CHAPTER 11

Statement of cash flows

We will classify cash flows, reconcile net income to operating cash, and prepare a complete statement.



Read a complete statement of cash flows

Pinehaven Supply | Statement of Cash Flows | Year ended December 31, 2026 | US dollars

Cash flows	Dollars
Operating activities	
Net income	**$30,000**
Depreciation expense	$12,000
Gain on equipment sale	($2,000)
Increase in accounts receivable	($8,000)
Increase in inventory	($10,000)
Decrease in prepaid insurance	$2,000
Increase in accounts payable	$6,000
Increase in wages payable	$1,000
Increase in customer advances	$3,000
Increase in interest payable	$1,000
Decrease in income taxes payable	($1,000)
Net cash provided by operating activities	**$34,000**
Investing activities	
Proceeds from equipment sale	$10,000
Cash paid for equipment	($40,000)
Net cash used in investing activities	**($30,000)**
Financing activities	
Proceeds from borrowing	$25,000
Principal repaid	($12,000)
Proceeds from issuing common stock	$10,000
Dividends paid	($8,000)
Net cash provided by financing activities	**$15,000**
Increase in cash and restricted cash	**$19,000**
Cash and restricted cash at beginning of year	$35,000
Cash and restricted cash at end of year	**$54,000**

The change to explain.

Cash and restricted cash increased from $35,000 to $54,000. The statement reports that $19,000 increase.

Operating activities.

Cash from customers and cash paid to run the business provided $34,000.

Investing activities.

Purchases and sales of long-term assets used a net $30,000.

Financing activities.

Transactions with lenders and owners provided a net $15,000.

Income and cash differ.

Net income was $30,000. We will explain why operating cash and the total change in cash differ from that income.

Income and cash change at different times

Event	Effect on income	Effect on cash
Make a credit sale.	Record revenue and the related expense.	No customer receipt occurs yet.
Collect that receivable.	Record no new revenue.	Cash increases.
Buy equipment for cash.	Record an asset at purchase.	Cash decreases.
Record depreciation.	Expense reduces income.	No cash payment occurs.

Income timing: Revenue can precede collection, and expenses can occur without current payments.

Cash outside income: Equipment purchases use cash without an immediate expense.

Use the statement of cash flows to identify cash received and paid and reconcile the change in cash.

Two operating presentations

Direct method

Report operating receipts and payments.

Show customer collections and payments to suppliers and employees.

Indirect method

Start with net income and adjust to operating cash.

Show noncash expenses, gains or losses, and operating timing differences.

Both methods produce the same operating cash total under the same classification rules.

- Investing and financing presentation stays the same.
- US generally accepted accounting principles (GAAP) require a separate net-income reconciliation when a business uses the direct method.
- **International Financial Reporting Standards (IFRS):** The direct method does not require that separate reconciliation.

Find the information for the full statement

Review the full income statement

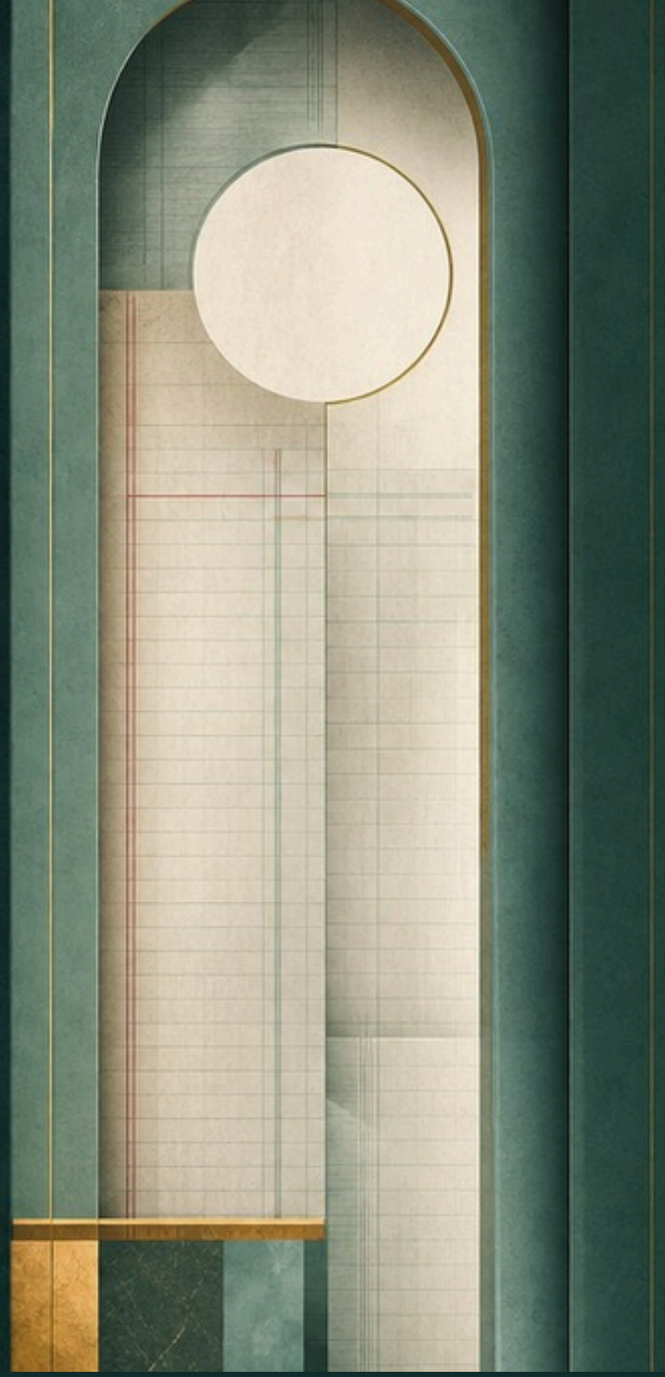
- Examine revenues, expenses, gains, and losses. Use transaction details to identify noncash items and effects connected with investing or financing.
- **Indirect method:** Start with net income. Adjust for those effects and operating timing differences.
- **Direct method:** Begin with operating revenues and expenses. Use related balance changes and transaction details to calculate operating receipts and payments.

An income-statement item is not automatically an operating cash flow. Exclude noncash items and cash flows belonging in other sections from operating receipts and payments.

Compare balance sheets and transaction details

- **Review every account.** Calculate each beginning-to-ending change and identify the transactions behind it.
- **Classify the cash effects.** Use the additional information to separate operating, investing, and financing cash flows. One transaction can affect several sections.
- **Identify noncash transactions.** Disclose significant noncash investing and financing transactions separately.
- **Reconcile cash.** The three activity totals must equal the change in cash and restricted cash.

Our source boxes supply selected excerpts. With complete statements, you locate that information yourself.



