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Adaptation to Gai:
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Theoretical Classes nº 5 and nº 6

Chapter 3
Operational Decisions and the Income Statement

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In the end of this chapter you should…

✓ Understand the relation between the Income Statement and the business **(page 137 and 138)**;

✓ Explain the way as the business operations affect the elements of the income Statement **(page 139 to 143)**;

✓ Explain the concept of accrual basis and apply the recognition criteria's for revenues and expenses **(page 144 to 149)**;

In the end of this chapter you should…

✓ Apply the process of transaction analysis to see and record the effect od operational activities in the financial statements **(page 150 to 157)**.
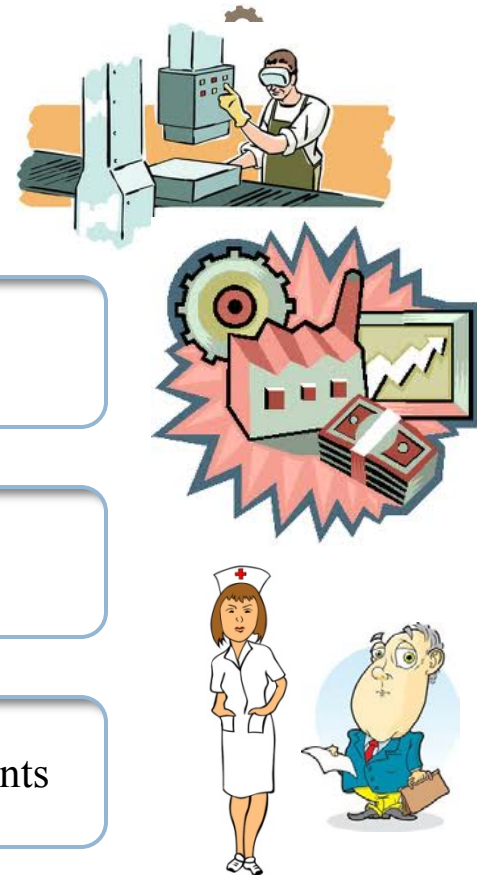
To understand the information presented in **Income Statement** it is necessary understand:

How do business operations affect Income Statement

How do business operations are measured

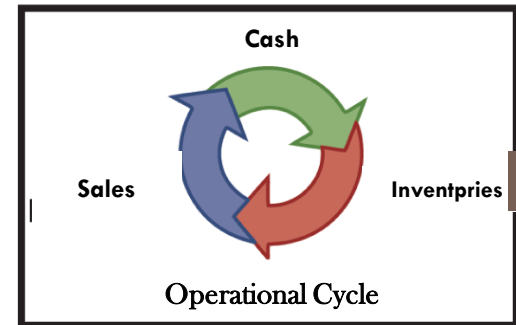How do business operations are recorded in the financial statements

Effects of activities in the Income Statement

Operating Activities

Cash

Sales

Inventpries

Operational Cycle

Financing Activities

Investing Activities

Effects of activities in the Income Statement

Entity: Portucel	2006	2010	Var.
Income Statement			
Sells and rendered services	**1.080.658**	**1.385.455**	**28%**
Cost of Sales	**(359.275)**	**(522.858)**	46%
External Supplies and services	**(300.164)**	**(336.907)**	12%
Employment costs	**(107.850)**	**(127.020)**	18%
Other revenues and gains	10.560	15.072	36%
Other expenses and losses	(37.457)	(14.740)	-61%
Earnings Before Depreciation, Amortiz. Int. and taxes (EBITDA)/	286.472	399.002	39%
Depreciation and amortization expenses	**(77.161)**	**(121.185)**	57%
Impairment of tangible and intangible assets	0	0	0%
Earnings before Interests and Taxes (EBIT)/Operational results	**209.311**	**277.817**	**33%**
Investment Income/revenue	0	0	0%
Interests/Financial Expenses	(26.456)	(20.080)	-24%
Earnings before taxes	181.855	257.737	42%
Income tax expense	(58.184)	(47.157)	-19%
Net Income	**124.671**	**210.580**	**69%**

Elements of IS

Concept

Income: are **enhancements of assets** or **decreases of liabilities** that result in **increases in equity**, other than those relating to contributions from equity participants.

Revenues: are generated by the operating (ordinary) activities of each entity (sells, interest earned, dividends earned, royalties and rents)

Gains: include, for instance, earnings from selling non-current assets.

