MULTI-STEP INCOME STATEMENT

Key Terms and Concepts to Know

Single-Step Income Statement
• Total revenue – total expenses = Net Income

Multi-Step Income Statement
• Separates revenues into operating and non-operating
• Separates expenses into cost of goods sold, operating and non-operating
• May further divides Operating Expenses into Selling Expenses and Administrative Expenses
• Adds subtotals to increase usefulness of income statement

Comprehensive Income Statement
• Certain other gains or losses are not included in net income but are included in the more inclusive income measure, Comprehensive Income
• Gains or losses result from adjustments such as marking certain assets to their fair values

Cost of Goods Sold:
• Inventory that has been sold becomes an expense, Cost of Goods Sold, in the period of sale.

Gross Profit:
• Gross Margin = Gross Profit = Net Sales – Cost of Goods Sold
• Gross Margin ratio = Gross Margin / Net Sales
• First key indicator of profitability
Key Topics to Know

Single-Step Income Statement

- Very simple format:
  - One section for total revenue, including operating and non-operating revenues
  - Second section for total expenses, including operating and non-operating expenses
  - Single step is to subtract total expenses from total revenues to determine net income

Multi-Step Income Statement

- Highlights the components of net income:
  - Separates revenues into operating and non-operating
  - Separates expenses into cost of goods sold, operating and non-operating
  - May further divides Operating Expenses into Selling Expenses and Administrative Expenses
  - Operating results are reported as Income from Operations
  - Adds subtotals to increase usefulness of income statement
- More complex format:
  - Net Sales = Sales + transportation-in – sales returns and allowances – sales discounts
  - Gross Profit or Gross Margin = Net Sales – Cost of Goods sold
  - Operating Income = Gross Profit – Operating Expenses (end of operating revenues and expenses)
  - Net Income = Operating Income + Non-operating Revenues – Non-operating Expenses – Income Tax Expense
  - Comprehensive Income = Net Income + Other Comprehensive Income – Other Comprehensive Expenses

Key changes compared to the single-step income statement include:
- Gross-to-Net Sales to account for contra-revenue accounts
- Gross Profit to report the margin or profit remaining after covering the cost of merchandise sold that is available to cover operating expenses
- May also separating Operating Expenses into Selling Expenses and Administrative Expenses to provide an additional level detail
• Income from Operations to report the profitability of the company’s reason for being in business
• Other Income and Other Expense to identify the revenues and expenses not related to the company’s reason for being in business
• Income tax expense would be reported between net other revenues and expenses and Net Income.

Gross Sales $500,000
Less: Sales Returns & allowances $5,000
Less: Sales Discounts 3,000 8,000
Net Sales 492,000
Cost of Merchandise Sold 294,000
Gross Profit 198,000
Operating Expenses:
   Selling Expenses 50,000
   Admin Expense 45,000
   Total Operating Expenses 95,000
Income from Operations 103,000
Other Income:
   Interest Revenue 1,000
Other Expenses:
   Interest Expense 700 300
Income tax expense 30,000
Net Income $73,700

Example #1

A portion of the adjusted trial balance for the G Company is shown below.

Sales (net of $8,000 sales discounts and $24,500 sales returns and allowances) $417,500
Cost of goods sold $210,000
Salaries expense 38,000
Depreciation expense—building 40,000
Advertising expense 12,300
Office supplies expense 3,500
Gain on disposal of store equipment 3,000
Interest expense 1,000

Required: a) Prepare a single-step income statement b) Prepare a multiple-step income statement
### Solution #1

#### a)

**G Company**  
**Income Statement**  
**For the year ended December 31**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Revenues</strong></td>
<td></td>
</tr>
<tr>
<td>Net Sales</td>
<td>$417,500</td>
</tr>
<tr>
<td>Gain on disposal of store equipment</td>
<td>3,000</td>
</tr>
<tr>
<td><strong>Total revenues</strong></td>
<td><strong>$420,500</strong></td>
</tr>
<tr>
<td><strong>Expenses:</strong></td>
<td></td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>$210,000</td>
</tr>
<tr>
<td>Sales salaries expense</td>
<td>38,000</td>
</tr>
<tr>
<td>Depreciation expense—building</td>
<td>40,000</td>
</tr>
<tr>
<td>Advertising expense</td>
<td>12,300</td>
</tr>
<tr>
<td>Office supplies expense</td>
<td>3,500</td>
</tr>
<tr>
<td>Interest expense</td>
<td>1,000</td>
</tr>
<tr>
<td><strong>Total expenses</strong></td>
<td><strong>304,800</strong></td>
</tr>
<tr>
<td><strong>Net income</strong></td>
<td><strong>$115,700</strong></td>
</tr>
</tbody>
</table>
### G Company

