



WICHITA STATE  
UNIVERSITY

# Fundamentals of Accounting

## Module 5

### *Balance Sheet – Liabilities & Stockholders' Equity*

# Prior Module's Focus

## Assets

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## Liabilities + Stockholders Equity

### Assets:

- Current Assets
  - Cash
  - Receivables
  - Inventory
- Long-term Assets
  - Property, Plant & Equipment
  - Goodwill

Long-term Receivables

### Liabilities:

- Current Liabilities
  - Accounts Payable
  - Other Accrued Liabilities
  - Short-term Debt (payable within the upcoming 12 months)
- Long-term Liabilities
  - Long-term Debt

### Stockholders Equity:

- Paid-in Capital
- Retained Earnings (The net income a firm generates less any dividends paid out)

# Typical Balance Sheet

## Assets

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## Liabilities + Stockholders Equity

### Assets:

- Current Assets
  - Cash
  - Receivables
  - Inventory
- Long-term Assets
  - Property, Plant & Equipment
  - Goodwill
  - Long-term Receivables

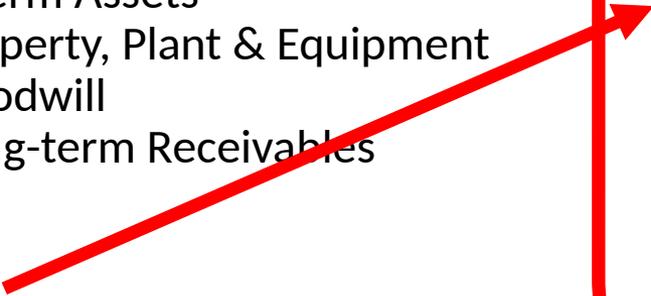
### Liabilities:

- Current Liabilities
  - Accounts Payable
  - Other Accrued Liabilities
  - Short-term Debt (payable within the upcoming 12 months)
- Long-term Liabilities
  - Long-term Debt

### Stockholders Equity:

- Paid-in Capital
- Retained Earnings (The net income a firm generates less any dividends paid out)

**THIS MODULE'S FOCUS**



# What Does The Term “Liabilities”

## Represent?

- Liabilities are obligations that represent “probable future sacrifice of economic benefits”
- The term accrued expenses is often used on the balance sheet to describe liabilities
- Current liabilities are those liabilities that will be paid within one year of the current balance sheet date
  - Accounts payable
  - Short-term debt (Notes payable)
  - Current maturities of long-term debt (i.e. due within the next 12 months)
  - Unearned revenue or deferred credits
  - Other accrued liabilities
- Long-term liabilities represent those liabilities that will be paid at a time > 1 year from the current balance sheet date
  - Long-term debt (Bonds payable due in periods beyond 12 months from the financial statement date)
  - Deferred tax liabilities
- The recognition of a liability usually means that an expense has been recorded.
  - Expenses always reduce income.

# Walmart Annual Report - Balance Sheet Liabilities

## Consolidated Balance Sheets

(Amounts in millions)

	As of January 31,	
	2014	2013
<b>LIABILITIES, REDEEMABLE NONCONTROLLING INTEREST AND EQUITY</b>		
<i>Current liabilities:</i>		
Short-term borrowings	\$ 7,670	\$ 6,805
Accounts payable	37,415	38,080
Accrued liabilities	18,793	18,808
Accrued income taxes	966	2,211
Long-term debt due within one year	4,103	5,587
Obligations under capital leases due within one year	309	327
Current liabilities of discontinued operations	89	—
<b>Total current liabilities</b>	<b>69,345</b>	<b>71,818</b>
Long-term debt	71	38,394
Long-term debt due after one year	38	3,023
Deferred income taxes	17	7,613
Redeemable noncontrolling interest	11	519

**5 Accrued Liabilities**

The Company's accrued liabilities consist of the following:

	As of January 31,	
(Amounts in millions)	2014	2013
Accrued wages and benefits <sup>(1)</sup>	\$ 4,652	\$ 5,059
Self-insurance <sup>(2)</sup>	3,477	3,373
Accrued taxes <sup>(3)</sup>	2,554	2,851
Other <sup>(4)</sup>	8,110	7,525
<b>Total accrued liabilities</b>	<b>\$18,793</b>	<b>\$18,808</b>

(1) Accrued wages and benefits include accrued wages, salaries, vacation, bonuses and other incentive plans.

