

University of Mississippi

eGrove

---

Guides, Handbooks and Manuals

American Institute of Certified Public  
Accountants (AICPA) Historical Collection

---

1986

## Other comprehensive bases of accounting; Technical information for practitioners series, 1

Lawrence Lindenberg

Margaret Monaghan

Susan Sgromo

Follow this and additional works at: [https://egrove.olemiss.edu/aicpa\\_guides](https://egrove.olemiss.edu/aicpa_guides)



Part of the [Accounting Commons](#), and the [Taxation Commons](#)

---

### Recommended Citation

Lindenberg, Lawrence; Monaghan, Margaret; and Sgromo, Susan, "Other comprehensive bases of accounting; Technical information for practitioners series, 1" (1986). *Guides, Handbooks and Manuals*. 722.

[https://egrove.olemiss.edu/aicpa\\_guides/722](https://egrove.olemiss.edu/aicpa_guides/722)

This Book is brought to you for free and open access by the American Institute of Certified Public Accountants (AICPA) Historical Collection at eGrove. It has been accepted for inclusion in Guides, Handbooks and Manuals by an authorized administrator of eGrove. For more information, please contact [egrove@olemiss.edu](mailto:egrove@olemiss.edu).

Technical  
Information for  
Practitioners  
Series

1

OTHER  
COMPREHENSIVE  
BASES OF  
ACCOUNTING

---

**AICPA**

American Institute of  
Certified Public Accountants

Technical  
Information for  
Practitioners  
Series

1

# OTHER COMPREHENSIVE BASES OF ACCOUNTING

---

Lawrence Lindenberg, CPA, *Technical Manager*  
Margaret Monaghan, *Senior Technical Advisor*  
Susan Sgromo, CPA, *Technical Manager*

AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS  
1211 AVENUE OF THE AMERICAS  
NEW YORK, N.Y. 10036-8775  
TEL: (212) 512-2000  
FAX: (212) 512-2001

Copyright © 1986 by the  
American Institute of Certified Public Accountants, Inc.  
1211 Avenue of the Americas, New York, N.Y. 10036-8775

1 2 3 4 5 6 7 8 9 0 T I 8 9 8 7 6

# PREFACE

---

## ***OTHER COMPREHENSIVE BASES OF ACCOUNTING***

This is the first in a new series entitled Technical Information for Practitioners (TIPS). Each book in the series is designed to give practical guidance to one aspect of an accounting or audit engagement.

This booklet includes illustrative accountants' reports, financial statement formats, and a limited number of illustrative notes for uncomplicated nonpublic entities that prepare their financial statements on a comprehensive basis of accounting other than generally accepted accounting principles (referred to as an "other comprehensive basis of accounting," or OCBOA).

This is a nonauthoritative kit of practice aids. Various formats of financial statement presentations are in use; nevertheless, inclusion of only certain formats in this booklet in no way means that they are preferable. In addition, these illustrative formats and notes may become of limited use if any complexity is encountered in a particular entity's transactions because the illustrations deal with relatively uncomplicated entities. Readers are urged to refer directly to authoritative pronouncements when appropriate.

Illustrative financial statement formats are often helpful in developing a consistent style within a firm. However, no set of illustrative financial statements can cover all the situations that are likely to be encountered in practice because the circumstances of engagements vary widely. The nature of an entity will affect the format and classifications of the financial statements. This booklet includes different formats and classifications to demonstrate some of the possible variations.

Readers should consider other sources of illustrative financial presentations, such as those in authoritative pronouncements, AICPA audit and accounting guides, and library collections of published financial reports.

