

# Preparing Statements of Changes in Owner's Equity

by Sophia



## WHAT'S COVERED

This tutorial will cover how to prepare the statement of changes in owner's equity.

Our discussion breaks down as follows:

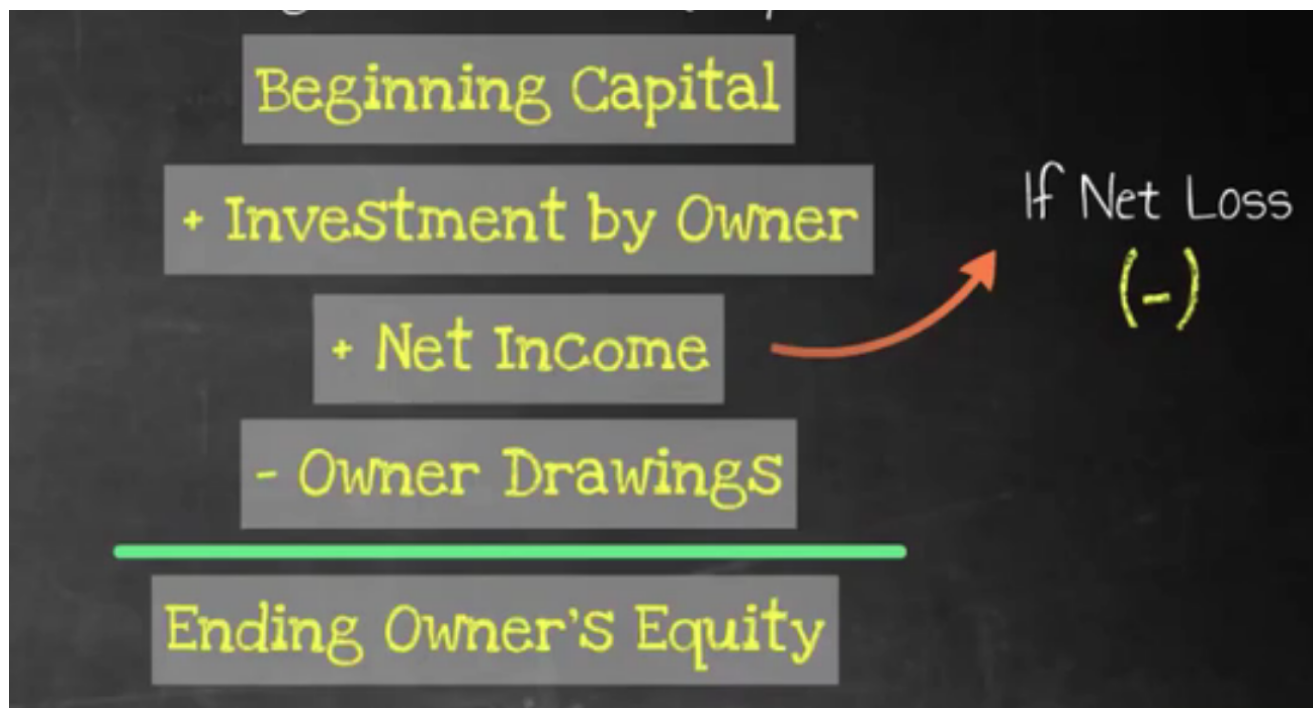
- [1. Statement of Changes in Owner's Equity: A Review](#)
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## 1. Statement of Changes in Owner's Equity: A Review

To review, the statement of changes in owner's equity is a financial statement that provides information about changes to the equity of a business, for a given time period. Note that it is period- or activity-based. It can also be referred to as the statement of retained earnings.

Owner's equity refers to owner activity--activity such as income, draws, or loss. Typically, the statement of changes in owner's equity involves one year or less of an activity period, detailing the changes in owner's equity for that time period, similar to the income statement.

The formula for the statement of changes in owner's equity starts with the beginning capital, or the beginning balance in owner's equity at the beginning of the year. Then, we input any capital added or investments by the owner, plus any net income that the business might have earned, and then subtract owner drawings, meaning any money that the owner or owners pulled out of the business. This results in the ending owner's equity, or the ending balance in the owner's equity account.



Now, if we have a net loss instead of having net income, we would have to subtract the net loss in this formula instead of adding that income.



#### FORMULA TO KNOW

##### Statement of Changes in Owner's Equity

$$\text{Ending Owner's Equity} = \text{Beginning Capital} + \text{Investment by Owner} + \text{Net Income} - \text{Owner Drawings}$$

## 2. Statement of Changes in Owner's Equity: Example

Let's look at a detailed example of preparing a statement of changes in owner's equity.

