Chapter 2: Self-Test Problem 2:1

THE HOME DEPOT'S INCOME STATEMENTS

The Home Depot's income statements presentation in the company annual report does not differ much from that of OS Distributors. The Home Depot has two additional sources of revenues or expenses: one account entitled "Other" and another account entitled "Earnings (loss) from discontinued operations, net of tax."

OTHER

The $163 million expense during fiscal year 2008 is a write-down on a company activity, which was disposed of during that year.

EARNINGS (LOSS) FROM DISCONTINUED OPERATIONS (NET OF TAX)

Over the three fiscal years, 2006 to 2008, The Home Depot has disposed of some of its operations. The contribution of these discontinued operations to the company's Net Earnings in each of these years is reported in the account entitled "Earnings (Loss) from Discontinued Operations, net of tax."

Finally, note that the income tax expense is reported as "Provision for Income Tax." The terminology is (slightly) different, but the meaning is the same.

FURTHER READING

1. Cohen, Jacob, and David Young. *The Convergence of Global Accounting Standards*, Working Paper, INSEAD, 2005.
2. Kieso, Donald, Jerry Weygandt, and Terry Warfield. *Intermediate Accounting*, 13th ed. John Wiley & Sons, 2010. See Chapters 1 to 5.
3. Stickney, Clyde, Roman Weil, Katherine Schipper, and Jennifer Francis. *Financial Accounting*, 13th ed. South-Western, 2010. See Chapters 2, 3, and 4.

SELF-TEST PROBLEMS

2.1 CONSTRUCTING INCOME STATEMENTS AND BALANCE SHEETS.

Based on the information provided below, prepare the following financial statements for CompuStores, a company that assembles and distributes personal computers:

a. An income statement for the calendar year 2010
b. A balance sheet on December 31, 2009
c. A balance sheet on December 31, 2010

1. Accounts receivable increased by $6,400,000 in 2010
2. Profits in 2010 were taxed at 40 percent
3. At the end of 2010, inventories equaled 10 percent of the year's sales
4. The net book value of fixed assets at the end of 2009 was $76 million
5. Cost of goods sold, other than the direct labor expenses related to the assembling of computers, equaled 70 percent of sales in 2010
6. The average interest rate on short- and long-term borrowing in 2010 was 10 percent of the amount of funds borrowed at the *beginning* of the year

7. Accounts receivable at the end of 2010 equaled 12 percent of sales
8. Accounts payable at the end of 2009 equaled $30 million
9. Depreciation expense was $9 million in 2010
10. The company owed its employees $4 million at the end of 2009; a year later, it owed them $1,810,000
11. Material purchased in 2010 amounted to $228 million
12. Selling, general, and administrative expenses for 2010 were $18 million
13. Fees related to a technical license amount to $4 million per year
14. Taxes payable in 2009 equaled $6 million, and the company paid in advance the same amount on December 15, 2009
15. The balance of long-term debt was $27 million at the end of 2009, of which $4 million was due at year-end
16. Shares of common stocks were not issued and outstanding shares were not repurchased in 2010
17. Direct labor expenses equaled 11.25 percent of sales
18. Repayment of long-term debt is $4 million per year
19. Inventories rose from $28 million at the end of 2009 to $32 million at the end of 2010
20. In 2010, one of the company's warehouses was enlarged at a cost of $14 million, which was partly financed with a $6 million long-term loan
21. Dividend payments for 2010 were $9,360,000
22. Accounts payable at the end of 2010 equaled 1.85 of a month of purchases
23. Equity capital at the end of 2009 was $81 million
24. At the end of 2009, the company had enough cash that it could have immediately paid one-fourth of its accounts payable; at the end of 2010, it could have paid only one-tenth
25. The company paid in advance $9,600,000 of taxes on December 15, 2010
26. The company's line of credit was $3 million at the end of 2009. A year later it increased by two-thirds
27. In 2010, the company had a $2 million nonrecurrent loss related to the discontinuation of an old product line
28. The company prepaid $1,500,000 on rent and insurance in 2009, and $2,085,000 a year later

2.2 FORECASTING INCOME STATEMENTS AND BALANCE SHEETS.

Having prepared CompuStores' financial statements for the year 2010, the company's financial manager wishes to *forecast* next year's income statement and balance sheet (called projected or **pro forma statements**). Prepare these projected statements using the following assumptions and the 2010 statements in the previous problem:

1. Sales are expected to grow by 10 percent
2. Gross profit and the components of the cost of goods sold, expressed as a percentage of sales, should be the same as in 2010