The sole responsibility for this material rests with the staff of the Technical Information Division. This material has not been approved, disapproved, or otherwise acted upon by the senior technical committees of the American Institute

of Certified Public Accountants or the Financial Accounting Standards Board.  
Comments and suggestions should be addressed to the following:

Technical Information Division  
American Institute of Certified Public Accountants  
1211 Avenue of the Americas  
New York, N.Y. 10036-8775

John H. Graves, CPA  
*Director of Technical Information*

# TABLE OF CONTENTS

Section	Page
12,100 <b>General Comments on Illustrative Financial Statements— Other Comprehensive Bases of Accounting</b> .....	1
12,200 <b>Description and Explanation of Bases</b>	
<b>Illustrated</b> .....	5
Overview .....	5
Cash Basis .....	5
Tax Basis .....	6
12,300 <b>Recommended Measurement and Disclosure Guidelines—</b>	
<b>Cash Basis</b> .....	7
General Comments .....	7
Measurement Guidelines .....	7
Disclosure Guidelines .....	7
General .....	7
Significant Accounting Policies .....	7
Accounting Changes .....	8
Business Combinations .....	8
Related Party Transactions .....	8
Pension Plans and Commitments and Contingencies .....	8
Subsequent Events .....	8
Assets and Liabilities .....	8
Stockholders' Equity .....	9
Income and Expense .....	9
12,310 <b>Illustrative Financial Statements—Cash Basis</b> .....	11
General Comments .....	11
Cash Basis—Financial Statements (a Corporation) .....	12
Statements of Assets and Liabilities—Cash Basis .....	12
Statements of Revenues and Expenses, and Retained Earnings—Cash Basis .....	13
Notes to Financial Statements—Cash Basis .....	14
Cash Basis—Financial Statements (a Partnership) .....	16
Statements of Assets and Liabilities—Cash Basis .....	16
Statements of Revenues and Expenses—Cash Basis .....	17

	Statements of Changes in Partners' Capital—	
	Cash Basis .....	18
	Notes to Financial Statements—Cash Basis .....	19
	Cash Basis—Financial Statements (a Professional	
	Corporation) .....	21
	Statements of Assets and Liabilities—Cash Basis .....	21
	Statements of Revenues and Expenses, and	
	Retained Earnings—Cash Basis .....	22
	Notes to Financial Statements—Cash Basis .....	23
	Cash Basis—Financial Statements (an S Corporation) .....	26
	Statements of Assets and Liabilities—Cash Basis .....	26
	Statements of Revenues and Expenses, and	
	Retained Earnings—Cash Basis .....	27
	Notes to Financial Statements—Cash Basis .....	28
	Cash Basis—Financial Statement (Not-for-Profit).....	30
	Statement of Cash Receipts and Disbursements .....	30
	Notes to Statement of Cash Receipts and Disbursements ...	31
12,400	<b>Recommended Measurement and Disclosure Guidelines—</b>	
	<b>Income Tax Basis</b> .....	33
	General Comments.....	33
	Measurement Guidelines .....	33
	Nontaxable Revenues.....	33
	Nondeductible Expenses.....	33
	Additional Income Taxes for Prior Years.....	34
	Adjustments to Balance Sheet for IRS Changes .....	34
	Accounting Changes for Tax Purposes .....	34
	S Corporations .....	34
	Disclosure Guidelines .....	34
	General.....	34
	Significant Accounting Policies.....	35
	Accounting Changes.....	35
	Business Combinations .....	35
	Related Party Transactions .....	36
	Pension Plans and Commitments and Contingencies .....	36
	Subsequent Events.....	36
	Assets and Liabilities.....	36
	Stockholders' Equity .....	36
	Income and Expense .....	37
12,410	<b>Illustrative Financial Statements—Income Tax Basis</b> .....	39
	General Comments.....	39
	Statements of Assets and Liabilities—Income Tax Basis ...	40
	Statements of Revenues and Expenses—Income Tax Basis	41
	Statements of Retained Earnings—Income Tax Basis .....	41



	Notes to Financial Statements—Income Tax Basis . . . .	42
12,500	<b>Types of Accountants' Reports</b> . . . . .	47
	Overview . . . . .	47
	Audit Reports . . . . .	48
	Cash Basis Statements . . . . .	48
	Income Tax Basis Statements . . . . .	48
	Review Reports . . . . .	49
	Cash Basis Statements . . . . .	49
	Income Tax Basis Statements . . . . .	49
	Compilation Reports . . . . .	50
	Cash Basis Statements—Full Disclosure . . . . .	50
	Cash Basis Statements—Omission of Substantially All Disclosures . . . . .	50
	Income Tax Basis Statements—Full Disclosure . . . . .	51
	Income Tax Basis Statements—Omission of Substantially All Disclosures . . . . .	51
	Other Reports . . . . .	52
	Report for a Change From Generally Accepted Accounting Principles to an Other Comprehensive Basis of Accounting . . . . .	52
	Report on Statements of Cash Receipts and Disbursements . . . . .	52



