The Foresight Companies, LLC
Accounting News

What Foresight Accounting Has Been Working On, Doing and Learning This Month JUNE 2014

"Show me the Money!"

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Reading Financial Statements
If you can read a nutrition label or a baseball box score, you can learn to read basic financial statements. If you can follow a recipe or apply for a loan, you can learn basic accounting. The basics aren't difficult and they aren't rocket science.

We all remember Cuba Gooding Jr.'s immortal line "Show me the money" from the movie Jerry Maguire. Well, that's what financial statements do. They show you where a company's money came from, where it went, and where it is now.

Let's look at the two major financial statements.

1. Balance Sheets
A balance sheet provides detailed information about a company's assets, liabilities and shareholder's equity, based on a particular date (i.e. year ending December 31, or month ending Jan 31).

The following formula summarizes what a balance sheet shows:

Assets = Liabilities + Shareholders' Equity

Assets are items a company owns that have value. This typically means they can be sold or used by a company to make products or provide services that can be sold. Assets include physical property, such as land, buildings, autos, equipment and inventory. It also includes cash in the bank and receivables you plan to collect.

Liabilities are the amount of money that a company owes to others. This can include obligations such as money borrowed from a bank to purchase assets, mortgages, payables to vendors for products already received or services already performed, and payroll or sales taxes owed.

Shareholder's Equity is sometimes called capital or net worth. It's the money that would be left if a company sold all of its assets and paid all of its liabilities. This money belongs to the shareholders or owners of the company.

2. Income Statements
An income statement reports how much revenue a company earned over a specific period time period (i.e. fiscal year Jan – Dec, or month Jan 1 – Jan 31). An income statement also shows the costs and expenses associated with earning that revenue. The literal "bottom line" of the statement shows a company's net earnings or losses for the specified period of time.

To understand how income statements are set up, think of time as a set of stairs. You start at the top with the total amount of sales made during the accounting period. Then you go down, one step at a time. At each step you make a deduction for certain costs or operating expenses. At the bottom of the stairs, after deducting all of the expenses, you learn how much the company actually earned or lost during the accounting period.

The following formula summarizes what an Income Statement shows:

Gross Sales – Discounts/Refunds – Cost of Goods Sold – Operating Expenses = Net Profit/Loss

At the top of the income statement is the total amount of money brought in from sales of products or services. This top line is often referred to as **gross revenues or sales**. It's called "gross" because expenses have not been deducted from it yet.

The next step is money the company doesn't expect to collect on certain sales due, for example, to **discounts or refunds**.

Moving down the stairs, there are line items to subtract for **Cost of Goods Sold** and **operating expenses** such as rents paid, supplies, payroll, insurance, interest, and marketing expenses.

Finally, you arrive at the bottom line; **Net Profit or Net Loss**, this number rolls onto the Owner Equity section of the balance sheet.