

# Income Statement

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## WHAT'S COVERED

This tutorial will cover the income statement.

Our discussion breaks down as follows:

1. [Income Statement](#)
2. [Income Statement vs. Balance Sheet](#)
3. [Types of Income Statements](#)
4. [Single Step Income Statement: Examples](#)

## 1. Income Statement

Before we begin our discussion of the income statement, it is important to take a step back and define **financial statements**, which are reports providing financial information about a business at a given time.

An **income statement**, then, is a financial statement that provides information about the revenue, expenses, and net profit or loss of a business for a given time period. A key phrase in that definition is "a given time period."

Let's break down the net profit or loss idea. The income statement helps to identify the business's profitability, which is a key component of the purpose of the income statement:

- The income statement reports on one year or less of a time period.
- The income statement helps to assess the health or strength of a business, which is important information for shareholders and potential investors, as well as banks.

Now, the income statement formula is revenues minus expenses equals net income, revenues being the inflows from the business operations and expenses being the outflows or the use of assets from the business operations.



### FORMULA TO KNOW

## Income Statement Formula

*Revenues – Expenses = Net Income*



### TERMS TO KNOW

#### Financial Statements

Reports providing financial information about a business at a given time.

#### Income Statement

A financial statement that provides information about the revenue, expenses, and net profit or loss of a business for a given time period.

## 2. Income Statement vs. Balance Sheet

Now let's compare the income statement to the balance sheet. Keep in mind that the balance sheet reports balances and the income statement reports activity.

	Income Statement	Balance Sheet
Reporting	Reports for a period of time; activity based.	Reports at a point in time.
Accounts Included	Temporary accounts; revenues and expenses.	Permanent accounts; assets, liabilities, and equity.
Decision Tool	Assess past performance and predict future performance.	Primarily forward-looking; identify the business's position, as of a certain date, and the implications going forward.

## 3. Types of Income Statements

There are two types of income statement formats: single step and multi-step.

The single step income statement is called such because there is only one step. Remember the income statement formula? Revenues minus expenses equals net income. This is what the single step income statement looks like, below. You take your revenues, subtract out your expenses, and arrive at your net income.



The multi-step income statement, on the other hand, has multiple steps.

- First, you start with your sales and subtract the cost of goods sold to get your gross profit.
- Second, you take that gross profit and subtract all of your operating expenses from the business operations to get to income from operations.
- Third, once you have income from operations, you subtract the other revenues and expenses to ultimately arrive at your net income.

Multi-step	
Sales	
- Cost of Goods Sold	1
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Gross Profit	
- Operating Expenses	2
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Income from Operations	
- Other Revenues (Expenses)	3
<hr/>	
Net Income	

At the end of the day, the single step and multi-step income statements arrive at the same place, but the multi-step statement has several individual steps that involve calculating gross profit and separating out income from operations, as well as other revenues and expenses.

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## 4. Single Step Income Statement: Examples

Let's look at our first example of a single step income statement and break down its component parts:

<b>Single Step</b>	
<b>Header</b> →	<b>Acme Inc.</b> <b>Income Statement</b> For the period ending December 31, 2012
<b>Revenues</b> →	<b>Revenues:</b> Sales \$ 300,000 Interest revenue 10,000 <b>Total revenue 310,000</b>
<b>Expenses</b> →	<b>Expenses:</b> Selling expense 150,000 Rent expense 10,000 Marketing expense 5,000 Interest expense 10,000 <b>Total expenses 175,000</b>
<b>Net income</b> →	<b>Net income \$ 135,000</b>
<b>Earnings per Share</b> →	<b>Earnings per Share \$ 1.35</b>

- *Header.* The header is going to have the name of the company. It will say "Income Statement," and will also say "For the period ending...", in this case, December 31, 2012.

#### HINT

It is important that the header includes the words, "For period ending...", because this indicates that the income statement is reporting on activity for a given period.

- *Revenues.* This section includes sales and any other revenue--in this case, interest revenue. It reflects the total revenue from the single step income statement formula.
- *Expenses.* Next is a detail of all expenses. In this case, there are some selling expense, rent expense, marketing expense, and interest expense, summed to equal the total expenses.
- *Net Income.* The total revenue of \$310,000 minus total expenses of \$175,000 equals a net income of \$135,000.
- *Earnings per Share.* This is the other piece of information contained on this single step income statement, calculated by taking the net income and dividing it by the number of shares that are owned and issued by the company. If this was a publicly traded company and they had shares on an exchange, you would list the earnings per share. In this case, we assumed there were 100,000 shares, so the earnings per share are \$1.35 per share.

Let's look at a second example of the single step income statement. It's quite similar to the first example.

## Single Step

Header →

Revenues →

Expenses →

Net income →

Earnings per Share →

### Accountants Inc. Income Statement For the period ending December 31, 2012

Revenues:	
Service revenue	\$ 500,000
Interest revenue	20,000
Total revenue	<u>520,000</u>
Expenses:	
Salaries expense	250,000
Rent expense	30,000
Software expense	25,000
Income tax expense	<u>5,000</u>
Total expenses	<u>310,000</u>
Net income	<u><u>\$ 210,000</u></u>

Earnings per Share \$ 1.05

- *Header.* Again, you can see the company name, "Income Statement," and "For the period ending December 31, 2012."
- *Revenues.* Revenues are detailed; in this case, service revenue and interest revenue.
- *Expenses.* Expenses are also detailed, slightly different from our first example. In this case, the expenses include salaries, rent, software and income tax, summed to provide the total expenses.
- *Net Income.* Net income is calculated by taking total revenue and subtracting total expenses.
- *Earnings per Share.* At the bottom of the statement is included the earnings per share figure. Assuming we had 200,000 shares outstanding, earnings per share are \$1.05 per share.



#### SUMMARY

Today we learned all about the **income statement**, which is a financial statement that provides information about the revenue, expenses, and net profit or loss of a business for a given time period. Remember, those words at the end--"for a given period of time"--are very important because the income statement is activity-based. We compared the **income statement vs. balance sheet**, and learned about the two **types of income statements**: the single step and the multi-step. Lastly, we examined two

**examples of the single step income statement**, utilizing the single step of the income statement formula: total revenues minus total expenses equals net income.

Source: Adapted from Sophia instructor Evan McLaughlin.



## TERMS TO KNOW

### **Financial Statements**

Reports providing financial information about a business at a given time.

### **Income statement**

A financial statement that provides information about the revenue, expenses, and net profit or loss of a business for a given time period.