Beginning and ending cash

Determine which balances belong in the cash total.

Which balances belong in the cash total?

Pinehaven Supply | 2026 | US dollars

Cash flows	Dollars
Operating activities	
Net income	**$30,000**
Depreciation expense	$12,000
Gain on equipment sale	($2,000)
Increase in accounts receivable	($8,000)
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Cash and restricted cash at end of year	**$54,000**

Cash includes currency and deposits available on demand.

A **cash equivalent** is a short-term, highly liquid investment that converts readily to a known cash amount with insignificant value risk.

- Generally, its maturity is 3 months or less when acquired.
- Measure maturity from the acquisition date, not the reporting date.
- Apply and disclose the company's policy for qualifying investments.

Restricted cash remains in the total

Restricted cash has limits on its use, such as a deposit reserved for debt repayment.

- **Include in the US GAAP totals:** Cash, cash equivalents, restricted cash, and restricted cash equivalents belong in beginning and ending cash.
- **Transfers within that total:** Moving cash between included accounts leaves the combined balance unchanged. Report no operating, investing, or financing cash flow.
- **IFRS:** A contractual use restriction alone does not exclude a deposit that remains available on demand from cash.

Compensating balances and overdrafts

Bank arrangement	Meaning	US GAAP treatment
Compensating balance	The company maintains a deposit with a lender under a credit arrangement.	Include it as cash or restricted cash, depending on the restriction.
Bank overdraft	The bank advances money to cover payments exceeding the deposit.	Report a liability outside the cash total.

IFRS: Include a bank overdraft in cash and cash equivalents only if it is repayable on demand and integral to day-to-day cash management.

Which cash treatment is correct?

iClicker | Question 1 of 5

A company buys a note on July 1, 2026, with repayment due December 31, 2026. Its reporting date is September 30.

It also transfers money from its bank account into restricted cash. Which treatment is correct under US GAAP?

A The note is a cash equivalent, and the transfer is an investing outflow.

B The note is a cash equivalent, and the transfer creates no cash flow.

C The note is not a cash equivalent, and the transfer creates no cash flow.

D The note is not a cash equivalent, and the transfer is an investing outflow.

Which cash treatment is correct?

iClicker | Answer 1 of 5

Correct answer: C.

A company buys a note on July 1, 2026, with repayment due December 31, 2026. Its reporting date is September 30. It also transfers money from its bank account into restricted cash. Which treatment is correct under US GAAP?

A **The note is a cash equivalent, and the transfer is an investing outflow.**
The note had a 6-month maturity when acquired. Both deposit accounts remain within the cash-flow total.

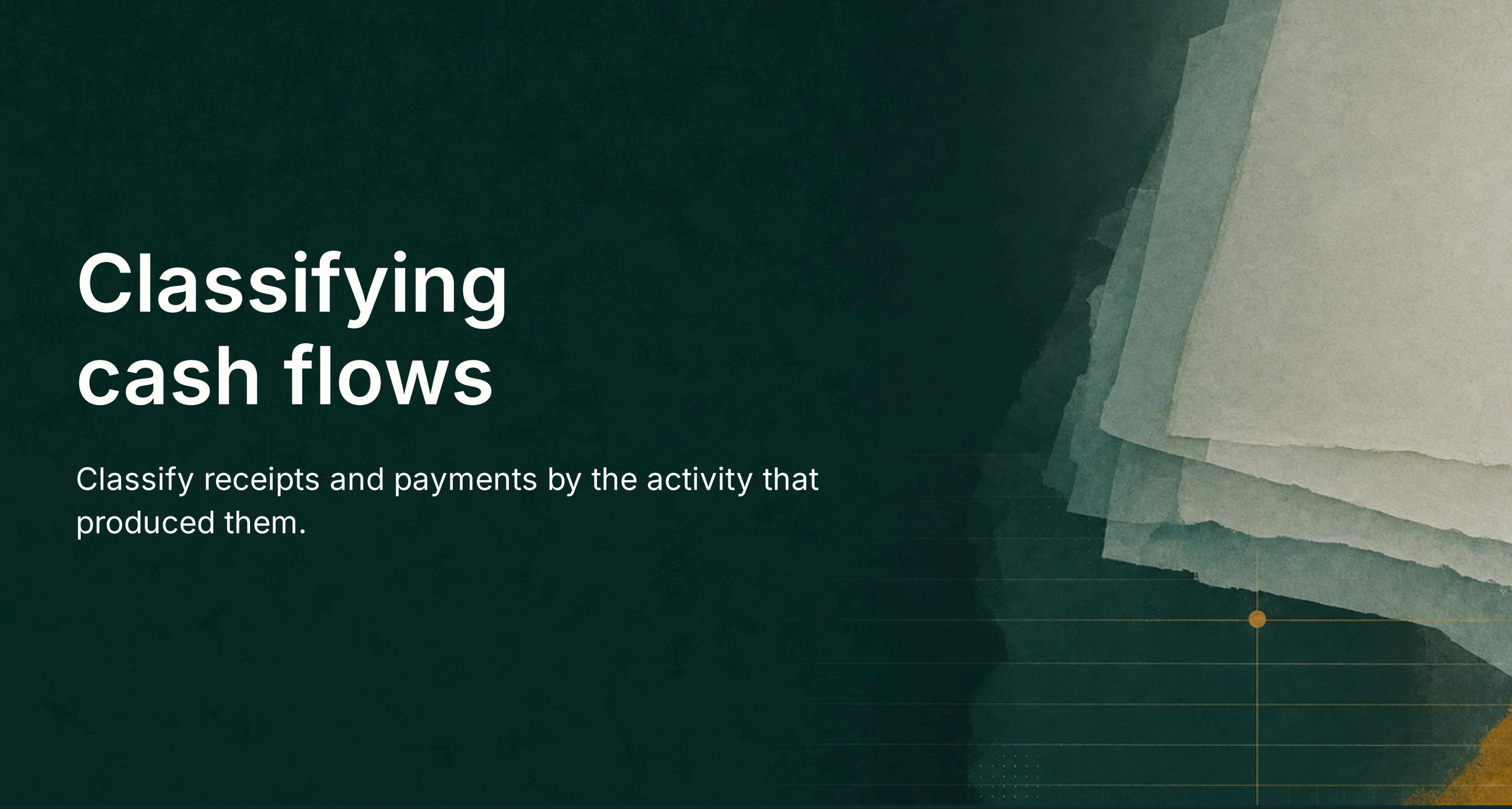
B **The note is a cash equivalent, and the transfer creates no cash flow.**
The transfer treatment is correct, but 3 months remaining at the reporting date does not change maturity at acquisition.

C **The note is not a cash equivalent, and the transfer creates no cash flow.**
The original maturity exceeds 3 months. Moving money between included cash accounts leaves the combined total unchanged.

