

Invertible Ralph

Ralph is analyzing Equipment Leasing Corp., a startup firm that buys and leases equipment from vendors and in turn leases the equipment bundled with service warranties to customers. Financial statements for Equipment Leasing are attached. During period 2, Equipment Leasing engaged in the following transactions (the first 11 are cash transactions, the remainder are accrual transactions; some amounts may be zero).

1. Collected cash proceeds from bond issues.
2. Acquired equipment for cash.
3. Acquired available-for-sale securities for cash.
4. Acquired treasury stock for cash.
5. Collected cash proceeds from resale of treasury stock.
6. Paid cash for warranty claims.
7. Collected cash from lease payments.
8. Lease payments paid with cash.
9. Bond interest and/or principal paid with cash.
10. Collected cash dividends from available-for-sale securities.
11. Collected cash dividends from equity method securities.
12. Leased equipment from vendors.
13. Recognized revenue from sales-type leases.
14. Recognized cost of sales from sales-type leases.
15. Accrued warranty liability and warranty expense.
16. Accrued interest revenue on sales-type leases.
17. Accrued interest expense on leases.
18. Accrued interest expense on bonds.
19. Re-valued available-for-sale securities at market value.
20. Recognized income from investments in equity method securities.
21. Allocated proceeds from sale of treasury stock to additional paid-in capital.

Required: 1. Determine the transaction amounts for period 2.

(Hint: Use T accounts and/or the directed graph to organize your analysis.)

2. Utilize the directed graph/T accounts to analyze/explain the cash flow statement.

Equipment Leasing Corp. Balance Sheets		
	Time 1	Time 2
Cash	\$76.67	\$101.01
Equipment-net	-	-
Net investment in leases	125.71	125.71
Investment in available-for-sale securities	29.00	27.00
Investment in equity method securities	48.00	49.00
Total assets	\$279.38	\$302.72

Liability for warranties	11.00	10.00
Lease obligations-net	52.38	52.38
Bonds payable-net	100.00	100.00
Total liabilities	\$163.38	\$162.38
Preferred stock, 8%, \$1 par value, 200 shares authorized, none issued	-	-
Common stock, \$.10 par value, 400 shares authorized, 100 issued of which 10 are held as treasury stock	10.00	10.00
Additional paid-in capital - common	90.00	91.00
Retained earnings	27.00	54.34
Unrealized gains on available-for-sale securities	4.00	2.00
Less: treasury stock at cost	(15.00)	(17.00)
Total stockholders' equity	\$116.00	\$140.34
Total equities	\$279.38	\$302.72

Equipment Leasing Corp. Income statements		
Income statements	Period 1	Period 2
Sales revenue	\$240.00	\$240.00
Cost of sales	200.00	200.00
Gross margin	40.00	40.00
Lease financing revenue	24.00	36.58
Dividend income	2.00	2.00
Income from equity method investments	1.00	4.00
Gross margin and other income	\$67.00	\$82.58
Expenses:		
Warranty expense	\$20.00	\$20.00
Interest expense on leases	10.00	15.24
Interest expense on bonds	10.00	20.00
Total expenses	\$40.00	\$55.24
Net Income	\$27.00	\$27.34
Less: Preferred dividends	-	-
Income available for common	\$27.00	\$27.34
Earnings per share	\$0.28	\$0.29
Weighted average shares outstanding	95	95

Notes to the financial statements indicate Equipment Leasing elected the following accounting choices.

1. Leases and bonds are capitalized using effective-interest amortization.
2. Passive investments are classified as available-for-sale securities.
3. Active investments are accounted for using the equity method.
4. Estimated warranty costs are recognized when leases are signed.
5. Treasury stock is valued at cost.

Equipment Leasing Corp. Cash flow statements		
	Period 1	Period 2
Net income	\$27.00	\$27.34
Adjust: income from equity method investments	(1.00)	(4.00)
Increase (decrease) in liability for warranty	11.00	(1.00)
Cash flows from operations	\$37.00	\$22.34
Investing activities:		
Investment in leases	(240.00)	(240.00)
Principal payments collected on leases	114.29	240.00
Investments in available-for-sale securities	(25.00)	-
Investments in equity method securities	(50.00)	-
Dividends collected on equity method securities	3.00	3.00
Cash flows from investing activities	\$(197.71)	\$3.00
Financing activities:		
Bond issues	100.00	100.00
Principal repaid on bonds	-	(100.00)
Lease obligations incurred	100.00	100.00
Principal payments on leases	(47.62)	(100.00)
Common stock issues	100.00	-
Treasury stock acquired	(15.00)	(17.00)
Treasury stock resold	-	16.00
Cash flows from financing activities	\$237.38	\$(1.00)
Net cash flows	\$76.67	\$24.34
Beginning cash balance	-	76.67
Ending cash balance	\$76.67	\$101.01