#### Income Statement

**For the year ended December 31**

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>$450,000</td>
</tr>
<tr>
<td>Less: Sales discounts</td>
<td>$8,000</td>
</tr>
<tr>
<td>Sales returns and allowances</td>
<td>24,500</td>
</tr>
<tr>
<td>Net sales</td>
<td>$417,500</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>$210,000</td>
</tr>
<tr>
<td>Gross profit</td>
<td>207,500</td>
</tr>
<tr>
<td>Operating expenses</td>
<td></td>
</tr>
<tr>
<td>Sales salaries expense</td>
<td>$38,000</td>
</tr>
<tr>
<td>Depreciation expense—building</td>
<td>40,000</td>
</tr>
<tr>
<td>Advertising expense</td>
<td>12,300</td>
</tr>
<tr>
<td>Office supplies expense</td>
<td>3,500</td>
</tr>
<tr>
<td>Total operating expenses</td>
<td>93,800</td>
</tr>
<tr>
<td>Income from operations</td>
<td>113,700</td>
</tr>
<tr>
<td>Other revenues and gains (expenses and losses)</td>
<td></td>
</tr>
<tr>
<td>Gain on disposal of store equipment</td>
<td>3,000</td>
</tr>
<tr>
<td>Interest expense</td>
<td>(1,000)</td>
</tr>
<tr>
<td>Net income</td>
<td>$115,700</td>
</tr>
</tbody>
</table>
Practice Problems

Practice Problem #1

B Company provided an adjusted trial balance as of December 31.

<table>
<thead>
<tr>
<th>Account</th>
<th>Debit</th>
<th>Credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>$34,400</td>
<td></td>
</tr>
<tr>
<td>Merchandise inventory</td>
<td>32,000</td>
<td></td>
</tr>
<tr>
<td>Inventory returns estimated</td>
<td>4,000</td>
<td></td>
</tr>
<tr>
<td>Store equipment</td>
<td>75,900</td>
<td></td>
</tr>
<tr>
<td>Accumulated depreciation—store equipment</td>
<td>$22,000</td>
<td></td>
</tr>
<tr>
<td>Office equipment</td>
<td>60,000</td>
<td></td>
</tr>
<tr>
<td>Accumulated depreciation—office equipment</td>
<td>15,000</td>
<td></td>
</tr>
<tr>
<td>Accounts payable</td>
<td>35,000</td>
<td></td>
</tr>
<tr>
<td>Sales refund payable</td>
<td>7,000</td>
<td></td>
</tr>
<tr>
<td>Notes payable</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>Common stock</td>
<td>1,000</td>
<td></td>
</tr>
<tr>
<td>Retained earnings</td>
<td>109,700</td>
<td></td>
</tr>
<tr>
<td>Dividends</td>
<td>48,000</td>
<td></td>
</tr>
<tr>
<td>Sales</td>
<td>325,000</td>
<td></td>
</tr>
<tr>
<td>Sales discounts</td>
<td>6,000</td>
<td></td>
</tr>
<tr>
<td>Sales returns and allowances</td>
<td>16,500</td>
<td></td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>195,000</td>
<td></td>
</tr>
<tr>
<td>Selling expenses</td>
<td>32,500</td>
<td></td>
</tr>
<tr>
<td>General and administrative expenses</td>
<td>19,800</td>
<td></td>
</tr>
<tr>
<td>Interest expense</td>
<td>600</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>$524,700</td>
<td>$524,700</td>
</tr>
</tbody>
</table>

Required:  

a) Prepare a single-step income statement  
b) Prepare a multiple-step income statement
Practice Problem #2

Following are 6 statements about income statements.

1. __________________ expenses are those costs that support a company's overall operations and include expenses related to accounting, human resource management, and financial management.

2. A __________________ income statement format shows detailed computations of net sales and other costs and expenses, and reports subtotals for various classes of items.

3. A __________________ income statement includes cost of goods sold as another expense and shows only one subtotal for total expenses.

