Financial statements meanings overview

Finance

ASSIGN BUSTER

The following paper will talk about the income statement and what the income statement tells about the company including why this statement is important and what business decisions can be made using the income statement. Also, the paper will talk about the balance sheet and what the balance sheet tells about the company. Also, the reason the balance sheet is important and what business decisions can be will be covered. Lastly, it will talk about the statement of cash flows and what it tells about the company.

It will talk about what kind of business decisions can be made using the statement of cash flows. In the conclusion the paper will provide the information how data provided in the statements can assist in making business decisions and what information is not provided that can assist managerial decision making. As it was indicated by FASB, the main purpose of financial reporting is to provide financial information about company performance. The income statement is one of the most important financial statements because of its predictive value and qualitative characteristics.

The income statement is also known as profit and loss statement that records company revenues and expenses during a certain period of time. The reason the income statement has very high importance is because it can determine the company’s operating performance during a specific period of time. “ Specific items that are causing unexpected expenditures can be pinpointed, such as phone, fax, mail, or supply expenses. Income statements can also track dramatic increases in product returns or cost of goods sold as a percentage of sales” (Business Town, 2010).

Also because it provides so much important information about the business, the income statement is required by lenders, investors, and vendors. There are many users that can make their business decisions based on an income statement of the organization. The bank can use income statement information to determine if a company produces enough revenue to be able to pay back a loan. An owner of the company can determine if the company makes enough revenue to hire new employees or to look at the sales performance for the month. The balance sheet should disclose a company's wealth at a point in time.

These measurement techniques of balance sheet can be summarized as past oriented—historical; current oriented—replacement amounts; and future oriented—expected amounts" (Schroeder, Clark, & Cathey, 2005). A balance sheet can be defined as a summary of financial balances of the organization. There are three main elements of balance sheet: assets, liabilities, and equity. Usually the following classifications are presented in the typical balance sheet: Assets Current assets •Investments •Property, plant, and equipment •Intangible assets •Other assets Liabilities •Current liabilities •Long-term liabilities •Other liabilities Stockholders' equity •Capital stock •Additional paid-in capital •Retained earnings (Schroeder, Clark, & Cathey, 2005)

As well as income statements, the balance sheet will help lenders, creditors, and investors to determine profitability of the company and help to decide whether to invest in the company or not. The balance sheet statement will help to detail the history of the business, including the profit and loss, the

seasonality of earnings, and other factors that are unique to the business" (Business Town, 2010).

The statement of the cash flow is also very importantfinancial statement. The purpose of this statement is to record cash generated during the specific time period. The statement of cash flow reports cash that was generated and used in following categories: operating activities, investing activities, and financial activities. The FASB has emphasized the importance of cash flow information in its deliberations. SFAC No 1 states that effective financial reporting must enable investors, creditors, and other users to assess cash flow prospects and evaluate liquidity, solvency, and flow of funds" (Schroeder, Clark, & Cathey, 2005). The statement of the cash flows tells the company's liquidity, solvency, and its financial flexibility. As well as other financial statements discussed in this paper, the statement of the cash flow helps investors to make right decision based on provided information.

The statement of the cash flow also helps predict and evaluate future returns or potential risks. " In 1987, the FASB issued SFAS No. 95, " Statement of Cash Flows. " This statement established standards for cash flow reporting , as a result, all business enterprises are now required to present a statement of cash flows in place of the statement of changes in financial positions as part of the full set of financial statements" (Schroeder, Clark, & Cathey, 2005). The main purpose of the statement of cash flow is to provide information about cash receipts and cash payments during selected period of time.

This information is necessary for investors and creditors, so they can see a potential picture of prospective cash receipts. In conclusion, financial statements are very important for any business, starting from small startup companies to global corporations. Financial statements can help determine an organization's problem as well as identify a corrective action. Understanding of financial statements is also very important because it can tell accurate information about what happened in the past. By using financial statements, it is possible to analyze and evaluate financial activity from the past and forecast the most likely future activity.

Besides financial statements there is other non financial information that can assist in making business decisions and assist in managerial decision making. It is important to compare both, financial and nonfinancial measures to see a better picture of the organization as a whole. It is important for managers to include nonfinancial performance standards in their analysis of operations because not every aspect of corporate activity can be expressed in terms ofmoney. Nonfinancial performance measures relate to manufacturing and production, sales and marketing, people, research and development, and theenvironment.