sheet.

**ASTRO-MED INC.**
**Consolidated Balance Sheets (in part)**
**Years ended January 31**

| ($ in thousands) | 2011 | 2010 |
|---|---|---|
| Shareholders' equity: | | |
| Common stock | 433 | 416 |
| Additional paid-in capital | 36,586 | 34,713 |
| Retained earnings | 26,843 | 26,817 |
| Accumulated other comprehensive income | 266 | 317 |
| Treasury stock | (9,840) | (8,030) |
| Total shareholders' equity | $54,288 | $54,233 |