## AAM Section 12,100

# **General Comments on Illustrative Financial Statements—Other Comprehensive Bases of Accounting**

.01 This booklet includes illustrative accountants' reports, financial statement formats, and notes on disclosure of accounting policies for entities whose financial statements are prepared on a comprehensive basis of accounting other than generally accepted accounting principles (OCBOA). Additional notes to financial statements that may be appropriate would be comparable with those required under generally accepted accounting principles (GAAP). In practice, some accountants include the statement of changes in financial position (statement of changes in assets and liabilities—cash basis, or some other appropriate title) among financial statements prepared on comprehensive bases of accounting other than GAAP. Although not required by authoritative pronouncements, a statement of changes in financial position may be useful to the user of financial statements prepared on a comprehensive basis of accounting other than GAAP. A recommendation of this statement by the practitioner should be based on the specific facts and circumstances of each case. Such statements of changes in financial position would be comparable with the illustrations in the *Audit and Accounting Manual* (AAM), section 11,500, and accordingly are not presented in this booklet.

.02 Statement on Auditing Standards (SAS) No. 14 (AICPA, *Professional Standards*, vol. 1, AU section 621), *Special Reports*, addresses the following matters concerning financial statements prepared in accordance with a comprehensive basis of accounting other than GAAP:

- Descriptions of each basis that constitutes a comprehensive basis of accounting other than GAAP [SAS No. 14, paragraph 4 (AICPA, *Professional Standards*, vol. 1, AU section 621.04)]
- Suitable titles for financial statements prepared on a comprehensive basis of accounting other than GAAP [SAS No. 14, paragraph 7 (AICPA, *Professional Standards*, vol. 1, AU section 621.07)]
- Reporting by auditors on financial statements prepared in accordance with a comprehensive basis of accounting other than GAAP [SAS No. 14, paragraph 5 (AICPA, *Professional Standards*, vol. 1, AU section 621.05)]

.03 Adequacy of disclosure in financial statements prepared on a comprehensive basis of accounting other than GAAP is addressed in Interpretation No. 8 of SAS No. 14 (AICPA, *Professional Standards*, vol. 1, AU section 9621.34–.39) issued in February 1980 by the Auditing Standards Division of the AICPA. The interpretation states that the auditor should evaluate whether informative disclosures in such financial statements are appropriate. It is reproduced here.

The criteria the auditor should apply are essentially the same as those applicable to financial statements prepared in conformity with generally accepted accounting principles. These criteria are discussed in SAS No. 5, *The Meaning of "Present Fairly in Conformity With Generally Accepted Accounting Principles" in the Independent Auditor's Report*, paragraph 4 [AU section 411.04]. The auditor's opinion should be based on his judgment regarding whether the financial statements, including the related notes, are informative of matters that may affect their use, understanding, and interpretation.

Whenever an auditor reports on financial statements prepared on an other comprehensive basis of accounting, a note to the financial statements that states the basis of presentation and a description of how the basis of presentation differs from generally accepted accounting principles is required by SAS No. 14, paragraph 5 [AU section 621.05].

In addition, when the financial statements contain items that are the same as, or similar to, those in financial statements prepared in conformity with generally accepted accounting principles, the same degree of informative disclosures is generally appropriate. For example, financial statements prepared on an income tax basis or a modified cash basis of accounting usually reflect depreciation, long-term debt and owners' equity. Thus, the informative disclosures for depreciation, long-term debt and owners' equity in such financial statements should be comparable to those in financial statements prepared in conformity with generally accepted accounting principles.

To comply with the third standard of reporting, the auditor should also consider other matters that could reasonably be expected to materially affect the understanding of the financial statements, independent of the basis of accounting used, such as (a) contingencies and uncertainties, (b) changes in accounting principles or estimates, (c) related party transactions, (d) restrictions on assets and owners' equity, and (e) subsequent events.

