

Ron and Lisa Smith are examining the following statement of cash flows for Carpino Company for the year ended January 31, 2008.

CARPINO COMPANY
Statement of Cash Flows
For the Year Ended January 31, 2008

Sources of cash	
From sales of merchandise	\$380,000
From sale of capital stock	420,000
From sale of investment (purchased below)	80,000
From depreciation	55,000
From issuance of note for truck	20,000
From interest on investments	6,000
Total sources of cash	<u>961,000</u>
Uses of cash	
For purchase of fixtures and equipment	330,000
For merchandise purchased for resale	258,000
For operating expenses (including depreciation)	160,000
For purchase of investment	75,000
For purchase of truck by issuance of note	20,000
For purchase of treasury stock	10,000
For interest on note payable	3,000
Total uses of cash	<u>856,000</u>
Net increase in cash	<u>\$ 105,000</u>

Ron claims that Carpino's statement of cash flows is an excellent portrayal of a superb first year with cash increasing \$105,000. Lisa replies that it was not a superb first year. Rather, she says the year was an operating failure, that the statement is presented incorrectly, and that \$105,000 is not the actual increase in cash. The cash balance at the beginning of the year was \$140,000.

Instructions

Divide the class into groups, answer the following.
Using the data provided, prepare a statement of cash flows in proper form using the indirect method. The only noncash items in the income statement are depreciation and the gain from the sale of the investment.
With whom do you agree, Ron or Lisa? Explain your position.

HARRIS CORPORATIONBalance Sheet (partial)
December 31, 2008

Paid in capital	
Capital stock	
Preferred stock, authorized 1,000,000 shares cumulative, \$100 par value, \$8 per share, 6,000 shares issued and outstanding	\$ 600,000
Common stock, authorized 5,000,000 shares, \$1 par value, 3,000,000 shares issued, and 2,700,000 outstanding	3,000,000
Total capital stock	<u>3,600,000</u>
Additional paid-in capital	
In excess of par value—preferred stock	\$ 50,000
In excess of par value—common stock	<u>25,000,000</u>
Total additional paid-in capital	25,050,000
Total paid-in capital	<u>28,650,000</u>
Retained earnings	900,000
Total paid-in capital and retained earnings	<u>29,550,000</u>
Less: Common treasury stock (300,000 shares)	<u>9,300,000</u>
Total stockholders' equity	<u>\$20,250,000</u>

At the meeting, stockholders have raised a number of questions regarding the stockholders' equity section.

Instructions

With the class divided into groups, answer the following questions as if you were the chief financial officer for Harris Corporation.

- (a) "What does the cumulative provision related to the preferred stock mean?"
- (b) "I thought the common stock was presently selling at \$29.75, but the company has the stock stated at \$1 per share. How can that be?"
- (c) "Why is the company buying back its common stock? Furthermore, the treasury stock has a debit balance because it is subtracted from stockholders' equity. Why is treasury stock not reported as an asset if it has a debit balance?"
- (d) "Why is it necessary to show additional paid-in capital? Why not just show common stock at the total amount paid in?"