(2) Self-insurance consists of all insurance-related liabilities, such as workers' compensation, general liability, vehicle liability, property liability and employee-related health care benefits.

(3) Accrued taxes include accrued payroll, value added, sales and miscellaneous other taxes.

(4) Other accrued liabilities consist of various items such as maintenance, utilities, advertising and interest.

# Accounts Payable - Key Considerations

- Represents amounts due for items/services received
- May be vouchered or unvouchered
- Payment terms are important
  - Prompt pay discount opportunities?

# Payment Terms Example

- Company “X” has received an invoice from one of its suppliers
  - Invoice Amount: \$500,000
  - Product received on: January 15, 2015
  - Invoice date: January 15, 2015
  - Payment Terms: 2/10, n/30 from the invoice date
- Payment alternatives for Company “X”
  - Alternative 1:
    - Take advantage of the prompt pay discount
      - Payment date: January 25, 2015
      - Payment amount = \$490,000
  - Alternative 2:
    - Pay under normal terms
      - Payment date: February 14, 2015
      - Payment amount = \$500,000
- Which alternative would you choose?
- What considerations might lead you to choose the other alternative?

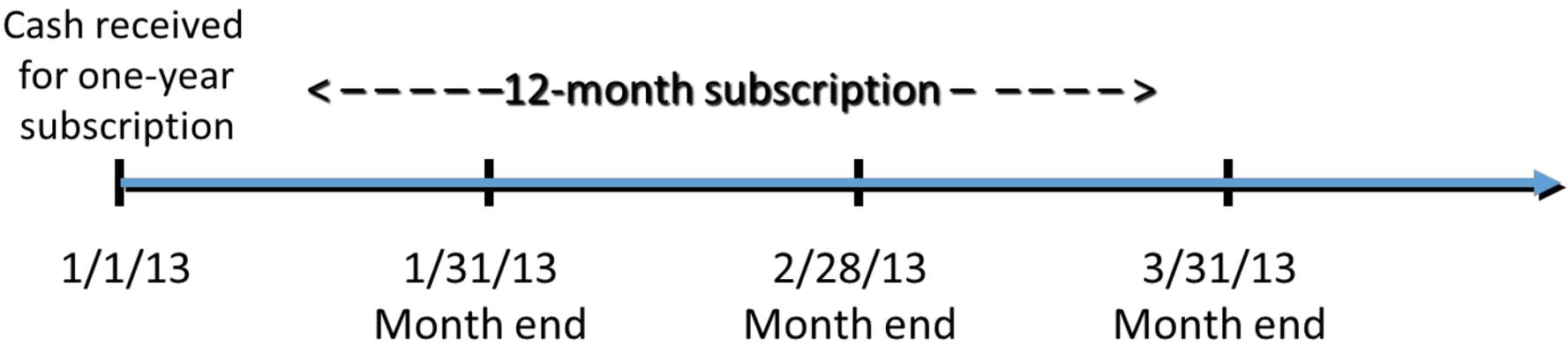
# Other Accrued Liabilities - Key Considerations

- Unearned Revenue or Deferred Credits
- Payroll
- Payroll taxes
  - Includes items such as FICA & Medicare taxes, Federal and State and Local income taxes, and other related payroll deductions
- Warranty
  - It is appropriate to recognize the estimated warranty expense in the same period as the sale is recorded
- Accrued interest on debt

# Unearned Revenue or Deferred Credits

- Unearned revenue is created when customers pay for services or products before delivery.