Income

Elements of IS

Concept

Expenses: are **reductions of assets** or **incurrences of liabilities** that result in **decreases in equity**, other than those relating to distributions to equity participants.
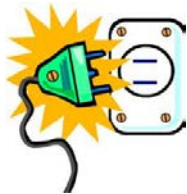
Expenses that are originated by ordinary/operating activities: for instance, cost of sales, external services and supplies, salaries expense, depreciations

Losses: for instance, from selling non-current assets, as well as disasters or fires.

Expenses

Elements of DR

SNC
CNC

Model include in *Portaria 986/2009*, published in *Diário da República* a *7/Setembro/2009*

IASB
IAS - IFRS

There is no pre-defined model (Minimum Content - IAS 1).

Entidade: ....
DEMONSTRAÇÃO (INDIVIDUAL/CONSOLIDADA) DOS RESULTADOS POR NATUREZAS
PERÍODO FINDO EM XX DE YYYYYYY DE 200N   *UNIDADE MONETÁRIA* (1)

| RENDIMENTOS E GASTOS	NOTAS	PERÍODOS	
		N	N-1
Vendas e serviços prestados		+	+
Subsídios à exploração		+	+
Ganhos/perdas imputados de subsidiárias, associadas e empreendimentos conjuntos		+ / –	+ / –
Variação nos inventários da produção		+ / –	+ / –
Trabalhos para a própria entidade		+	+
Custo das mercadorias vendidas e das matérias consumidas		–	–
Fornecimentos e serviços externos		–	–
Gastos com o pessoal			
Imparidade de inventários (perdas/reversões)		– / +	– / +
Imparidade de dívidas a receber (perdas/reversões)		– / +	– / +
Provisões (aumentos/reduções)		– / +	– / +
Imparidade de investimentos não depreciáveis/amortizáveis (perdas/reversões)		– / +	– / +
Aumentos/reduções de justo valor		+ / –	+ / –
Outros rendimentos e ganhos		+	+
Outros gastos e perdas		–	–
Resultado antes de depreciações, gastos de financiamento e impostos		=	=
Gastos/reversões de depreciação e de amortização		– / +	– / +
Imparidade de investimentos depreciáveis/amortizáveis (perdas/reversões)		– / +	– / +
Resultado operacional (antes de gastos de financiamento e impostos)		=	=
Juros e rendimentos similares obtidos		+	+
Juros e gastos similares suportados		–	–
Resultado antes de impostos		=	=
Imposto sobre o rendimento do período		– / +	– / +
Resultado líquido do período		=	=
Resultado das actividades descontinuadas (líquido de impostos) incluído no resultado líquido do período			
Resultado líquido do período atribuível a: (2) Detentores do capital da empresa-mãe Interesses minoritários		=	=
Resultado por acção básico			

(1) – O euro, admitindo-se, em função da dimensão e exigências de relato, a possibilidade de expressão das quantias em milhares de euros
(2) Esta informação apenas será fornecida no caso de contas consolidadas

