

Income Statement – Multiple-step

This video is the second part of the income statement video. Before viewing this video, please view the income statement – single step video. The first part of the income statement video discusses the purposes of the income statement and how to prepare a single step income statement. In this video we will discuss how to prepare a multiple step income statement.

The multiple-step income statement shows detailed computations of sales, costs, and expenses. It provides more detail than a single-step income statement would.

The multiple-step income statement consists of three parts: gross profit computation, income from operations, and nonoperating activities.

When preparing the multiple-step income statement follow these steps.

Step 1 – prepare the heading. Step 2 – prepare the gross profit calculation. Step 3 – prepare the income from operations section, Step 4 – prepare the nonoperating activities and Step 5 – calculate Net Income. Let's look at the steps in detail.

Step 1 – Record the statements heading. Notice that the heading includes the name of the company, the name of the statement – income statement, and the time period, for the year ending December 31, 2008. Remember that an income statement always represents a period of time which is why the income statement includes for the year or for the month.

In step 2, prepare the gross profit calculation. Gross profit is equal to net sales minus cost of goods sold. In order to complete step 2, you must know how to calculate net sales and cost of goods sold.

Let's look at how to calculate net sales. Net Sales is calculated as sales minus sales discounts and sales returns.

After you calculate net sales, you will need to calculate cost of goods sold. Cost of goods sold is calculated as beginning inventory + purchases – ending inventory.

Here's an example of the gross profit computation of the income statement. Notice the two sections: Net Sales and Cost of Goods Sold. Remember that gross profit is calculated by subtracting cost of goods sold from net sales.

Step 3 – Prepare the income from operations section. To calculate income from operations, first start with gross profit (from step 2). Then subtract the operating expenses.

Operating expenses are made up of two categories: selling expenses and general and administrative expenses. Selling expenses are the expense of promoting sales. Some examples of selling expenses are advertising expense, depreciation expense – store equipment, and rent expense – selling space. General and Administrative expenses are the expenses for supporting a companies' operations. Some examples of general and administrative expenses are insurance expense, depreciation expense – office equipment, and rent expense – office space.

Here's a condensed example of the income from operations section of the income statement. Notice that we started with gross profit and then subtracted operating expenses to determine income from operations. Do you see the two sections of the operating expenses – selling and general and administrative?

Step 4 – Prepare the nonoperating activities section. Nonoperating activities consist of other expenses, revenues, losses, and gains that are unrelated to a company's operations. Nonoperating activities consist of other revenue and gains such as: interest revenue and gains from disposal of assets. Nonoperating activities also include other expenses and losses such as: interest expense and losses from disposals of assets.

Here's an example of the nonoperating activities section of the income statement. Notice that this includes the other revenues and gains and other expenses and losses.

The final step to preparing the income statement is to calculate net income. Net income is calculated by taking income from operations (step 3) plus or minus nonoperating activities.

Using the information from step 3, income from operations, minus nonoperating activities, step 4, we can calculate net income!

Preparing a multiple-step income statement is difficult, but if you remember these five steps and with a little practice you can easily master this topic!