4. Non-operating activities reported on the income statement that includes interest, dividend, and rent revenues, and gains from asset disposals are called ___________________.

5. Non-operating activities reported on the income statement that includes interest expense, losses from asset disposals, and casualty losses are called ___________________.

6. When a company has no reportable non-operating activities, its income from operations is reported as ___________________.

Required: Fill in the blanks with the correct answers.
**Practice Problem #3**

T Company reported the following information on its income statement for the first quarter of the year.

<table>
<thead>
<tr>
<th></th>
<th>January</th>
<th>February</th>
<th>March</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>$375,000</td>
<td>$750,000</td>
<td>?</td>
</tr>
<tr>
<td>Sales returns and allowances</td>
<td>32,000</td>
<td>?</td>
<td>25,000</td>
</tr>
<tr>
<td>Sales discounts</td>
<td>12,000</td>
<td>9,000</td>
<td>15,000</td>
</tr>
<tr>
<td>Net sales</td>
<td>?</td>
<td>736,000</td>
<td>?</td>
</tr>
<tr>
<td>Cost of merchandise sold</td>
<td>255,000</td>
<td>?</td>
<td>620,000</td>
</tr>
<tr>
<td>Gross profit</td>
<td>?</td>
<td>310,000</td>
<td>185,000</td>
</tr>
</tbody>
</table>

Required: Calculate the missing information.

**Practice Problem #4**

A multi-step income statement showed net sales of $870,000, cost of goods sold of $376,000, and total operating expenses of $330,000 for the fiscal year ended December 31, 2016.

Required:  

a) What was the gross profit?  
b) What was the net income from operations?
True / False Questions

1. A multiple-step income statement shows detailed computations of net sales and reports subtotals for various groups of items.
   True   False

2. Operating expenses in a multiple-step income statement are classified into two categories: selling expenses and cost of goods sold.
   True   False

3. Expenses related to accounting, human resource management, and financial management are classified as non-operating expenses in a multiple-step income statement.
   True   False

4. When a company preparing a multiple-step income statement has no reportable non-operating activities, its income from operations is simply labeled net income.
   True   False

5. A single-step income statement includes cost of goods sold as another expense and shows only one subtotal for total expenses.
   True   False

6. Advertising expense is reported as part of operating expenses in the seller's multiple-step income statement.
   True   False

7. Comprehensive Income includes gains and losses also included in the determination of net income.
   True   False

8. If a company has beginning inventory of $15,000, purchases during the year of $75,000, and ending inventory of $20,000, cost of goods sold equals $70,000.
   True   False

   True   False

10. Sales revenue minus cost of goods sold is referred to as operating income.
    True   False
Multiple Choice Questions

1. An income statement that includes cost of goods sold as another expense and shows only one subtotal for total expenses is a:
   a) Single-step income statement.  
   b) Balanced income statement.  
   c) Multiple-step income statement.  
   d) Simplified income statement.

2. Expenses that support the overall operations of a business and include the expenses relating to accounting, human resource management, and financial management are called:
   a) Cost of goods sold  
   b) Operating expenses.  
   c) Non-operating expenses  
   d) Comprehensive expenses

3. P Company had cash sales of $94,275, credit sales of $83,450, sales returns and allowances of $1,700, and sales discounts of $3,475. P Company's net sales for this period equal:
   a) $94,275.  
   b) $174,250.  
   c) $172,550.  
   d) $176,025.

4. Multiple-step income statements:
   a) Are required by the FASB and IASB.  
   b) List cost of goods sold as an operating expense.  
   c) Are only used by service businesses  
   d) Contain more detail than a simple listing of revenues and expenses.

5. S Company has net sales of $752,000 and cost of goods sold of $543,000. Its net income is $17,530. The company's gross margin and operating expenses, respectively, are:
   a) $209,000 and $191,470  
   b) $191,470 and $209,000  
   c) $525,470 and $227,000  
   d) $227,000 and $525,470
6. G Company had $800,000 in net sales, $350,000 in gross profit, and $200,000 in operating expenses. Cost of goods sold equals:
   a) $150,000.
   b) $450,000.
   c) $800,000.
   d) $350,000.

7. C Company had $800,000 in sales, sales discounts of $12,000, sales returns and allowances of $18,000, cost of goods sold of $380,000, and $275,000 in operating expenses. Gross profit equals:
   a) $770,000.
   b) $115,000.
   c) $390,000.
   d) $402,000.