These illustrative financial statement formats in sections 12,310 and 12,410 include specific cross-references to notes to financial statements. However, this is not always done in practice.

.04 The description of the cash receipts and disbursements basis in SAS No. 14, paragraph 4c (AICPA, *Professional Standards*, vol. 1, AU section 621.04c), includes the following phrase:

. . . modifications of the cash basis having substantial support, such as recording depreciation on fixed assets or accruing income taxes.

That phrase leads to the question of which modifications have "substantial support." The reply cannot be a simple reference to an authoritative source because the cash basis of accounting and modifications of the cash basis are not formalized in accounting literature as is the accrual basis of accounting. Mod-

ifications have evolved through common usage and practice. Ordinarily, a modification would have substantial support (a) if the method is equivalent to the accrual basis of accounting for the particular item and (b) if the method is not illogical (such as, recording revenue on the accrual basis and recording purchases and other costs on the cash basis). If modifications to the cash basis of accounting do not have substantial support, the accountant should include an explanatory paragraph and modify the recommended language of the applicable standard report.

.05 If the modifications are so extensive that the cash basis statements are, in the accountant's judgment, tantamount to financial statements on the accrual basis, the statements should be considered to be on the accrual basis. The accountant should use the applicable standard form of report, modified as appropriate because of departures from generally accepted accounting principles.<sup>1</sup> For example, financial statements that are presented in conformity with generally accepted accounting principles—with the exception that material leases are not capitalized (Financial Accounting Standards Board (FASB) Statement No. 13 [FASB Current Text, section L10])—are not considered to be cash basis financial statements.

.06 Authoritative literature does not address accounting for a change from generally accepted accounting principles to an other comprehensive basis of accounting. In this situation, restatement of prior period financial statements appears to be the preferable approach. Restatement allows the users to compare all periods presented because they will then be on the same basis.

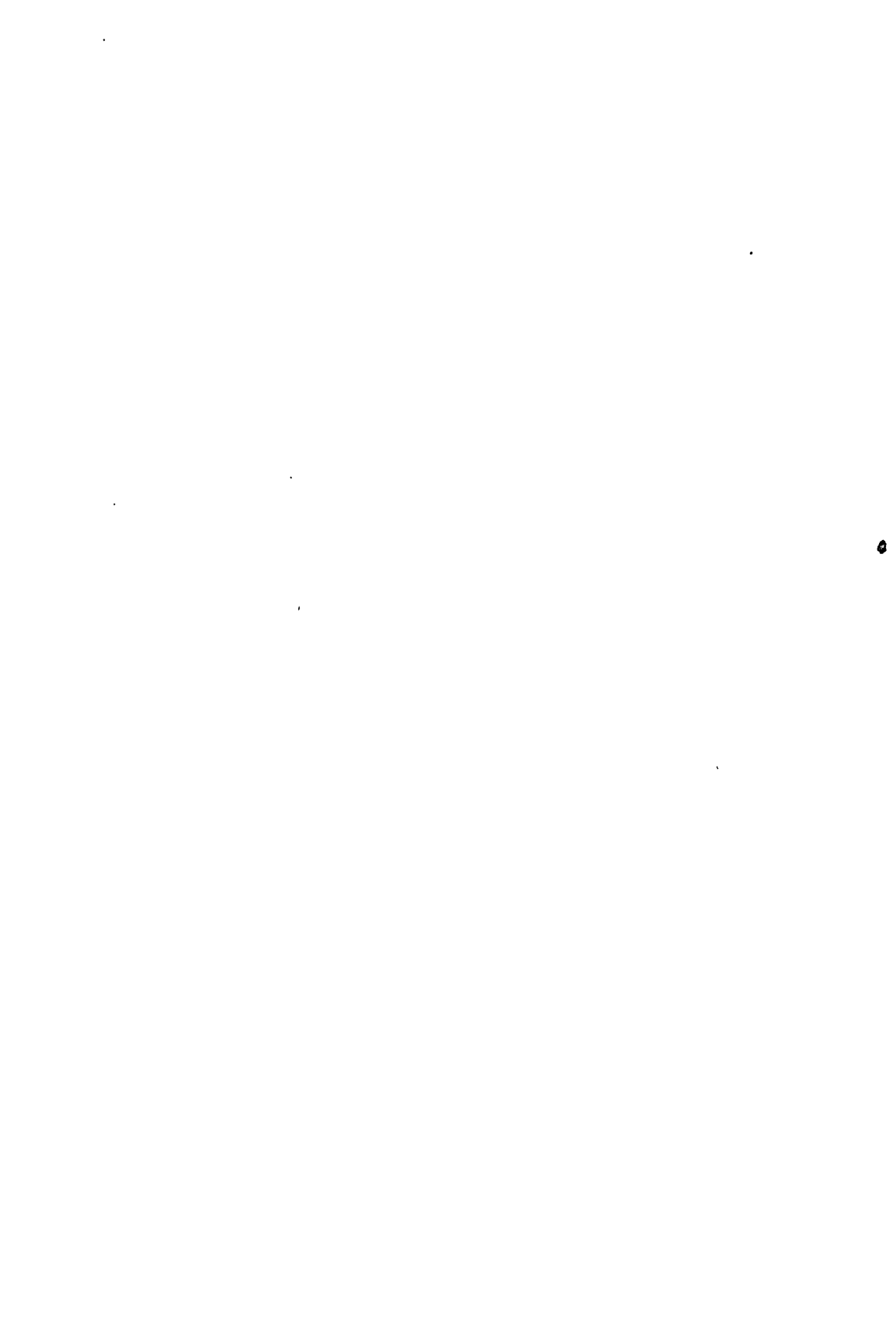
.07 When there is a change in the basis of accounting from generally accepted accounting principles to an other comprehensive basis of accounting, some accountants believe that—