The first order of business is to look at the adjusted trial balance, which we can get from our trial balance worksheet. You may recall that it is necessary to go through the adjusting process to prepare the adjusted trial balance, prior to preparing the financial statements.

Accounts	Adjusted Trial Balance			
	Dr.	Cr.		
Cash	120,000			
Accounts Receivable	10,000			
Supplies	500			
Prepaid Insurance	4,000			
Buildings	50,000			
Accumulated Depreciation - Buildings		11,000		
Accounts Payable		5,000		
Notes Payable		25,000		
Common Stock		100,000		
Retained earnings, 1/1/12		12,000		
Owner's Drawing	2,000			
Sales		300,000		
Interest Revenue		20,000		
Cost of Goods Sold	150,000			
Salaries Expense	121,500			
Advertising Expense	10,000			
Interest Expense	2,500			
Depreciation Expense - Buildings	1,000			
Insurance Expense	1,000			
Supplies Expense	500			
Totals	473,000	473,000		

Now, the adjusted trial balance will help to identify the balances and accounts that we need to use to prepare the statement of changes in owner's equity.

The other financial statement needed in order to prepare the statement of changes in owner's equity is the income statement, because we need to know if there is net income or loss for the period.

Accounts	Adjusted Trial Balance		Income Statement	
	Dr.	Cr.	Dr.	Cr.
Cash	120,000			
Accounts Receivable	10,000			
Supplies	500			
Prepaid Insurance	4,000			
Buildings	50,000			
Accumulated Depreciation - Buildings		11,000		
Accounts Payable		5,000		
Notes Payable		25,000		
Common Stock		100,000		
Retained earnings, 1/1/12		12,000		
Owner's Drawing	2,000			
Sales		300,000		300,000
Interest Revenue		20,000		20,000
Cost of Goods Sold	150,000		150,000	
Salaries Expense	121,500		121,500	
Advertising Expense	10,000		10,000	
Interest Expense	2,500		2,500	
Depreciation Expense - Buildings	1,000		1,000	
Insurance Expense	1,000		1,000	
Supplies Expense	500		500	
Totals	473,000	473,000	286,500	320,000
Net Income			33,500	
Totals			320,000	320,000

The income statement, from the trial balance worksheet, is used to identify the accounts that we need to put into our statement of changes in owner's equity:

- Owner drawings
- Retained earnings (beginning balance)
- Net income

Now that we have used our trial balance worksheet to identify the accounts needed, we are ready to prepare a detailed statement of changes in owner's equity, using the information from the trial balance worksheet.

Remember, we have captured the adjusted trial balance and income statement information.

The first line is the header. It includes the:

- Business name
- Name of the statement (In this case, "Statement of Changes in Owner's Equity")
- Since it is a period- or activity-based statement, we include the statement "For the period ending December 31, 2012."

Accounts	Adjusted Trial Balance		Income Statement	
	Dr.	Cr.	Dr.	Cr.
Cash	120,000			
Accounts Receivable	10,000			
Supplies	500			
Prepaid Insurance	4,000			
Buildings	50,000			
Accumulated Depreciation - Buildings		11,000		
Accounts Payable		5,000		
Notes Payable		25,000		
Common Stock		100,000		
Retained earnings, 1/1/12		12,000		
Owner's Drawing	2,000			
Sales		300,000		300,000
Interest Revenue		20,000		20,000
Cost of Goods Sold	150,000		150,000	
Salaries Expense	121,500		121,500	
Advertising Expense	10,000		10,000	
Interest Expense	2,500		2,500	
Depreciation Expense - Buildings	1,000		1,000	
Insurance Expense	1,000		1,000	
Supplies Expense	500		500	
Totals	473,000	473,000	286,500	320,000
Net Income			33,500	
Totals			320,000	320,000

<b>Acme Inc.</b>	
Statement of Changes in Owner's Equity	
For the period ending December 31, 2012	

The first thing we do is to input the beginning balance of retained earnings as of January 1, 2012. Now, where do we get this information? We get it from the adjusted trial balance, shown below. Therefore, our retained earnings as of the beginning of the year is \$12,000.

