I. STOCKHOLDERS' EQUITY
   A. Owners' equity includes five major components: 1) capital stock; 2) additional paid-in capital; 3) retained earnings or deficit; 4) accumulated other comprehensive income; and 5) treasury stock. When an entity presents consolidated financial statements, any noncontrolling interest must be shown in equity.
   B. Capital stock includes these terms: authorized, issued, and outstanding. Treasury stock is issued but not outstanding.
   C. Common shareholders’ equity equals total stockholders’ equity reduced for the claims of preferred shareholders.
   D. Book value per share is the common shareholders’ equity divided by the number of common shares outstanding at year-end.
   E. Preferred shares are “first in line” before common shareholders for dividends and payment in liquidation. P/S may also be cumulative, participating, or convertible. Mandatorily redeemable preferred stock is reported as a liability because it has a maturity date, like other debt instruments.
   F. Additional paid-in capital can come from several sources in addition to any amount received above the par value of shares issued.
   G. Retained earnings can be increased or decreased by many events, including: income, losses, cash dividends, property dividends, stock dividends, prior period adjustments, cumulative effects of changes in accounting principles, and quasi-reorganizations.
   H. Quasi-reorganizations eliminate deficit balances in retained earnings by reducing the amount in C/S or APIC.
   I. Accumulated other comprehensive income is an equity account into which the components of other comprehensive income flow.
   J. Treasury stock may be accounted for by the cost method or the legal (par value) method.
   K. Donated shares result in a credit to contributed capital.
   L. Stock subscriptions are contracts to buy stock at a future date.
   M. Stock rights provide existing shareholders with the opportunity to buy additional shares and do not affect equity until exercised.
   N. Dividends declared reduce R/E on the declaration date.
   O. Liquidating dividends are dividends in excess of R/E.
   P. Property dividends are recorded at their fair value at the declaration date. Gain or loss is recognized on that date.
   Q. Stock dividends occur in two sizes: small and large. The “break point” is 20 to 25 percent of outstanding C/S. Small stock dividends tend to be on the exam more often. Small stock dividends are recorded at fair value on the declaration date. Large stock dividends are recorded at par value.
R. Stock splits do not require a journal entry and total book value of C/S is unchanged.
S. Compensatory stock option plans are accounted via the fair value method.

II. EARNINGS PER SHARE
A. Basic earnings per share assumes no potentially dilutive securities. Basic EPS divides income available for common shareholders by the weighted average number of common shares outstanding.
B. Diluted EPS employs the "if converted" and/or "treasury stock" methods to re-compute EPS as it would be if any dilutive securities such as convertible bonds or preferred stock, rights, warrants, and options were exercised. Antidilutive securities are not considered.
C. Preferred stock, especially cumulative issues, cause calculation difficulties, as preferred claims are not available for common shareholders and preferred dividends do not reduce net income.
D. Contingent shares, if dilutive, are part of the Basic EPS calculation if all conditions for issuance are met.
E. Basic and diluted EPS are disclosed by income statement component for a proper presentation.

III. STATEMENT OF CASH FLOWS
A. This statement is composed of three sections:
   1. Cash Flows From Operating Activities (CFO)—Cash receipts and disbursements from transactions reported on the income statement and current assets and liabilities.
   Cash flows related to current notes payable and the current portion of long-term debt are reported as financing cash flows.
   2. Cash Flows From Investing Activities (CFI)—Cash receipts and disbursements from non-current assets.
   3. Cash Flows From Financing Activities (CFF)—Cash receipts and disbursements from debt (including non-current liabilities) and equity.
B. Cash equivalents (treated as cash) are debt securities with an original maturity date of three months or less.
C. Under the indirect method, the operating activities section adjusts net income to cash provided, or used, by operating activities. The mnemonic CLAD is useful to remember the various adjustments.
D. When the indirect method is used, a supplemental disclosure of cash paid for interest and income taxes is required.
E. Under the direct method, the operating activities section shows the major classes of cash receipts and disbursements in their gross amounts to arrive at net cash provided by (used in) operating activities.
F. When the direct method is used, a supplemental disclosure entitled the reconciliation of net income to cash provided by operating activities is required under U.S. GAAP, but is not required under IFRS.

G. Under both the direct and indirect methods, a disclosure of noncash investing and financing activities is required.

H. Under U.S. GAAP, interest received and dividends received are classified as CFO. Under IFRS, interest received and dividends received may be classified as CFO or CFI.

I. Under IFRS, interest paid and dividends paid may be classified as CFO or CFF. Under U.S. GAAP, interest paid is classified as CFO and dividends paid are classified as CFF.

IV. RATIO ANALYSIS

It is important to memorize and understand the key financial ratios presented in the textbook.