**On January 1, 2013, Matrix, Inc. receives \$2,400 cash as an advance payment for a one-year subscription to its monthly investment newsletter.**



**Our goal is to recognize revenue as the subscription is fulfilled each month.**

# Accrued Taxes - Key Considerations

- The difference between tax expense and taxes payable is referred to as deferred taxes.
- Tax expense is calculated on the income statement following the Generally Accepted Accounting Principles (GAAP) rules for preparing financial statements.
- Income taxes payable are calculated following the Internal Revenue Service (IRS) rules.
- Income tax expense usually does not equal income taxes payable within the same period.
- Long-term portion is referred to as “Deferred Tax Liability”

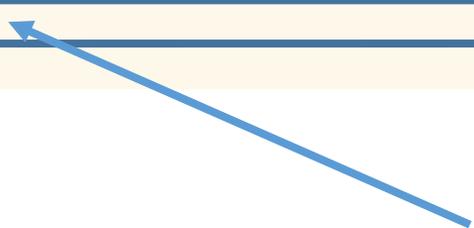
# Walmart Annual Report - Balance Sheet Liabilities

## Consolidated Balance Sheets

(Amounts in millions)

	As of January 31,	
	2014	2013
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Long-term debt due within one year	4,103	5,587
Obligations under capital leases due within one year	309	327
Current liabilities of discontinued operations	89	—
<b>Total current liabilities</b>	<b>69,345</b>	<b>71,818</b>
Long-term debt	41,771	38,394
Long-term obligations under capital leases	2,788	3,023
Deferred income taxes and other	8,017	7,613
Redeemable noncontrolling interest	1,491	519

