Chapter 1

A New Business

Two young graduates, Shelley and Jim, start their own business. Their idea is to open a store to sell computer games. The initial investments on January first require the following ($):

Shop Fixtures	60,000
Computers	10,000
Inventory (4,000 items)	40,000
Checking Bank account	6,000

The initial inventory is bought on a credit terms of two months. A local bank is willing to grant a loan of $30,000. The loan must be paid back in four equal annual payments. The interest is 6%. The owners themselves finance the remaining amount. They will hire two employees and rent a building in a trendy, yet affordable part of town.

Required
The opening balance sheet.

During the year the following takes place:

A total of 15,000 items were sold. The average sales price was $25. On December 31, the clients have paid for 85% of their purchases

A total of 16,000 items have been bought (purchase price the same as on January 1st). By December 31, 95% of these purchases have been paid for.

The total annual salaries are $150,000. Included in this amount is a $15,000 year-end bonus that, unfortunately for the workers, will be paid in January of the next year.

The rent is $2,000 per month and is always paid at the end of the month.

The redemption charge and the interest payment on the loan are made at year-end.

The monthly depreciation on the fixtures and the computers is $1,000 and $250 respectively.

At year-end the owners withdraw an amount of $4,600 from the business.

Required
- The income statement for this year
- The cash flow statement for this year
- The balance sheet at year end

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Opening Balance sheet

Assets	
Shop	60,000
Computers	10,000
Inventory	40,000
Bank	6,000
Total	116,000
Sources	
Loan	30,000
Trade Payables	40,000
Equity	116,000 – 70,000 = 46,000
Total	116,000

Income statement

Sales	15,000*25	375,000
Cost of sales	15,000*10	(150,000)
Depreciation fixtures	12*1,000	(12,000)
Depreciation computers	12*250	(3,000)
Rent	12*2,000	(24,000)
Salary		(150,000)
EBIT		**36,000**
Interest	30,000*6%	(1,800)
Profit		**34,200**

Cash flow statement

Sales receipt	0.85*375,000	318,750
Payable begin		(40,000)
Purchases	0.95*160,000	(152,000)
Rent		(24,000)
Salary	150,000-15,000	(135,000)
Redemption	30,000/4	(7,500)
Interest		(1,800)
Withdrawal		(4,600)
Change bank		**(46,150)**

Ending Balance sheet

Fixtures	60,000-12,000	48,000
Computer	10,000-3,000	7,000
Inventory	40,000-150,000+160,000	50,000
Receivable	0,15 * 375,000	56,250
Total		**161,250**
Equity	46,000 + 34,200 – 4,600	75,600
Loan	30,000 – 7,500	22,500
Payable	0,05 * 160,000	8,000

Unpaid Salary		15,000
Bank	6,000 – 46,150	40,150
Total		**161,250**

Trading Company

The balance sheet on January 1 2012 shows the following:

Assets	$	Sources	$
Bank	10,000	Trade Payables	30,000
Receivables	50,000	Long term debt (6%)	70,000
Inventory	60,000	Equity	170,000
Fixed assets	150,000		
	270,000		**270,000**

Products are bought at $6 a piece and sold for $10. The credit term for both sales and purchases is 1.5 months. We assume that sales and purchases are divided evenly over the year.

Required A. Sales revenues of 2011?

For 2012 the following planning has been made:

Sales is expected to be 45,000 units.

The opening inventory is considered to be too high. At the end of the year the inventory level should be equal to one month of sales.

Fixed assets are depreciated to a scrap value of $10,000 in 4 more years.

Total regular salaries this year are $100,000. On top of that, this year's working regulations dictate that have to receive a 10% bonus for working odd hours. This bonus will be paid in 2013.

In December, the company will sign a contract to lease a company car, starting January 2013. The monthly fee will be $600 and the leasing company demands a prepayment for three months upon signing the contract.

In December management proposes to pay $16,000 to the owners in March 2013. The rest of the profits will be retained.

At year end the interest and a $10,000 redemption on the loan is paid.

Required B. The income statement for 2012 C. The cash flow statement for 2012 D. The balance sheet of December 31, 2012

Solutions Trading Company

A. 2011 Sales = $50,000/1.5 *12 = $400,000

B.

Sales	45,000*10	450,000
Cos	45,000*6	(270,000)
Depre	(150 – 10)/4	(35,000)
Salaries		(110,000)
EBIT		**35,000**
Interest	70,000*6%	(4,200)
Income		**30,800**
Dividend		16,000
Retain	retain	14,800

C

Credit Sales	450,000*10.5/12	393,750
		50,000
Purchases	(45,000 – 6,250)*6*10.5/12	(203,437.50)
Trade payable		(30,000)
Salaries		(100,000)
Lease fee		(1,800)
Redemption		(10,000)
Interest		(4,200)
Net cash flow		**94,312.50**

D.

Bank	10,000 + 94,312.50	104,312.50
Prepaid Lease		1,800
Receivables	450,000*1.5/12	56,250
Inventory	45,000/12 * 6	22,500
Fixed Assets	150,000 – 35,000	115,000
		299,862.50
Trade payable	(45,000 – 6,250) *6 * 1.5/12	29,062.50
Dividend payable		16,000
Salary payable		10,000
Loan	70,000 – 10,000	60,000
Equity	170,000 + 14,800	184,800
Total		**299,862.50**