**Accrual Basis /
Accrual Accounting**

The effects of transactions (income and expenses) are recognized when the transaction that causes them **occurs**, not necessarily when cash is received or paid. Thus, they should be recorded in those financial statements that are related with the occurrence of those revenues and expenses (when they happened).
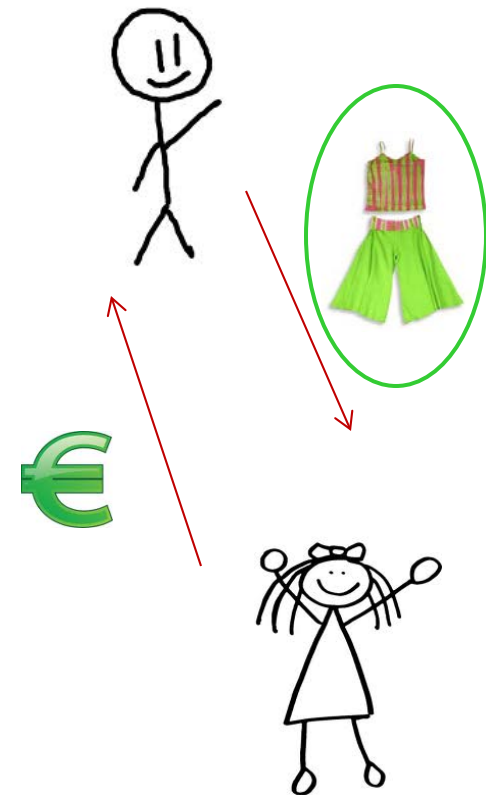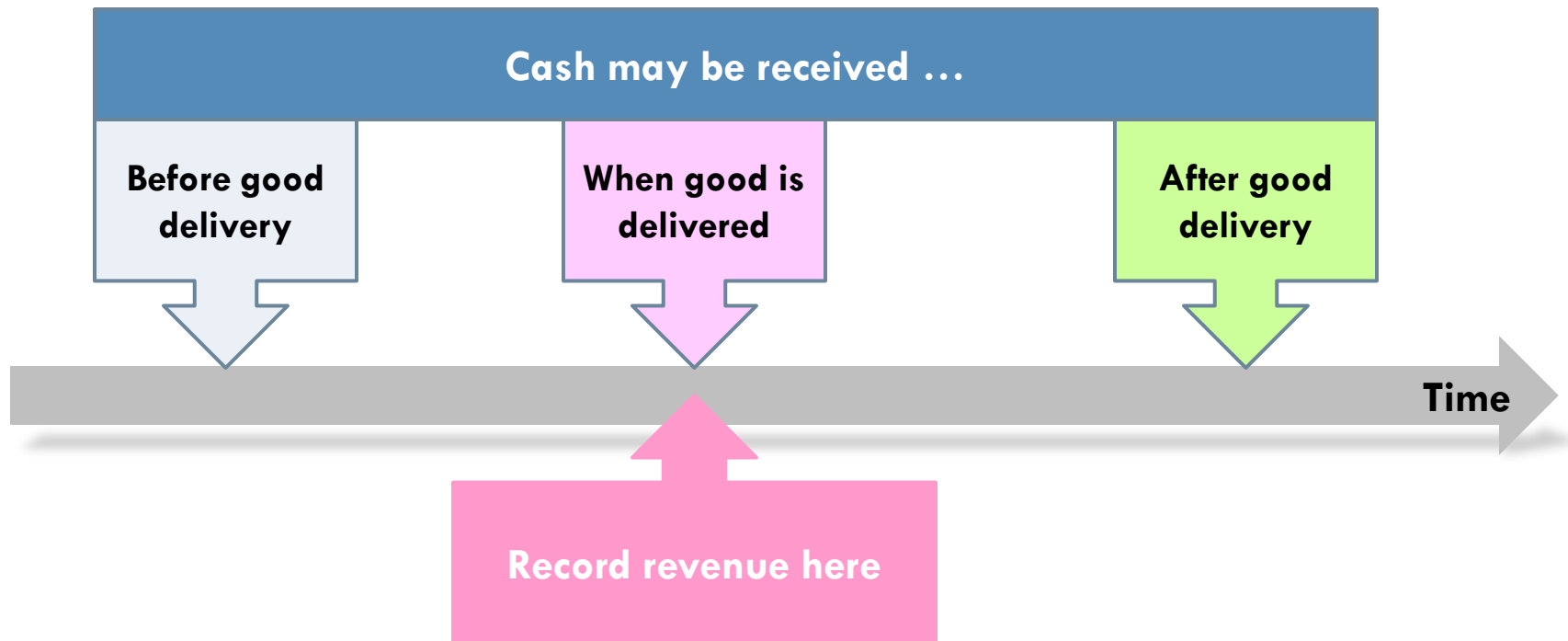
Elements of DR

Recognition

Revenues from Sales: shall be recognized when all the following conditions have been satisfied:

(a) the entity has transferred to the buyer the significant risks and rewards of ownership of the goods;
(b) the entity retains no effective control over the goods sold;
(c) the amount of revenue can be measured reliably;
(d) it is probable that the economic benefits associated with the transaction will flow to the entity.
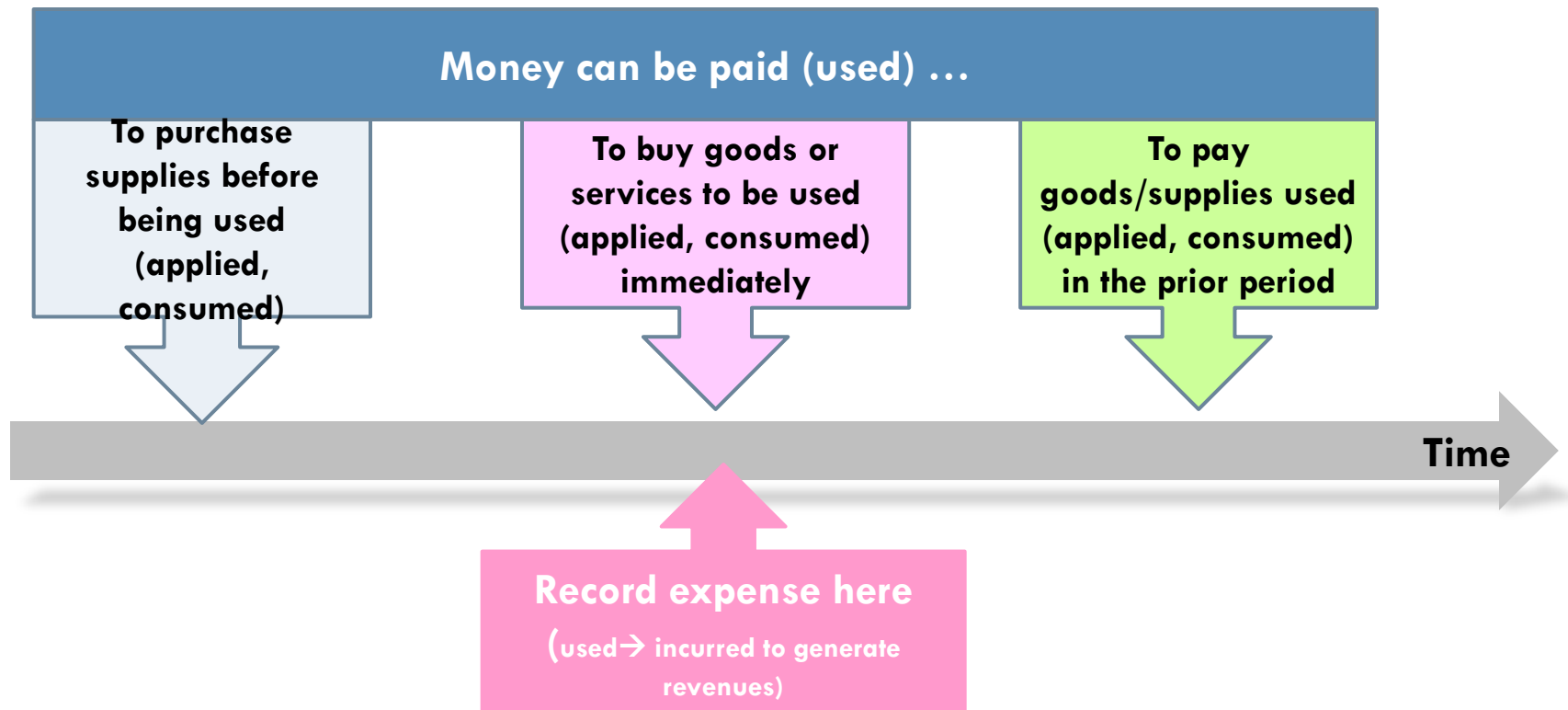
Elements of IS

Recognition

Expenses: Expenses are recognized in the income statement on the basis of a direct association between the costs incurred and the earning of specific items of income. This process is commonly referred to as matching.

Money can be paid (used) …

To purchase supplies before being used (applied, consumed)

To buy goods or services to be used (applied, consumed) immediately

To pay goods/supplies used (applied, consumed) in the prior period

Time

Record expense here

(used→ incurred to generate revenues)

Analysis of transactions:

analysis process to determine the effect of a transaction

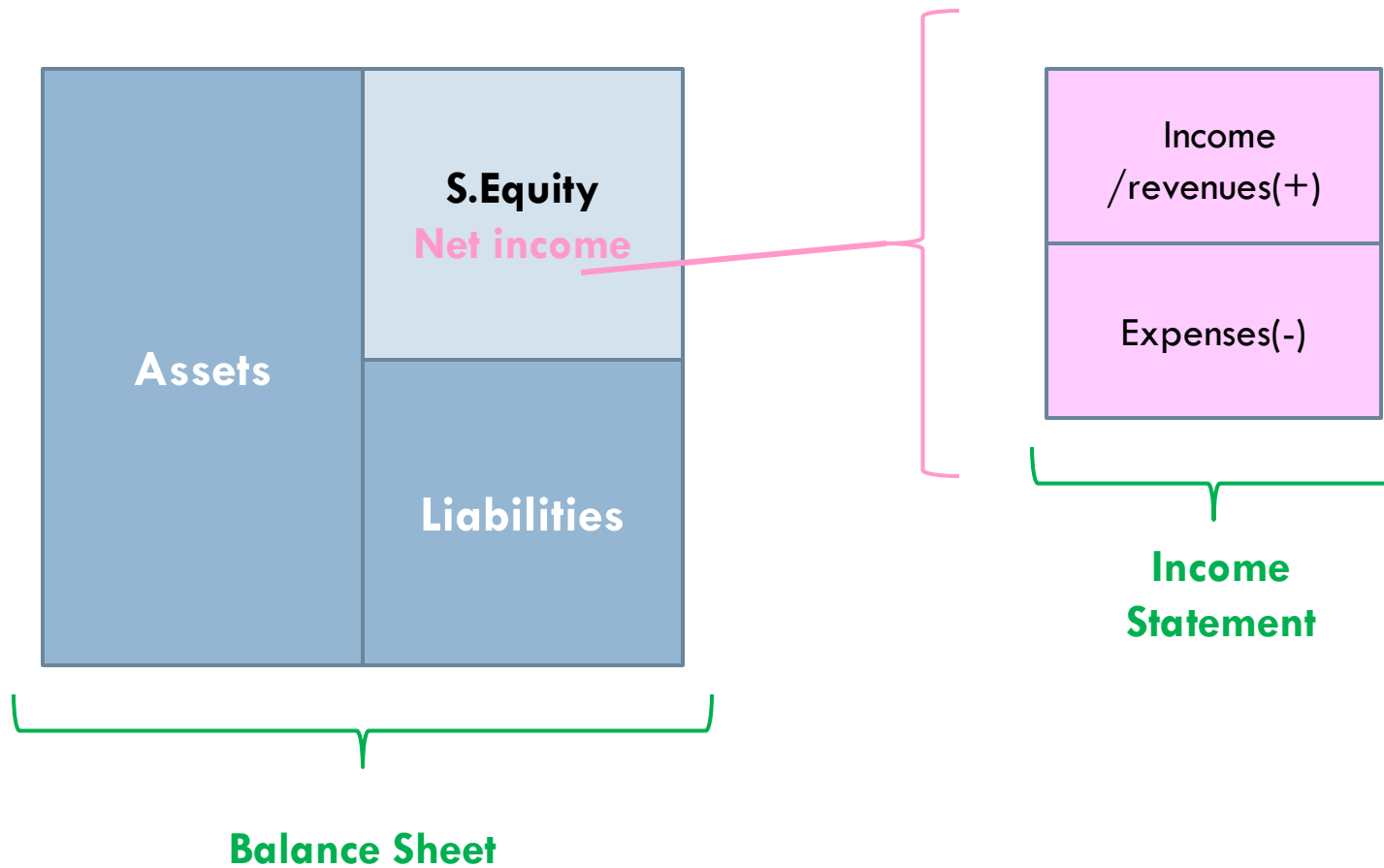in terms of the fundamental accounting equation**.**

| Assets | = | Liabilities | + | Shareholders equity |

Assets = Liabilities + SE (…,NI)