Accounts	Adjusted Trial Balance		Income Statement	
	Dr.	Cr.	Dr.	Cr.
Cash	120,000			
Accounts Receivable	10,000			
Supplies	500			
Prepaid Insurance	4,000			
Buildings	50,000			
Accumulated Depreciation - Buildings		11,000		
Accounts Payable		5,000		
Notes Payable		25,000		
Common Stock		100,000		
Retained earnings, 1/1/12		12,000		
Owner's Drawing	2,000			
Sales		300,000		300,000
Interest Revenue		20,000		20,000
Cost of Goods Sold	150,000		150,000	
Salaries Expense	121,500		121,500	
Advertising Expense	10,000		10,000	
Interest Expense	2,500		2,500	
Depreciation Expense - Buildings	1,000		1,000	
Insurance Expense	1,000		1,000	
Supplies Expense	500		500	
Totals	473,000	473,000	286,500	320,000
Net Income			33,500	
Totals			320,000	320,000

<b>Acme Inc.</b>	
Statement of Changes in Owner's Equity	
For the period ending December 31, 2012	
Beginning balance, January 1	\$ 12,000

The next step is to add any net income. We pull the net income from our income statement, shown below. In this case, our net income is \$33,500. We add the net income to retained earnings for a subtotal of \$45,500.

Accounts	Adjusted Trial Balance		Income Statement	
	Dr.	Cr.	Dr.	Cr.
Cash	120,000			
Accounts Receivable	10,000			
Supplies	500			
Prepaid Insurance	4,000			
Buildings	50,000			
Accumulated Depreciation - Buildings		11,000		
Accounts Payable		5,000		
Notes Payable		25,000		
Common Stock		100,000		
Retained earnings, 1/1/12		12,000		
Owner's Drawing	2,000			
Sales		300,000		300,000
Interest Revenue		20,000		20,000
Cost of Goods Sold	150,000		150,000	
Salaries Expense	121,500		121,500	
Advertising Expense	10,000		10,000	
Interest Expense	2,500		2,500	
Depreciation Expense - Buildings	1,000		1,000	
Insurance Expense	1,000		1,000	
Supplies Expense	500		500	
Totals	473,000	473,000	286,500	320,000
Net Income			33,500	
Totals			320,000	320,000

<b>Acme Inc.</b>	
Statement of Changes in Owner's Equity	
For the period ending December 31, 2012	
Beginning balance, January 1	\$ 12,000
Add: Net income	33,500
	<u>45,500</u>

Next we have our subtractions. In this case, we have owner drawings, as shown on the adjusted trial balance. This means that the owner has pulled money out of the business, in the amount of \$2,000.

Accounts	Adjusted Trial Balance		Income Statement	
	Dr.	Cr.	Dr.	Cr.
Cash	120,000			
Accounts Receivable	10,000			
Supplies	500			
Prepaid Insurance	4,000			
Buildings	50,000			
Accumulated Depreciation - Buildings		11,000		
Accounts Payable		5,000		
Notes Payable		25,000		
Common Stock		100,000		
Retained earnings, 1/1/12		12,000		
Owner's Drawing	2,000			
Sales		300,000		300,000
Interest Revenue		20,000		20,000
Cost of Goods Sold	150,000		150,000	
Salaries Expense	121,500		121,500	
Advertising Expense	10,000		10,000	
Interest Expense	2,500		2,500	
Depreciation Expense - Buildings	1,000		1,000	
Insurance Expense	1,000		1,000	
Supplies Expense	500		500	
Totals	473,000	473,000	286,500	320,000
Net Income			33,500	
Totals			320,000	320,000

ACme Inc.	
Statement of Changes in Owner's Equity	
For the period ending December 31, 2012	
Beginning balance, January 1	\$ 12,000
Add: Net income	33,500
	<u>45,500</u>
Less: Drawings	2,000
	<u>2,000</u>

Now, we don't have to include a net loss as a subtraction, because, in this case, we had net income. Therefore, we subtract the owner draws from the subtotaled retained earnings and net income to arrive at our ending balance, as of December 31, of \$43,500.

ACme Inc.	
Statement of Changes in Owner's Equity	
For the period ending December 31, 2012	
Beginning balance, January 1	\$ 12,000
Add: Net income	33,500
	<u>45,500</u>
Less: Drawings	2,000
	<u>2,000</u>
Ending balance, December 31	\$ <u>43,500</u>



## SUMMARY

Today we covered a **review of the statement of changes in owner's equity**, which is a financial statement that provides information about changes to the equity of a business, for a given time period. Remember, it is an activity-based report about the equity of a business. We also walked through a

comprehensive **example of preparing a statement of changes in owner's equity**, which involves looking at the adjusted trial balance to pull all of the equity balances, as well as consulting the income statement to pull the net income.

Source: Adapted from Sophia instructor Evan McLaughlin.