D **The note is not a cash equivalent, and the transfer is an investing outflow.**
The note treatment is correct. The internal transfer does not buy an asset outside the combined cash total.

Classifying cash flows

Classify receipts and payments by the activity that produced them.



Operating, investing, and financing activities

In Class 3, we classified cash receipts and payments by the activity that produced them.

Operating	Investing	Financing
Cash effects of revenue and expenses, unless classified elsewhere.	Buy or sell long-term operating assets and investments; make loans and collect principal.	Obtain cash from lenders and owners, and return cash to them.
Buy inventory; collect customer receivables.	Buy equipment; collect principal on a loan to another company.	Borrow or repay debt principal; issue shares; pay dividends.

Borrow cash and buy equipment

A company borrows cash from a bank and spends all the proceeds on equipment.

How should the cash borrowing be classified?

How should the equipment payment be classified?

Should both transactions appear if ending cash equals beginning cash?

Record both cash movements

A company borrows cash from a bank and spends all the proceeds on equipment.

How should the cash borrowing be classified?

Financing inflow. The lender provides cash financing.

How should the equipment payment be classified?

Investing outflow. The company buys a long-term operating asset.

Should both transactions appear if ending cash equals beginning cash?

Yes, report both separately. Equal receipts and payments leave cash unchanged. The company still acquired equipment and incurred debt.

Interest and dividends under US GAAP

Receipt or payment	Classification
Receive interest or ordinary cash dividends.	Operating.
Pay ordinary interest expense.	Operating.
Pay dividends to owners or repurchase shares.	Financing.

Interest expense and dividend income enter net income.

Dividends paid distribute earnings to owners. They do not reduce net income.

IFRS: Interest and dividend classifications can differ; check IFRS 18 adoption before comparing operating cash flow.

How should the bank payment be split?

iClicker | Question 2 of 5

A company pays its bank $11,000: $10,000 of loan principal and $1,000 of ordinary interest. The loan is due within the year.

Which classification follows US GAAP?

A Both amounts are operating outflows because the loan is a current liability.

B Principal is a financing outflow, and interest is an operating outflow.

C Principal is an investing outflow, and interest is an operating outflow.

D Both amounts are financing outflows because the bank received the cash.

How should the bank payment be split?

iClicker | Answer 2 of 5

Correct answer: B.

A company pays its bank $11,000: $10,000 of loan principal and $1,000 of ordinary interest. The loan is due within the year.

Which classification follows US GAAP?

A **Both amounts are operating outflows because the loan is a current liability.**
The due date concerns balance-sheet classification. Principal still repays bank financing.

B **Principal is a financing outflow, and interest is an operating outflow.**
Principal repays borrowed funds. US GAAP classifies the payment of ordinary interest expense as operating.

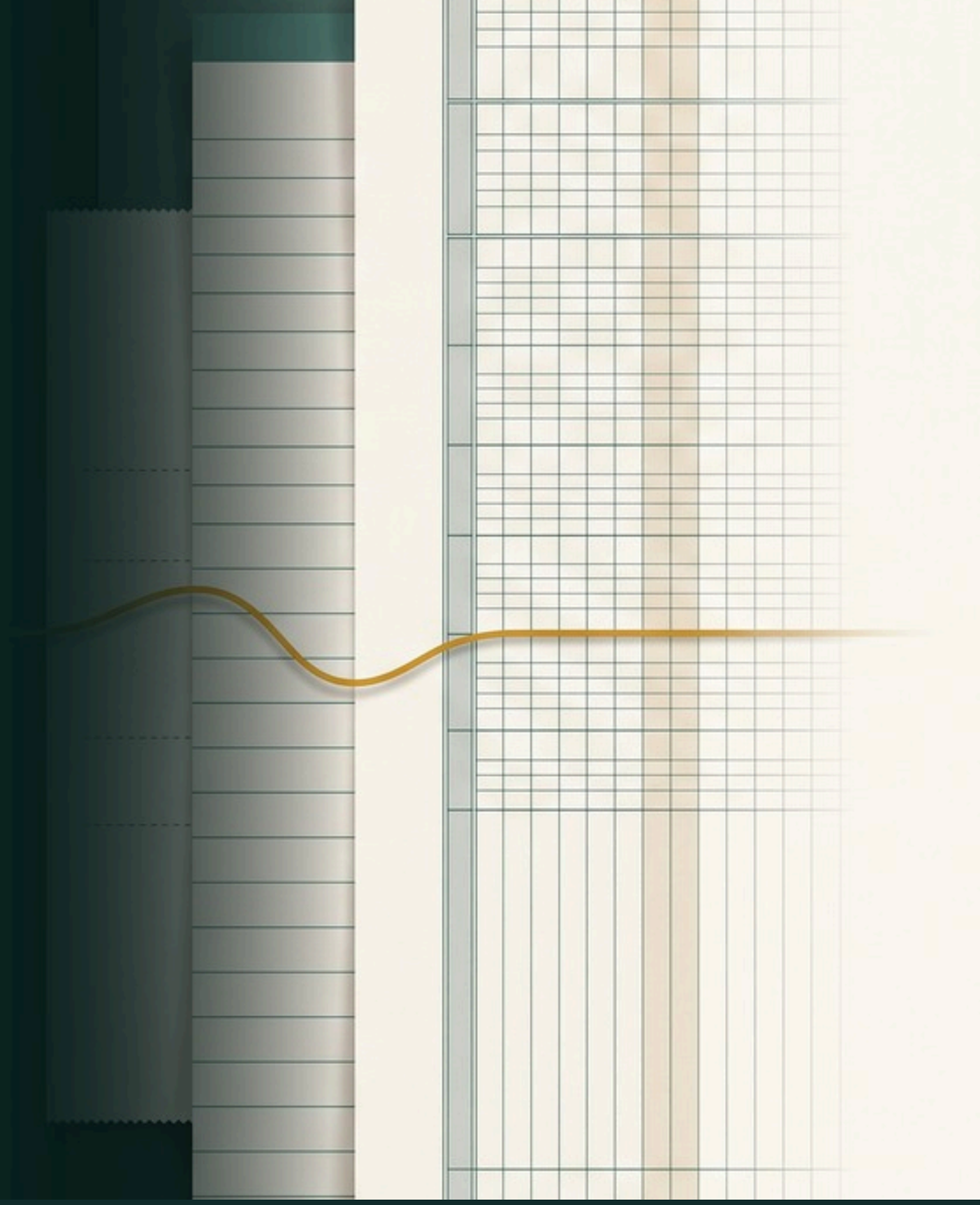
C **Principal is an investing outflow, and interest is an operating outflow.**
Repaying the company's own borrowing differs from making or collecting a loan to another company.