Debit	Credit
+	-

Debit balances

Debit	Credit
-	+

Credit balances

Net Income

Expenses

Income

Debit | Credit

Debit | Credit

+ | -

- | +

Debit balances
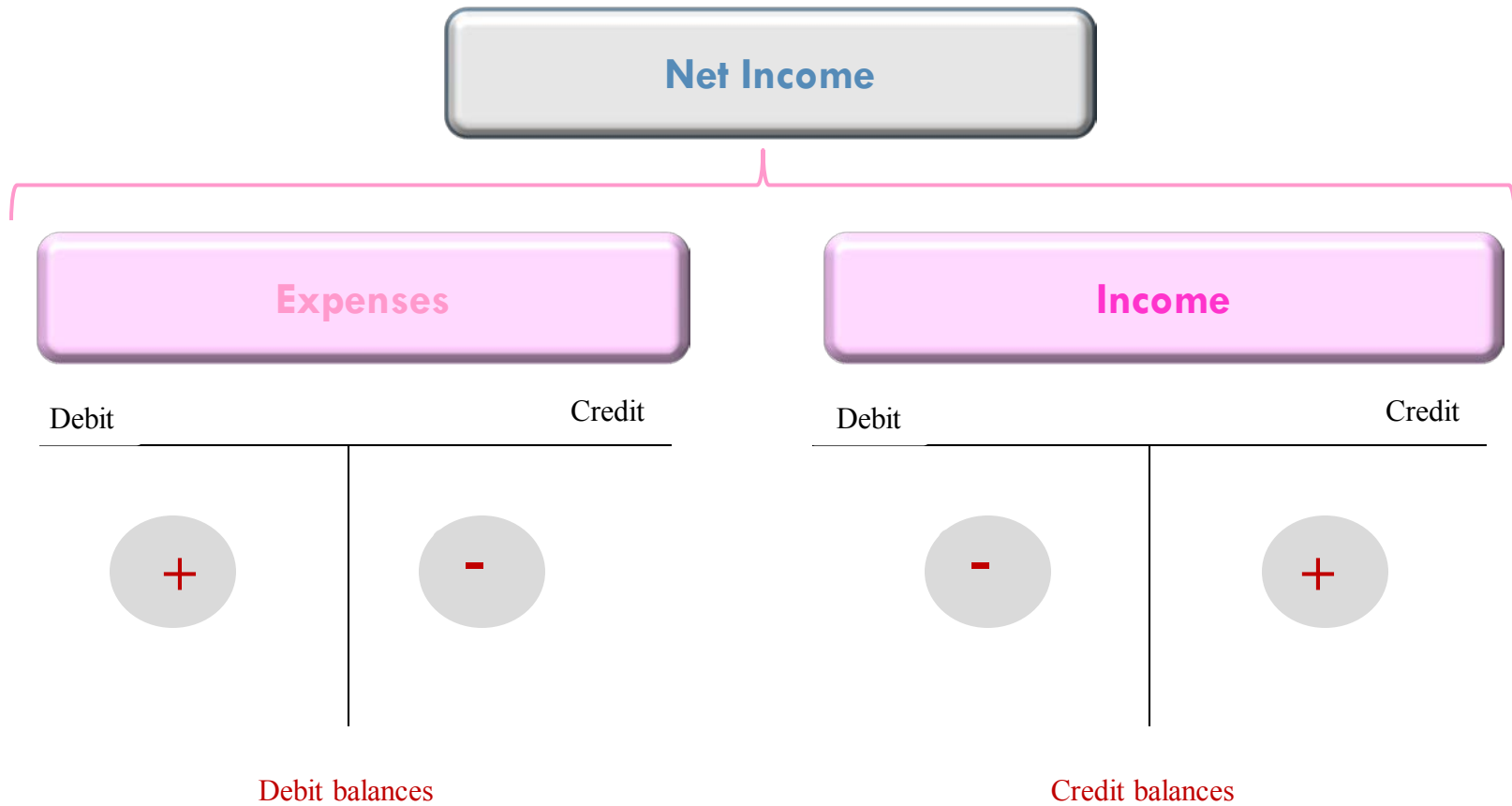
Credit balances

Recording the effect of the transaction

Assets	=	Liabilities	+	Shareholders Equity
Is debited by ↑		Is credited by ↑		Is credited by ↑
Is credited by ↓		Is debited by ↓		Is debited by ↓
The accounts have debit balance		The accounts have credit balance		The accounts have credit balance

Recording the effect of the transaction

Expenses	Income
Is debited by ↑	Is credited by ↑
Is credited by ↓	Is debited by ↓
The accounts have debit balance	The accounts have credit balance

Recording the effect of the transaction

1. Inventories sold by 500.000 euros, immediately received.

Data	Descrição	Débito	Crédito	Valor
	Sale of inventories	Cash	Sales	500.000

Debit   **Cash**   Credit   Debit   **Sales**   Credit

(1) 500.000   **500.000 (1)**

Recording the effect of the transaction

2. **The cost of inventories used in generating sales is 300.000 euros**

Data	Descrição	Débito	Crédito	Valor
	Cost of goods sold	Cost of sales	Inventories	300.000

Cost of sales

Debit   Credit

(2) 300.000

Inventories

Debit   Credit

300.000 (2)

Recording the effect of the transaction

3. **Payment of salaries in the amount of 50.000 euros**

Data	Descrição	Débito	Crédito	Valor
	Salaries paid	Emplyee expense	Cash	50.000

Employee Expense

Debit	Credit
(3) 50.000	

Cash

Debit	Credit
	50.000 (3)

End of chapter 3