Deferred Tax Liability



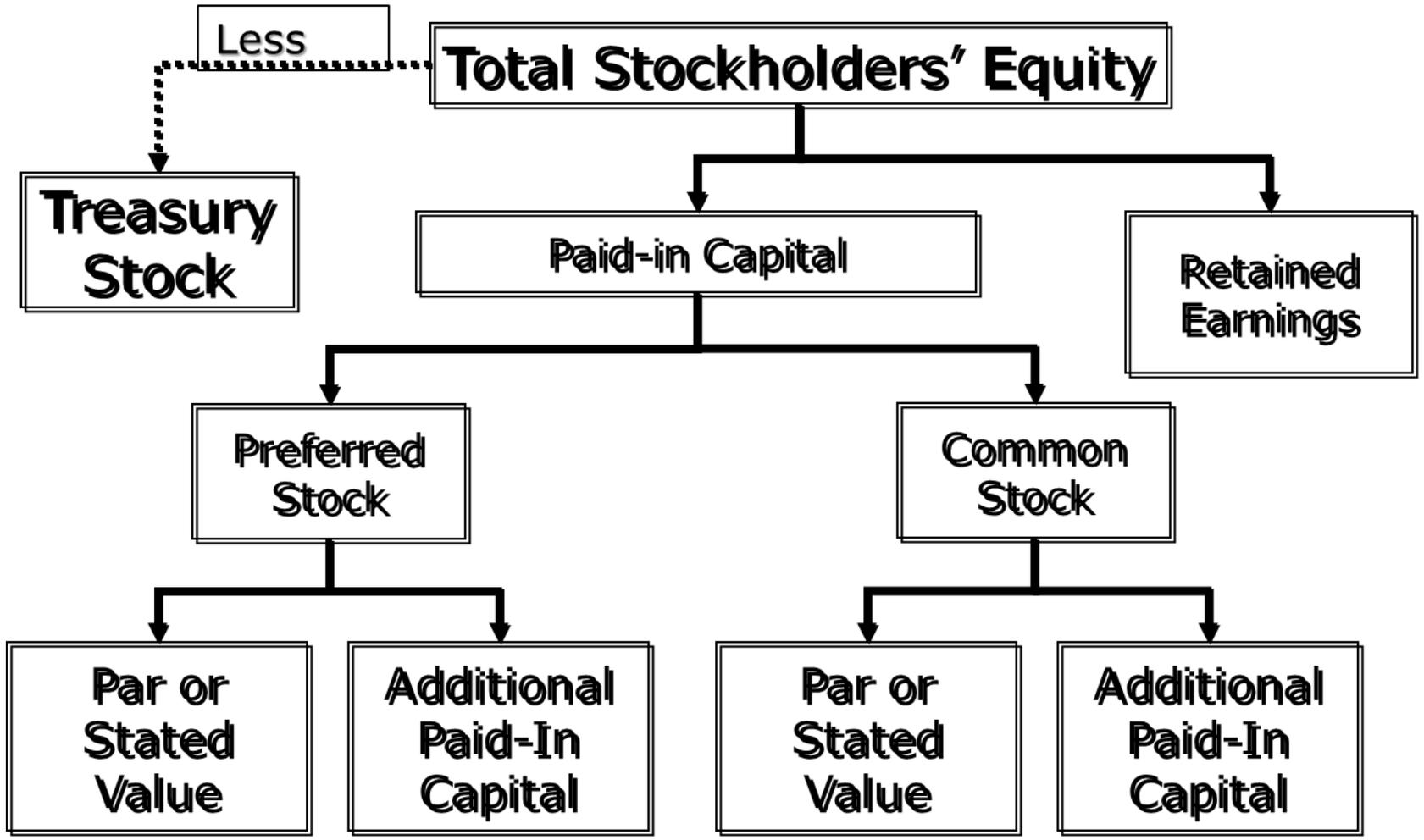
# Debt - Key Considerations

- Distinction between current vs. long-term debt
  - Any portion of long-term debt that is to be repaid within a year of the balance sheet date is reclassified from the noncurrent liability section to the current liability section under the title, current maturities of long-term debt
- Interest on debt is tax deductible but dividends on stock are not.
  - The after-tax cost of debt can be less than the cost of equities
- Long-term debt can provide positive financial leverage.
  - Leverage is the difference between the ROI and the ROE

# Other Non-Current Liabilities

- Obligations relating to pension plans and other employee benefit plans, including deferred compensation and bonus plans.
  - Expenses relating to these plans are accrued and reflected in the income statement of the fiscal period in which the benefits are earned by the employees
- Contingent liabilities
  - Potential claims on the resources of a company arising from:
    - Pending litigation,
    - Environmental hazards,
    - Casualty losses to property,
    - Product warranties, or u
    - Unsettled disputes with the Internal Revenue Service
  - Recognized on the balance sheet if the loss is:
    1. Probable and
    2. The amount of the future loss is reasonably estimable