D **Both amounts are financing outflows because the bank received the cash.**
The recipient alone does not determine classification. Ordinary interest paid belongs in operating activities under US GAAP.

Building the SCF

Operating activities

Reconcile net income to cash from operations.



Reconcile net income to operating cash

Adjust the revenue and expenses in net income to operating receipts and payments.

Compare what entered income with what happened to cash:

What happened?	Why adjust net income?
An expense reduced income without a current cash payment.	Add it back to remove the deduction that used no cash.
Revenue increased income before cash was collected.	Subtract the uncollected amount because income includes more than cash received.
The company collected cash for revenue recognized in an earlier period.	Add the collection because cash increased, but current net income does not include that revenue.
The company paid cash for an expense recognized in an earlier period.	Subtract the payment because cash decreased, but current net income does not include that expense.

Asset sales: Remove gains and losses from income; report the actual proceeds in investing activities.

No timing difference: An expense paid as incurred reduces income and operating cash equally. No adjustment is needed.

Reconciliation only: These adjustments do not reverse journal entries or record new revenue and expenses.

IFRS: After IFRS 18 adoption, the indirect reconciliation starts with operating profit or loss.

Depreciation reduces income without using cash

Source documents:

Income statement: Net income was $17,000; depreciation expense was $16,000.

Zoomies Pet Store is a fictional US corporation. We will prepare its full statement for the year ended December 31, 2026, in US dollars.

Begin the indirect operating section with net income. Zoomies recorded depreciation as follows:

Account	Debit	Credit
Depreciation expense	$16,000	
Accumulated depreciation		$16,000

- Depreciation reduced net income without a cash payment.
- **Add back the expense** to remove that noncash deduction from operating cash flow. The expense remains recorded in the accounts.

On the statement of cash flows

Start with net income: $17,000. Add depreciation expense: $16,000.

Credit loss expense and write-offs differ

Source documents:

Income statement: Credit loss expense was $3,000.

Additional information: A daycare closed with an unpaid $4,000 invoice. Zoomies wrote off that balance against the allowance.

Zoomies sells pet supplies to dog daycares on 30-day credit. An **allowance for credit losses** reduces receivables for amounts Zoomies expects not to collect.

Credit loss expense during 2026: Zoomies recorded the annual expense.

Account	Debit	Credit
Credit loss expense	$3,000	
Allowance for credit losses		$3,000

The expense reduces income without using cash.

Daycare write-off during 2026: Zoomies removed the unpaid balance against the allowance.

Account	Debit	Credit
Allowance for credit losses	$4,000	
Accounts receivable		$4,000

The write-off reduces gross receivables and the allowance equally. It creates no new expense and no cash receipt.

On the statement of cash flows: Add credit loss expense: $3,000 when using gross receivables. The write-off creates no separate cash-flow line.

Two ways to adjust for receivables

Gross receivables:

the balance before deducting the allowance.

Add back credit loss expense separately. Exclude write-offs when calculating the difference between credit sales and collections.

Net receivables:

gross receivables less the allowance.

Use the net balance change. Do not also add back credit loss expense because its effect is already included.

Both approaches give the same total adjustment when applied consistently.

- These relationships assume only sales, collections, credit loss expense, and write-offs change the accounts.
- We will use gross receivables first, then check the result using net receivables.

Separate write-offs from collections

Source documents:

Comparative balance sheets: Gross receivables decreased from $40,000 to $30,000.

Additional information: Write-offs were $4,000. Only credit sales, collections, and write-offs changed gross receivables.

Accounts receivable (gross)

DEBIT		CREDIT	
Beginning balance	**$40,000**		
Credit sales			Collections
		$4,000	Write-offs
Ending balance	**$30,000**		

- Gross receivables decreased by $10,000, including an unpaid balance written off.
- **Exclude the $4,000 write-off.** Determine how much collections exceeded credit sales.

Collections exceeded credit sales

Source documents:

Comparative balance sheets: Gross receivables decreased from $40,000 to $30,000.

Additional information: Write-offs were $4,000. Only credit sales, collections, and write-offs changed gross receivables.

Accounts receivable (gross)

DEBIT		CREDIT	
Beginning balance	$40,000		
Credit sales		credit sales + $6,000	Collections
		$4,000	Write-offs
Ending balance	$30,000		

Receivable decrease excluding write-offs: $10,000 - $4,000 = $6,000.

- Collections exceeded credit sales by that amount. We can calculate the difference without knowing either total.
- **Add the difference:** Cash received exceeded the sales revenue included in net income.

On the statement of cash flows

Add decrease in gross receivables, excluding write-offs: $6,000.

Net receivables give the same adjustment

Source documents:

Comparative balance sheets: Gross receivables were $40,000 at the beginning and $30,000 at the end. The allowance was $2,000 and $1,000, respectively.

Additional information: Only credit loss expense and write-offs changed the allowance.

Net receivables = gross receivables - allowance.

Allowance for credit losses

DEBIT		CREDIT	
		$2,000	Beginning balance
		$3,000	Credit loss expense
Write-offs	**$4,000**		
		$1,000	Ending balance

Receivable balance	Beginning	Ending
Gross receivables	$40,000	$30,000
Less allowance	($2,000)	($1,000)
Net receivables	$38,000	$29,000

- **Same total adjustment:** The $9,000 net decrease equals $3,000 of expense plus the $6,000 collection difference.
- **No second expense adjustment:** The net balance change already includes the credit loss expense.
- **No write-off effect on net receivables:** Gross receivables and the allowance decrease equally.

On the statement of cash flows: Alternative using net receivables: add decrease in net receivables, $9,000. Do not also add credit loss expense. Zoomies' completed statement uses the gross method.

Gift card sales, redemptions, and refunds

Zoomies also sells gift cards redeemable for merchandise. Its policy permits cash refunds of unused balances.

Event	Cash effect	Revenue effect	Gift card liability
Sell a gift card.	Cash increases.	No revenue is earned yet.	The liability increases.
Redeem a card for merchandise.	No new cash is received.	Revenue increases.	The liability decreases.
Refund an unused balance.	Cash decreases.	No revenue is earned or reversed.	The liability decreases.

Add card-sale receipts: Cash arrives before revenue.

Subtract redemption revenue: Revenue increases without new cash.

Subtract refunds: Cash decreases without reducing revenue.

Why did the gift card liability change?

Source documents:

Comparative balance sheets: The beginning gift card liability was $9,000.

Additional information: Zoomies sold $24,000 of cards, redeemed $25,000 for merchandise, and refunded $2,000 in cash. No expirations or other changes occurred.

iClicker | Question 3 of 5

Which adjustment converts gift card revenue to net operating cash from these transactions?

A. Add $3,000 because settling a liability increases cash.

B. Subtract only $1,000 because redemptions exceeded new card sales.

C. Subtract only $2,000 because refunds are the only cash payments.

D. Subtract $3,000 because revenue exceeded new card receipts and refunds also reduced cash.

Why did the gift card liability change?