- The explanatory paragraph of the auditor's report describing the basis of accounting used should indicate that the basis was adopted during the current year and that the prior year financial statements have been restated.
- The consistency reference in the opinion paragraph refers to consistent application of principles within a basis of presentation, not the consistent use of the basis of presentation. Therefore, a change in basis of presentation of financial statements from generally accepted accounting principles to an other comprehensive basis of accounting does not require the auditor to modify a report concerning consistency.

These two concepts are illustrated in an example of a report on comparative financial statements in section 12,500.11.

---

<sup>1</sup>SAS No. 2, paragraphs 15 through 17 (AICPA, *Professional Standards*, vol. 1, AU section 509.15-.17) and Statement on Standards for Accounting and Review Services (SSARS) 1, paragraphs 39 through 41 (AICPA, *Professional Standards*, vol. 2, AR section 100.39--41).



## AAM Section 12,200

# ***Description and Explanation of Bases Illustrated***

### **Overview**

.01 SAS No. 14, paragraph 4 (AICPA, *Professional Standards*, vol. 1, AU section 621.04), describes several common comprehensive bases of accounting other than generally accepted accounting principles.

- a. A basis of accounting that the reporting entity uses to comply with the requirements or financial reporting provisions of a government regulatory agency to whose jurisdiction the entity is subject. Examples include a basis of accounting that is prescribed in a uniform system of accounts that the Interstate Commerce Commission requires railroad companies to use and a basis of accounting that insurance companies use pursuant to the rules of a state insurance commission
- b. A basis of accounting that the reporting entity uses or expects to use to file its income tax return for the period covered by the financial statements
- c. The cash receipts and disbursements basis of accounting, as well as modifications of the cash basis having substantial support, such as recording depreciation on fixed assets or accruing income taxes
- d. A definite set of criteria having substantial support is applied to all material items appearing in financial statements, such as the price-level basis of accounting

.02 This booklet includes illustrations of the cash and income tax bases of accounting.

### **Cash Basis**

.03 The cash basis of accounting consists of recording transactions on the basis of cash receipts and disbursements with the results that (a) certain revenue and the related assets are recognized when received rather than when earned and that (b) certain expenses are recognized when paid rather than when the obligation is incurred. The cash basis is usually accompanied by certain modifications that have substantial support, such as capitalizing fixed assets, recog-

nizing debt arising from cash transactions, recording depreciation on fixed assets, and accruing income taxes on cash basis income. When accompanied by these modifications the basis is often described as the *modified cash basis*.