# Stockholders' Equity Components



# Stockholders' Equity

## Par Value from "Investopedia.com"

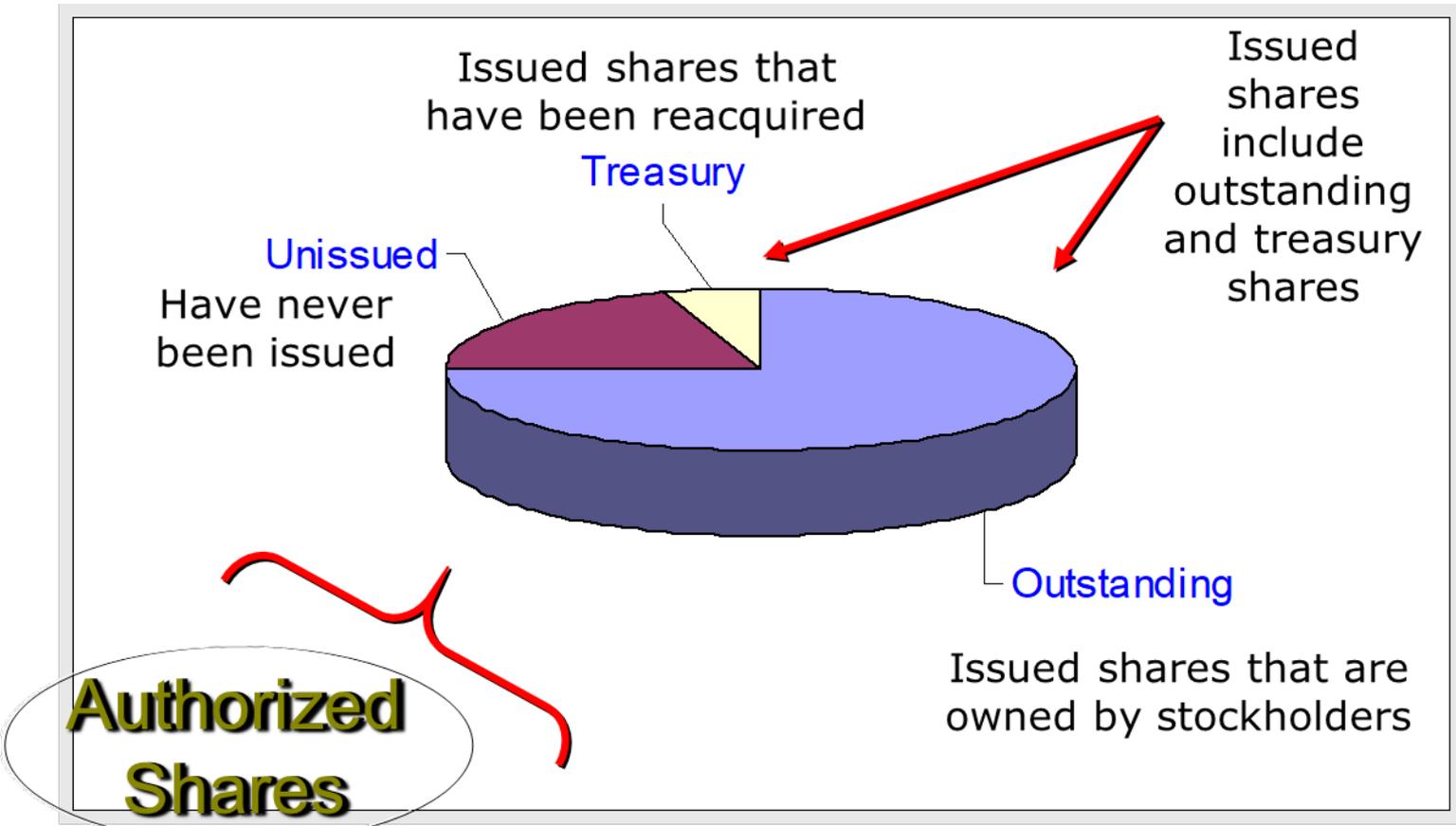
- Definition:
  - The face value of a bond
  - Par value for a share refers to the stock value stated in the corporate charter
- Par value is important for a bond or fixed-income instrument because it determines its maturity value as well as the dollar value of coupon payments.
  - Par value for a bond is typically \$1,000 or \$100
  - The market price of a bond may be above or below par, depending on factors such as the level of interest rates and the bond's credit status
- Shares usually have no par value or very low par value, such as 1 cent per share.
  - In the case of equity, par value has very little relation to the shares' market price

# Stockholders' Equity

## Additional Paid in Capital

- Represents the excess of the amount received from the sale of preferred or common stock over par (or stated) value

# Stockholders' Equity Common Stock



# Stockholders' Equity

## Preferred Stock

- Normally no voting rights, but dividend payment has preference over common stock
- Has a par or stated value with dividend expressed as a percent of par
- If callable, may be retired. If convertible, may be exchanged for common shares
- Normally, preferred stock is cumulative meaning that all dividends must be paid before any dividends can be paid to common shareholders
- Preferred may be noncumulative
  - If dividends are not paid, the company is not required to make-up the missed dividends
- Example: Matrix, Inc. has 50,000, \$100 par value, 6%, cumulative preferred stock outstanding
  - $50,000 \times \$100 = \$5,000,000$  total par  $\times 6\% =$  **\$300,000 dividend**

# Comparison of Preferred Stock & Debt/Bonds Payable

<b><i>Similarities</i></b>	
<b>Preferred Stock</b>	<b>Bonds Payable</b>
<b>Dividend is usually fixed claim to income</b>	<b>Interest is fixed claim to income</b>
<b>Redemption value is fixed claim to assets</b>	<b>Maturity value is a fixed claim to assets</b>
<b>Is usually callable and may be convertible</b>	<b>Is usually callable and may be convertible</b>
<b><i>Differences</i></b>	
<b>Dividend may be skipped, even if it must be caught up before payments to common</b>	<b>Interest must be paid or firm faces bankruptcy</b>
<b>No maturity date</b>	<b>Principal must be paid at maturity</b>
<b>Dividends are not an expense and are not tax deductible</b>	<b>Interest is a tax deductible expense</b>