8. Which of the following would be classified as Other Income or Other Expense?
   a) Advertising Expense
   b) Interest Expense
   c) Transportation Out
   d) Cost of merchandise sold

9. Gross Margin is calculated as:
   a) Sales less cost of merchandise sold
   b) Sales less merchandise inventory
   c) Sales less expenses
   d) Sales less operating expenses

10. A Company’s gross profit ratio has steadily declined for 5 years while the net profit ratio has remained constant. The most likely reason for this pattern is:
    a) Cost of merchandise sold and operating expenses both increased each year
    b) Selling price and operating expenses have both decreased each year
    c) Cost of merchandise sold and operating expenses both decreased each year
    d) Selling price decreased and operating expenses increased each year
# Practice Problem #1

a) B Company  
**Income Statement**  
For the year ended December 31  

<table>
<thead>
<tr>
<th>Revenues:</th>
<th></th>
<th>Expenses:</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Net sales</td>
<td>302,500</td>
<td>Cost of goods sold</td>
<td>195,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Operating expenses</td>
<td>52,300</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Interest expense</td>
<td>600</td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>Total expenses</strong></td>
<td><strong>247,900</strong></td>
</tr>
<tr>
<td></td>
<td></td>
<td>Net income</td>
<td><strong>$54,600</strong></td>
</tr>
</tbody>
</table>

b) B Company  
**Income Statement**  
For the year ended December 31  

<table>
<thead>
<tr>
<th>Sales</th>
<th>$325,000</th>
<th>Less: Sales discounts</th>
<th>$6,000</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Sales returns and allowances</td>
<td>16,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>Net sales</strong></td>
<td>302,500</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Cost of goods sold</td>
<td>195,000</td>
</tr>
<tr>
<td></td>
<td></td>
<td>Gross profit</td>
<td>107,500</td>
</tr>
<tr>
<td>Operating expenses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Selling expenses</td>
<td>32,500</td>
<td>General and administrative expenses</td>
<td>19,800</td>
</tr>
<tr>
<td>Total operating expenses</td>
<td>52,300</td>
<td>Income from operations</td>
<td>55,200</td>
</tr>
<tr>
<td>Other expenses</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Interest expense</td>
<td></td>
<td></td>
<td>600</td>
</tr>
<tr>
<td>Net income</td>
<td></td>
<td></td>
<td><strong>$54,600</strong></td>
</tr>
</tbody>
</table>
**Practice Problem #2**

1. Operating  
2. Multiple-step  
3. Single-step  
4. Other revenues and gains  
5. Other expenses and losses  
6. Net income

**Practice Problem #3**

January
Sales $375,000  
- Sales Returns & Allowances (32,000)  
- Sales Discounts (12,000)  
Net Sales 331,000  
- Cost of Merchandise Sold (255,000)  
Gross Profit $76,000

February
Sales $750,000  
- Sales Returns & Allowances  
  x 741,000 – x = 736,000  
- Sales Discounts (9,000)  
  x = 5,000  
Net Sales 736,000  
- Cost of Merchandise Sold  
  y y = 426,000  
Gross Profit $310,000

March
Sales X  
- Sales Returns & Allowances (25,000)  
- Sales Discounts (15,000)  
  y – 620,000 = 185,000  
Net Sales Y  
  y = 805,000  
- Cost of Merchandise Sold (620,000)  
  x = 845,000  
Gross Profit $185,000
### Practice Problem #4

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Sales</td>
<td>$870,000</td>
</tr>
<tr>
<td>Cost of Goods Sold</td>
<td>376,000</td>
</tr>
<tr>
<td>Gross Margin</td>
<td>494,000</td>
</tr>
<tr>
<td>Operating Expenses</td>
<td>330,000</td>
</tr>
<tr>
<td>Net Income from Operations</td>
<td>$164,000</td>
</tr>
</tbody>
</table>
Solutions to True / False Problems

1. True
2. False – operating expenses are classified as either selling expenses or administrative expenses
3. False – these are operating expenses
4. True
5. True
6. True
7. False – comprehensive income includes gains and losses not included elsewhere on the income statement
8. True
9. True
10. False - sales revenue minus cost of goods sold equals gross profit.
### Solutions to Multiple Choice Questions

1. A  
2. B  
3. C  
4. D  
5. A  
6. B  
7. C  
8. B  
9. A  
10. B