.04 Examples of entities that may use this cash basis include professional service organizations and individuals such as accountants, doctors, and lawyers.

.05 The cash basis also encompasses the presentation of a summary of cash receipts and disbursements. In this form of presentation cash receipts from sales, debt, contributions, and so forth, and disbursements for debt repayment, expenses, and the purchase of fixed assets are summarized to show the change in the cash balance for a period. [See section 12,310.16]

.06 Examples of some entities that may use this limited form of cash basis accounting are estates, trusts, civic ventures, and student activity funds.

## **Tax Basis**

.07 Entities that use the tax basis of accounting are typically either profit-oriented enterprises (such as small, closely held retail and manufacturing companies) for which conversion to GAAP would be costly or partnerships (such as tax shelters) whose partnership agreements require use of the tax basis of accounting.



## **AAM Section 12,300**

# ***Recommended Measurement and Disclosure Guidelines—Cash Basis***

### **General Comments**

.01 The measurement and disclosure guidelines for financial statements presented on the cash basis of accounting are set forth in this section.

### **Measurement Guidelines**

.02 Under the cash basis of accounting, the financial statements generally reflect assets, liabilities, income, and expenses arising from cash transactions, as well as certain accruals and amortizations that have substantial support.

.03 Adjusting one element of the financial statements without adjusting related items may be illogical. (For example, presenting sales on the accrual basis and purchases on the cash basis is illogical. Sales and purchases should be presented on the same basis because of their interrelationship.)

### **Disclosure Guidelines**

#### **General**

.04 Each financial statement should include prominent disclosure that it is prepared on the cash basis of accounting. Each page of the financial statements would be enhanced by including, where applicable, a reference to the notes to the financial statements, which are an integral part of the financial statements. One such reference would state that “the accompanying notes are an integral part of the financial statements.” Other wording may also be appropriate.

#### **Significant Accounting Policies**

.05 The notes, preferably the first note, to the financial statements should contain a “Summary of Significant Accounting Policies.” This note should describe the cash basis, including any accrual adjustments or modifications, and disclose material differences between the basis and GAAP.

.06 Modifications or adjustments of the cash basis should have substantial support.

### **Accounting Changes**

.07 The nature and effect on income of an accounting change should be disclosed in the period in which the change is made. Accounting changes consist of changes in methods of accounting and changes in accounting estimates.

### **Business Combinations**

.08 In the period in which a business combination occurs, information disclosed should include the following:

- a. The names and brief descriptions of the acquired or combined companies
- b. Information about any adjustments made to the carrying bases of the assets and liabilities of any of the companies as a result of the combination, as well as the period for which the results of operations of the acquired or combined companies are included in the income statement
- c. The consideration given, including the number and type of any shares of stock issued
- d. Contingent payments, options, and commitments arising from the combination (specified in the related agreement)

### **Related Party Transactions**

.09 The existence of related parties with which the reporting entity has participated in transactions that are material individually or in the aggregate and the nature and amounts of the transactions should be disclosed.

### **Pension Plans and Commitments and Contingencies**

.10 The existence and nature of a pension plan, and material commitments and contingencies should be disclosed.

### **Subsequent Events**

.11 The nature and financial effects of material events and transactions that occurred subsequent to the balance sheet date but before the financial statements are issued should be disclosed.

### **Assets and Liabilities**

- .12 Information disclosed on assets and liabilities should include these items:
- a. Restricted cash, segregated from cash available for current operations with a description of the nature of the restriction
  - b. The aggregate quoted market price of marketable securities
  - c. Accounts and notes receivable from officers, employees, and affiliates, presented separately with disclosure of the effective interest rate on notes receivable
  - d. The major classes of property, plant, and equipment, depreciation expense for the period, the method or methods used in computing depreciation, and the aggregate accumulated depreciation (lessors should make separate disclosure of leased property)

- e.* For a lessee, a general description of leasing arrangements and future lease payments for five years
- f.* Interest rates, maturities, and collateral of notes payable and other debt, including a five-year schedule of maturity