# Stockholders' Equity

## Retained Earnings

- Represents the cumulative earnings of a corporation less the cumulative dividends paid since the business started operations
- Retained earnings is NOT cash

# Stockholders' Equity

## Dividends

- Dividends must be declared by the board of directors before they can be legally paid
- The company must have sufficient cash and retained earnings to pay the dividend
- The company is not legally required to pay dividends, but once declared a legal liability is created
- In lieu of paying a cash dividend, a company may elect to issue a stock dividend
  - Distribution of additional shares of stock to stockholders
  - No change in par value of stock or in total stockholders' equity
  - Stockholders retain percentage ownership in the company (preemptive right)
  - Reasons for stock dividends:
    - Preserve cash
    - Decrease market price of stock
    - Reduce retained earnings

# Stockholders' Equity

## Stock Split

- A company may elect to declare a stock split to lower the market price of its common stock
  - Increase the number of shares outstanding
  - Decrease the par value per share
  - No change to total stockholders' equity value
  - No journal entry required

# Stockholders' Equity Accumulated Other Comprehensive Income/(Loss)

- A new category in stockholders' equity called accumulated other comprehensive income (loss)
  - Includes certain specific unrealized changes that have not flowed through the income statement
- Includes the following unrealized changes to stockholders' equity:
  - Cumulative foreign currency translation adjustments
  - Unrealized gains or losses on available-for-sale investments
  - Changes during the period in certain pension or other postretirement benefit items
  - Gains or losses on certain derivative instruments

# Stockholders' Equity

## Non-controlling Interest

- Non-controlling interest represents the portion of equity ownership in a subsidiary that is:
  1. Not attributable to the parent company;
  2. Where the reporting company has a controlling interest (greater than 50% but less than 100%) in the subsidiary; and
  3. The company consolidates the subsidiary's financial results with its own
- Also known as minority interest.
- The balance sheet model can be expanded as follows:
  - $ASSETS = LIABILITIES + (STOCKHOLDERS' EQUITY + NON-STOCKHOLDERS' EQUITY)$

# Walmart Annual Report - Stockholders' Equity

<b>LIABILITIES, REDEEMABLE NONCONTROLLING INTEREST AND EQUITY</b>		
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Current liabilities of discontinued operations	89	—
<b>Total current liabilities</b>	<b>69,345</b>	<b>71,818</b>
Long-term debt	41,771	38,394
Long-term obligations under capital leases	2,788	3,023
Deferred income taxes and other	8,017	7,613
Redeemable noncontrolling interest	1,491	519
<i>Commitments and contingencies</i>		
<i>Equity:</i>		
Common stock	323	332
Capital in excess of par value	2,362	3,620
Retained earnings	76,566	72,978
Accumulated other comprehensive income (loss)	(2,996)	(587)
<b>Total Walmart shareholders' equity</b>	<b>76,255</b>	<b>76,343</b>
Nonredeemable noncontrolling interest	5,084	5,395
<b>Total equity</b>	<b>81,339</b>	<b>81,738</b>
<b>Total liabilities, redeemable noncontrolling interest and equity</b>	<b>\$204,751</b>	<b>\$203,105</b>