Source documents:

Comparative balance sheets: The beginning gift card liability was $9,000.

Additional information: Zoomies sold $24,000 of cards, redeemed $25,000 for merchandise, and refunded $2,000 in cash. No expirations or other changes occurred.

iClicker | Answer 3 of 5

Correct answer: D.

Which adjustment converts gift card revenue to net operating cash from these transactions?

A **Add $3,000 because settling a liability increases cash.**
Redemptions and refunds reduce the liability without providing cash.

B **Subtract only $1,000 because redemptions exceeded new card sales.**
Subtracting excess redemptions alone omits the cash refunds.

C **Subtract only $2,000 because refunds are the only cash payments.**
Subtracting refunds alone leaves revenue from earlier card receipts in income.

D **Subtract $3,000 because revenue exceeded new card receipts and refunds also reduced cash.**
Redemptions exceed card sales, and refunds also use cash. Both require subtraction from net income.

On the statement of cash flows: Subtract decrease in gift card liability: $3,000.

Purchases, expense, and payment occur separately

01

Buy merchandise on credit.

Account	Debit	Credit
Inventory	Purchases	
Accounts payable		Purchases

Income/cash effect: No expense or cash payment occurs yet.

02

Record the cost of merchandise sold.

Account	Debit	Credit
Cost of goods sold	Cost of goods sold	
Inventory		Cost of goods sold

Income/cash effect: Expense reduces income; this entry does not pay cash.

03

Pay the supplier.

Account	Debit	Credit
Accounts payable	Payment	
Cash		Payment

Income/cash effect: Cash decreases without a new expense.

Inventory

DEBIT	CREDIT
Beginning balance	
Purchases	Cost of goods sold
Ending balance	

Calculate inventory purchases

Source documents:

Income statement: Cost of goods sold was $190,000.

Comparative balance sheets: Inventory increased from $50,000 to $62,000.

Additional information: No inventory write-downs or other noncash changes occurred.

01

Calculate purchases from cost of goods sold and the inventory change.

02

Explain why purchases differ from expense.

03

Identify the additional account needed to determine how much Zoomies paid.

Purchases exceeded cost of goods sold

Source documents:

Income statement: Cost of goods sold was $190,000.

Comparative balance sheets: Inventory increased from $50,000 to $62,000.

Additional information: No inventory write-downs or other noncash changes occurred.

Inventory

DEBIT		CREDIT	
Beginning balance	**$50,000**		
Purchases	**$202,000**	**$190,000**	Cost of goods sold
Ending balance	**$62,000**		

- Purchases were $202,000, or $12,000 more than cost of goods sold.
- **Subtract the inventory increase** to include purchases beyond the expense already deducted from income.
- Next, use supplier payables to determine how much of those purchases remained unpaid.

On the statement of cash flows

Subtract increase in inventory: $12,000.

Supplier payables reduced the cash paid

Source documents:

Income statement: Cost of goods sold was $190,000.

Comparative balance sheets: Inventory increased from $50,000 to $62,000. Accounts payable increased from $28,000 to $35,000.

Additional information: Accounts payable relates only to merchandise. No inventory write-downs or other noncash changes occurred.

Accounts payable to merchandise suppliers

DEBIT		CREDIT	
		$28,000	Beginning balance
Payments	**$195,000**	**$202,000**	Purchases
		$35,000	Ending balance

- Zoomies paid $195,000, or $7,000 less than its purchases.
- **Add the payable increase:** The unpaid portion of purchases used no cash.
- **Combined adjustment:** Subtract $5,000 because cash paid exceeded cost of goods sold by that amount.

On the statement of cash flows

Add increase in accounts payable: $7,000.

Calculate supplies used and cash paid

Source documents:

Comparative balance sheets: Beginning store supplies were $1,000.

Additional information: Zoomies bought $6,000 of cleaning materials and packing bags for cash. The year-end count found $2,000 unused. Supplies are used internally. None were lost, returned, or sold.

Store supplies

DEBIT		CREDIT	
Beginning balance	$1,000		
Cash purchases	$6,000	?	Supplies used
Ending balance	$2,000		

Supplies become expense when used.

1. Calculate supplies used from the beginning balance, purchases, and ending count.
2. Compare supplies expense with cash paid.
3. Determine the adjustment to net income and explain why it is needed.

Unused supplies remain an asset

Source documents:

Comparative balance sheets: Beginning store supplies were $1,000.

Additional information: Zoomies bought $6,000 of cleaning materials and packing bags for cash. The year-end count found $2,000 unused. Supplies are used internally. None were lost, returned, or sold.

Store supplies

DEBIT		CREDIT	
Beginning balance	**$1,000**		
Cash purchases	**$6,000**	**$5,000**	Supplies used
Ending balance	**$2,000**		

- **Expense:** Zoomies used $5,000 of supplies.
- **Cash payment:** Zoomies paid $6,000 for supplies.
- **Difference:** The $1,000 increase in unused supplies used cash without reducing income. Subtract that increase.

On the statement of cash flows

Subtract increase in store supplies: $1,000.

Connect inventory with supplier payables

Source documents:

Comparative balance sheets: Merchandise inventory increased by $12,000, and merchandise supplier payables increased by $7,000.

Additional information: Inventory changed only through purchases and cost of goods sold. Supplier payables changed only through those purchases and cash payments.

iClicker | Question 4 of 5

How should Zoomies adjust net income for inventory and supplier payables?

A. Subtract $5,000 because payments exceeded cost of goods sold.

B. Subtract $12,000 because the inventory increase equals the extra cash paid.

C. Add $5,000 because purchases not yet paid exceeded the inventory increase.

D. Add $7,000 because only the payable change affects cash paid.

Connect inventory with supplier payables

Source documents:

Comparative balance sheets: Merchandise inventory increased by $12,000, and merchandise supplier payables increased by $7,000.

Additional information: Inventory changed only through purchases and cost of goods sold. Supplier payables changed only through those purchases and cash payments.

iClicker | Answer 4 of 5

Correct answer: A.

How should Zoomies adjust net income for inventory and supplier payables?

A **Subtract $5,000 because payments exceeded cost of goods sold.**
Subtract purchases beyond expense, then add the portion still unpaid.

B **Subtract $12,000 because the inventory increase equals the extra cash paid.**
Some purchases remain unpaid. The inventory change alone overstates cash paid.

C **Add $5,000 because purchases not yet paid exceeded the inventory increase.**
The inventory increase exceeds the payable increase, so cash paid exceeds expense.

D **Add $7,000 because only the payable change affects cash paid.**
The payable change alone omits purchases beyond expense.

On the statement of cash flows: Net adjustment: subtract $5,000 from net income.

Cash paid exceeded cost of goods sold

Source documents:

Comparative balance sheets and worked calculations: Inventory changed only through purchases and cost of goods sold. Supplier payables changed only through purchases and cash payments.

Zoomies Pet Store | 2026 | US dollars

Inventory

DEBIT		CREDIT	
Beginning balance	$50,000		
Purchases	$202,000	$190,000	Cost of goods sold
Ending balance	$62,000		

Accounts payable to merchandise suppliers

DEBIT		CREDIT	
		$28,000	Beginning balance
Payments	$195,000	$202,000	Purchases
		$35,000	Ending balance

- **Subtract the inventory increase:** Purchases exceeded expense by $12,000.
- **Add the payable increase:** Cash payments were $7,000 below purchases.

On the statement of cash flows

Cash paid of $195,000 exceeded cost of goods sold of $190,000. Subtract $5,000 from net income.

Utility expense differs from cash paid

Source documents:

Comparative balance sheets: Utilities payable was $500 at the beginning and $1,000 at the end.

Additional information: The December 2025 bill was paid in January 2026. Zoomies paid $5,000 for January through November 2026 service. The December 2026 bill was paid in January 2027.

Expense for 2026 = $5,000 + $1,000 = $6,000.

Cash paid in 2026 = $500 + $5,000 = $5,500.

- **Expense follows the service period:** Include December 2026 service, even though Zoomies paid in 2027.
- **Cash flow follows the payment date:** Include the December 2025 bill paid in 2026.
- Add $500 to net income because expense exceeded cash paid.

On the statement of cash flows

Add increase in utilities payable: $500.

Adjust for interest and tax payables

Source documents:

Comparative balance sheets: Interest payable decreased from $2,000 to $1,000. Income taxes payable increased from $3,000 to $4,000.

Additional information: Only current expense and cash payments changed these payables.

For each payable:

01

Determine whether cash paid exceeded or fell below expense.

02

Decide whether to add or subtract the change in the operating reconciliation.

Adjust for the unpaid expense changes

Source documents:

Comparative balance sheets: Interest payable decreased from $2,000 to $1,000. Income taxes payable increased from $3,000 to $4,000.

Additional information: Only current expense and cash payments changed these payables.

Account	Beginning	Ending	Operating adjustment
Interest payable	$2,000	$1,000	Subtract $1,000. Cash paid exceeded expense.
Income taxes payable	$3,000	$4,000	Add $1,000. Cash paid was below expense.

The accounts changed only through current expense and cash payments. Other movements would require separate analysis.

On the statement of cash flows

Subtract decrease in interest payable: $1,000. Add increase in income taxes payable: $1,000.

Work through the van sale

Source documents:

Additional information: Zoomies sold its old van for $9,000. The van cost $30,000 and had accumulated depreciation of $18,000.

01

Calculate the van's carrying amount and the gain or loss on sale.

02

Determine the effect on the operating reconciliation.

03

Identify the cash receipt and its cash-flow classification.

Separate the loss from sale proceeds

Source documents:

Additional information: Zoomies sold its old van for $9,000. The van cost $30,000 and had accumulated depreciation of $18,000.

Sale fact	Amount
Equipment cost	$30,000
Accumulated depreciation removed	$18,000
Carrying amount: cost less accumulated depreciation	$12,000
Cash proceeds	$9,000
Loss: carrying amount less proceeds	$3,000

- **Operating adjustment:** Add back the $3,000 loss. It reduced net income, but it was not an operating cash payment.
- **Investing receipt:** Report the full $9,000 proceeds when we prepare the investing section.

On the statement of cash flows

Add loss on equipment sale: $3,000.

Complete Zoomies' operating section

Zoomies Pet Store | Year ended December 31, 2026 | US dollars

Operating activities	Amount
Net income	$17,000
Add depreciation expense.	$16,000
Add loss on equipment sale.	$3,000
Add credit loss expense.	$3,000
Add decrease in gross receivables, excluding write-offs.	$6,000
Subtract decrease in gift card liability.	($3,000)
Subtract increase in inventory.	($12,000)
Add increase in accounts payable.	$7,000
Subtract increase in store supplies.	($1,000)
Add increase in utilities payable.	$500
Subtract decrease in interest payable.	($1,000)
Add increase in income taxes payable.	$1,000
Net cash provided by operating activities	**$36,500**

On the statement of cash flows

Operating section complete: net cash provided is $36,500. Investing and financing activities remain to be prepared.

Building the SCF

Investing activities

Separate cash purchases and sale proceeds from noncash transactions.



Separate cash and noncash transactions

The operating section is complete. Next, prepare investing and financing cash flows and identify noncash transactions for separate disclosure.

Transaction	Cash-flow treatment
Acquire equipment entirely by issuing a note to the seller.	Disclose the noncash investing and financing transaction separately.
Reclassify long-term debt as current.	Report no cash flow for the reclassification.
Later repay principal on the equipment note.	Report a financing cash outflow.

Inventory supplier notes: Principal payments are operating because the company is paying for inventory.

Equipment additions can include noncash purchases

Beginning equipment cost

+ Purchases

- Original cost removed on disposal

= Ending equipment cost

1. **Recover total purchases.** Add the disposed asset's original cost to the net increase in equipment. The equipment account records original cost.

2. **Find the cash payment.** Subtract the seller-financed portion of purchases because issuing the note provided no cash.

Cash proceeds from selling the old equipment are a separate investing receipt.

How much cash bought equipment?

Source documents:

Comparative balance sheets: The equipment account balance increased from $120,000 to $155,000.

Additional information: The old van sold had originally been purchased for $30,000. The only purchase was a replacement van, paid partly in cash and partly with a $20,000 note issued to the seller.

iClicker | Question 5 of 5

Which calculation gives the cash purchase?

A $155,000 - $120,000.

B $155,000 - $120,000 + $30,000.

C $155,000 - $120,000 + $30,000 - $20,000.

D $155,000 - $120,000 - $30,000 - $20,000.

How much cash bought equipment?

Source documents:

Comparative balance sheets: The equipment account balance increased from $120,000 to $155,000.

Additional information: The old van sold had originally been purchased for $30,000. The only purchase was a replacement van, paid partly in cash and partly with a $20,000 note issued to the seller.

iClicker | Answer 5 of 5

Correct answer: C.

Which calculation gives the cash purchase?

A **$155,000 - $120,000.**
The net change includes both the van disposal and the seller-financed portion.

B **$155,000 - $120,000 + $30,000.**
Adding back the disposed cost gives total purchases, including the seller-financed portion.

C **$155,000 - $120,000 + $30,000 - $20,000.**
Add back the removed cost, then exclude the seller-financed portion. The cash purchase is $45,000.