Continued on next page

# Walmart Annual Report - Statement of Changes in Stockholders' Equity

## Consolidated Statements of Shareholders' Equity

(Amounts in millions)	Common Stock		Capital in Excess of Par Value	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total Walmart Shareholders' Equity	Nonredeemable Noncontrolling Interest	Total Equity	Redeemable Noncontrolling Interest
	Shares	Amount							
<b>Balances as of February 1, 2011</b>	3,516	\$352	\$ 3,577	\$63,967	\$ 646	\$68,542	\$2,705	\$71,247	\$ 408
Consolidated net income	—	—	—	15,699	—	15,699	627	16,326	61
Other comprehensive loss, net of income taxes	—	—	—	—	(2,056)	(2,056)	(660)	(2,716)	(66)
Cash dividends declared (\$1.46 per share)	—	—	—	(5,048)	—	(5,048)	—	(5,048)	—
Purchase of Company stock	(113)	(11)	(229)	(5,930)	—	(6,170)	—	(6,170)	—
Nonredeemable noncontrolling interest of acquired entity	—	—	—	—	—	—	1,988	1,988	—
Other	15	1	344	3	—	348	(214)	134	1
<b>Balances as of January 31, 2012</b>	3,418	342	3,692	68,691	(1,410)	71,315	4,446	75,761	404
Consolidated net income	—	—	—	16,999	—	16,999	684	17,683	73
Other comprehensive income, net of income taxes	—	—	—	—	823	823	138	961	51
Cash dividends declared (\$1.59 per share)	—	—	—	(5,361)	—	(5,361)	—	(5,361)	—
Purchase of Company stock	(115)	(11)	(357)	(7,341)	—	(7,709)	—	(7,709)	—
Nonredeemable noncontrolling interest of acquired entity	—	—	—	—	—	—	469	469	—
Other	11	1	285	(10)	—	276	(342)	(66)	(9)
<b>Balances as of January 31, 2013</b>	3,314	332	3,620	72,978	(587)	76,343	5,395	81,738	519
Consolidated net income	—	—	—	16,022	—	16,022	595	16,617	78
Other comprehensive loss, net of income taxes	—	—	—	—	(2,409)	(2,409)	(311)	(2,720)	(66)
Cash dividends declared (\$1.88 per share)	—	—	—	(6,139)	—	(6,139)	—	(6,139)	—
Purchase of Company stock	(87)	(9)	(294)	(6,254)	—	(6,557)	—	(6,557)	—
Redemption value adjustment of redeemable noncontrolling interest	—	—	(1,019)	—	—	(1,019)	—	(1,019)	1,019
Other	6	—	55	(41)	—	14	(595)	(581)	(59)
<b>Balances as of January 31, 2014</b>	3,233	\$323	\$ 2,362	\$76,566	\$(2,996)	\$76,255	\$5,084	\$81,339	\$1,491

See accompanying notes.

# Other Comprehensive Income/(Loss) - Walmart

<i>Equity:</i>		
Common stock	323	332
Capital in excess of par value	2,362	3,620
Retained earnings	76,566	73,078
Accumulated other comprehensive income (loss)	(2,996)	(587)
Total Walmart shareholders equity	76,255	76,343
Nonredeemable noncontrolling interest	5,084	5,395
Total equity	81,339	81,738

## 4 Accumulated Other Comprehensive Income (Loss)

Effective fiscal 2014, the Company adopted accounting guidance that requires, on a prospective basis, separate disclosure of significant items reclassified out of accumulated other comprehensive income (loss) by component. The following table provides the fiscal 2014, 2013 and 2012 changes in the composition of total accumulated other comprehensive income (loss), including the amounts reclassified out of accumulated other comprehensive income (loss) by component for fiscal 2014:

<i>(Amounts in millions and net of income taxes)</i>	Currency Translation and Other	Derivative Instruments	Minimum Pension Liability	Total
<b>Balances as of January 31, 2011</b>	\$ 1,226	\$ 60	\$(640)	\$ 646
Other comprehensive income (loss)	(2,032)	(67)	43	(2,056)
<b>Balances as of January 31, 2012</b>	(806)	(7)	(597)	(1,410)
Other comprehensive income (loss)	853	136	(166)	823
<b>Balances as of January 31, 2013</b>	47	129	(763)	(587)
Other comprehensive income (loss) before reclassifications	(2,769)	194	149	(2,426)
Amounts reclassified from accumulated other comprehensive income (loss)	—	13	4	17
<b>Balances as of January 31, 2014</b>	\$(2,722)	\$336	\$(610)	\$(2,996)

Amounts reclassified from accumulated other comprehensive income (loss) for derivative instruments are generally included in interest, net, in the Company's Consolidated Statements of Income, and the amounts related to the minimum pension liability are included in operating, selling, general and administrative expenses in the Company's Consolidated Statements of Income.

The Company's unrealized net gains and losses on net investment hedges, included in the currency translation and other category of accumulated other comprehensive income (loss), were not significant as of January 31, 2014 or January 31, 2013.