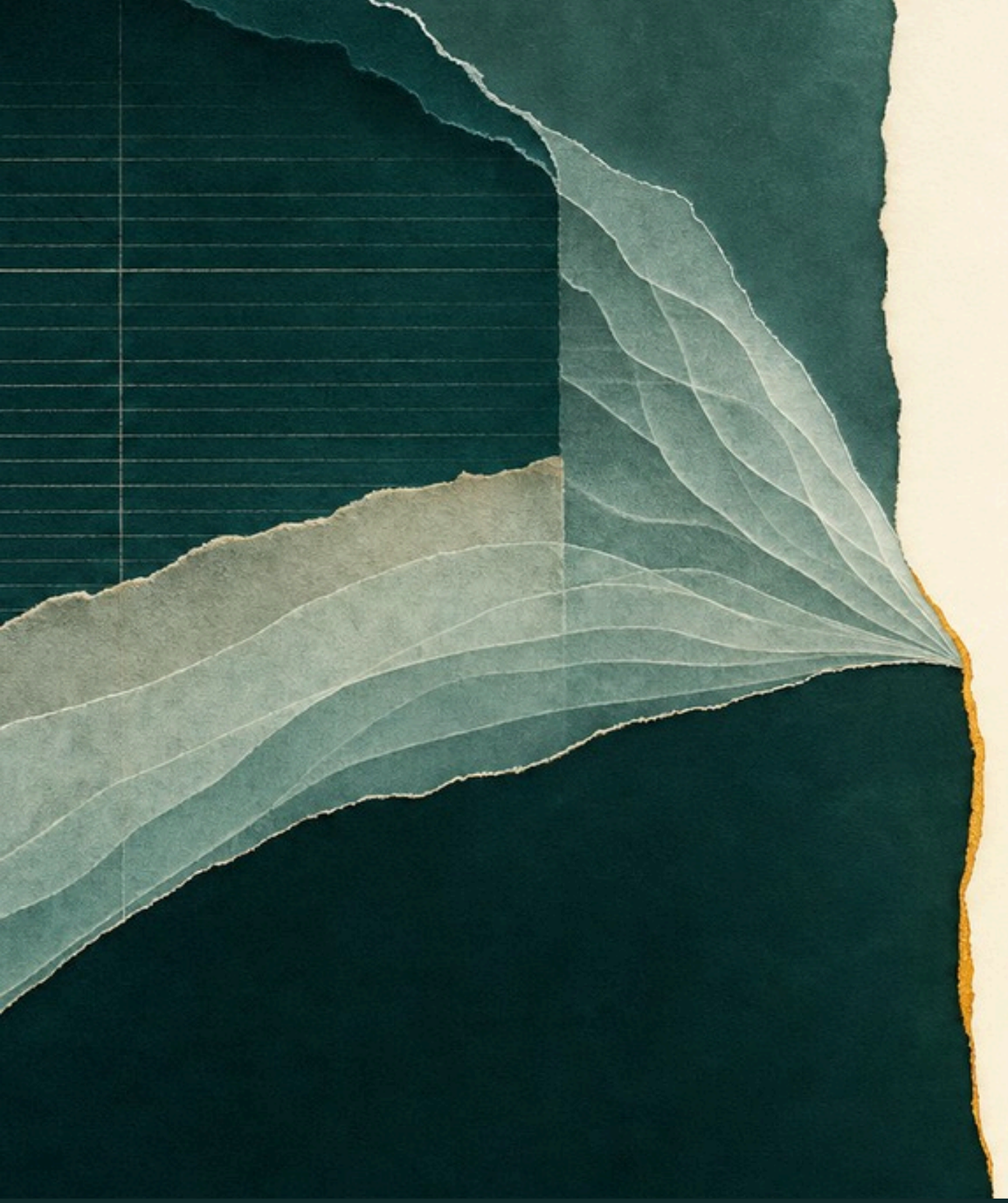
D **$155,000 - $120,000 - $30,000 - $20,000.**
The disposed cost already reduced ending equipment. Subtracting it again moves the calculation in the wrong direction.

Report equipment receipts and payments separately

Zoomies Pet Store | Investing activities for 2026 | US dollars

Investing activities	Amount
Proceeds from equipment sale	$9,000
Cash paid for equipment	($45,000)
Net cash used in investing activities	**($36,000)**

- **Sale proceeds:** Report the full receipt here. The loss has already been removed from operating cash flow.
- **Seller financing:** Disclose the $20,000 note portion of the van purchase separately.



Building the SCF

Financing activities

Identify cash received from lenders and owners and cash returned to them.

Separate cash borrowing from noncash debt

Source documents:

Comparative balance sheets: Notes payable increased from $60,000 to $92,000.

Additional information: Zoomies borrowed $30,000 in cash, repaid $18,000 of principal, and issued a $20,000 equipment note. No other debt changes occurred.

Notes payable reconciliation	Amount
Beginning notes payable	$60,000
Add cash borrowing.	$30,000
Add note issued for equipment.	$20,000
Subtract principal repaid.	($18,000)
Ending notes payable	**$92,000**

- **Cash financing:** Report $30,000 received and $18,000 repaid separately.
- **Noncash debt:** The equipment note increased debt without providing cash at acquisition.
- **IFRS:** Disclose both cash and noncash changes in liabilities arising from financing activities.

Calculate dividends paid

Source documents:

Comparative balance sheets: Dividends payable increased from $2,000 to $4,000.

Additional information: Zoomies declared $10,000 of dividends. Only declarations and payments changed the payable.

- **Declaration:** The company records a payable without paying cash.
- **Payment:** The company reduces the payable and cash.

Cash paid = beginning dividends payable + declarations - ending dividends payable.

Calculate cash paid to shareholders.

Declaration and payment occur separately

Source documents:

Comparative balance sheets: Dividends payable increased from $2,000 to $4,000.

Additional information: Zoomies declared $10,000 of dividends. Only declarations and payments changed the payable.

Beginning dividends payable + dividends declared - cash paid = ending dividends payable.

$2,000 + $10,000 - cash paid = $4,000.

Cash paid = $8,000. Report that amount as a financing outflow.

- Dividends distribute earnings to owners without reducing net income.
- The change in dividends payable therefore creates no operating adjustment.

Complete the financing section

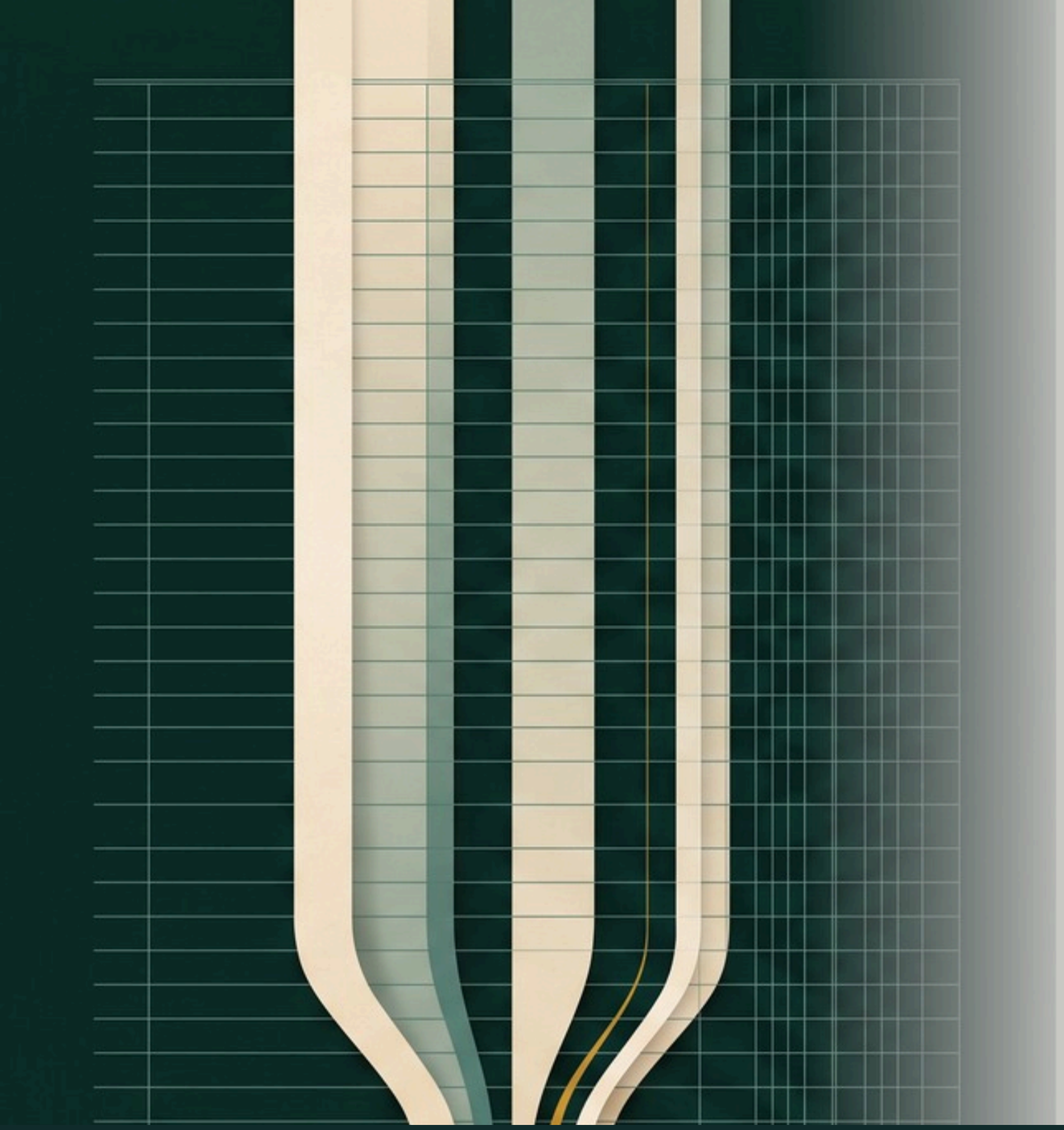
Source documents:

Additional information: Zoomies issued common stock for $12,000 cash.

Zoomies Pet Store | Financing activities for 2026 | US dollars

Financing activities	Amount
Proceeds from bank borrowing	$30,000
Principal repaid	($18,000)
Proceeds from issuing common stock	$12,000
Dividends paid	($8,000)
Net cash provided by financing activities	**$16,000**

The $12,000 stock issuance increased cash and equity without increasing revenue.



Complete statement and disclosures

Reconcile the cash totals and report the required disclosures.

Reconcile the three sections to cash

Source documents:

Comparative balance sheets: Cash increased from $24,000 to $36,500. Restricted cash increased from $6,000 to $10,000.

Completed section	Net cash flow
Operating activities	$36,500 inflow.
Investing activities	$36,000 outflow.
Financing activities	$16,000 inflow.

1. Calculate the net change from the three sections.
2. Calculate beginning and ending cash, including restricted cash.
3. Confirm that the activity totals equal the change in the combined cash balance.

Matching ending cash does not prove every cash flow is correct; offsetting errors can cancel.

Zoomies' complete statement of cash flows

Zoomies Pet Store | Year ended December 31, 2026 | US dollars

Cash flows	Amount
Operating activities	
Net income	$17,000
Depreciation expense	$16,000
Loss on equipment sale	$3,000
Credit loss expense	$3,000
Decrease in gross receivables, excluding write-offs	$6,000
Decrease in gift card liability	($3,000)
Increase in inventory	($12,000)
Increase in accounts payable	$7,000
Increase in store supplies	($1,000)
Increase in utilities payable	$500
Decrease in interest payable	($1,000)
Increase in income taxes payable	$1,000
Net cash provided by operating activities	**$36,500**
Investing activities	
Proceeds from equipment sale	$9,000
Cash paid for equipment	($45,000)
Net cash used in investing activities	**($36,000)**
Financing activities	
Proceeds from borrowing	$30,000
Principal repaid	($18,000)
Proceeds from issuing common stock	$12,000
Dividends paid	($8,000)
Net cash provided by financing activities	**$16,000**
Increase in cash and restricted cash	**$16,500**
Cash and restricted cash at beginning of year	$30,000
Cash and restricted cash at end of year	**$46,500**

1. Net change from the three sections.

$36,500 - $36,000 + $16,000 = $16,500 increase.

2. Beginning and ending cash totals.

Beginning: $24,000 + $6,000 = $30,000.
Ending: $36,500 + $10,000 = $46,500.

3. Reconciliation.

$46,500 - $30,000 = $16,500, matching the three activity totals.

Disclosures accompanying the statement

Cash restrictions

Of the $46,500 ending total, $10,000 is reserved for debt repayment in 2028. The internal $4,000 transfer created no cash flow.

Noncash financing of the van

The van cost $65,000. Zoomies paid $45,000 cash and issued a $20,000 seller note. Disclose the note portion separately.

Supplementary operating payments

Cash interest paid was $6,000, and cash income taxes paid were $6,000. The payments differ from expense because of the payable changes.

- **IFRS:** Income taxes paid are generally operating, except when specifically identifiable with an investing or financing transaction.

Next class: operating cash flows

Tuesday, October 13, 2026: Derive direct-method receipts and payments, then compare operating cash with net income.

Friday, October 9, 2026, at 11:59 PM: Initial company selections are due.

Sunday, October 11, 2026, at 11:59 PM: The Unit 3 review assignment is due.