### **Stockholders' Equity**

.13 The financial statements should disclose information on stockholders' equity as follows:

- a.* For each class of stock, the number of shares authorized, issued, and outstanding, the par or stated value, and, in summary form, the pertinent rights and privileges of each outstanding class if more than one class is outstanding
- b.* The existence of stock option and stock purchase plans
- c.* Restrictions on the payment of dividends
- d.* Changes for the period in the separate components of stockholders' equity

### **Income and Expense**

.14 The financial statements should disclose the following information relating to income and expense:

- a.* An explanation, where applicable, if income tax is not provided or if there is an unusual ratio of income tax to income before income taxes
- b.* The amount of tax credits
- c.* The amount of unused net operating loss and tax credit carryovers, together with their expiration dates
- d.* The nature and financial effects of material events or transactions that are unusual in nature or of infrequent occurrence



## **AAM Section 12,310**

# ***Illustrative Financial Statements—Cash Basis***

### **General Comments**

.01 This section presents illustrative financial statements prepared on the cash basis. The titles used differ from those used for financial statements based on generally accepted accounting principles because both SAS No. 14 and SSARS 1 indicate that titles of financial statements prepared on an other comprehensive basis of accounting should differ from those used for GAAP statements.

.02 A method of reporting under the cash basis limited to a statement of cash receipts and disbursements showing only the changes in the cash balances is presented in paragraphs .16 and .17.

Illustrative financial statements are on following pages.

# Cash Basis—Financial Statements (a Corporation)

## .03 Statements of Assets and Liabilities—Cash Basis

Y and Z Corporation  
 Statements of Assets and Liabilities—Cash Basis  
 December 31, 19X2 and 19X1

	<u>19X2</u>	<u>19X1</u>
<b>Assets</b>		
Current assets		
Cash .....	\$ x,xxx	\$ x,xxx
Due from officer (Note 2)* .....	—	<u>x,xxx</u>
Total current assets	<u>x,xxx</u>	<u>x,xxx</u>
Property and equipment, at cost (Note 1)		
Furniture .....	xx,xxx	xx,xxx
Office equipment .....	xx,xxx	xx,xxx
Leasehold improvements .....	<u>x,xxx</u>	<u>x,xxx</u>
	xx,xxx	xx,xxx
Less accumulated depreciation and amortization (Note 1) .....	<u>(x,xxx)</u>	<u>(x,xxx)</u>
	<u>xx,xxx</u>	<u>xx,xxx</u>
	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>
<b>Liabilities</b>		
Current liabilities		
Loan payable to bank, current portion (Note 3) .....	\$ x,xxx	\$ x,xxx
Note payable to officer (Note 2)* .....	<u>x,xxx</u>	—
Total current liabilities	<u>x,xxx</u>	<u>x,xxx</u>
Loan payable to bank less current portion included above (Note 3) .....	<u>x,xxx</u>	<u>x,xxx</u>
	<u>x,xxx</u>	<u>x,xxx</u>
<b>Stockholders' Equity</b>		
Common stock, \$xxx par value, authorized xxx number of shares, issued and outstanding xxx shares .....	x,xxx	x,xxx
Additional paid-in capital .....	xx,xxx	xx,xxx
Retained earnings—cash basis .....	<u>x,xxx</u>	<u>x,xxx</u>
	<u>xx,xxx</u>	<u>xx,xxx</u>
	<u>\$ xx,xxx</u>	<u>\$ xx,xxx</u>

The accompanying notes are an integral part of the financial statements.

\*If the promissory notes are continuously renewed at the due date, the accounts should be classified out of the current asset or liability section.

**.04 Statements of Revenues and Expenses, and Retained Earnings—Cash Basis**

Y and Z Corporation  
 Statements of Revenues and Expenses,  
 and Retained Earnings—Cash Basis  
 For the Years Ended December 31, 19X2 and 19X1

	<u>19X2</u>	<u>19X1</u>
<b>Revenues</b>		
Operating revenues .....	\$ xx,xxx	\$ xx,xxx
Miscellaneous .....	x,xxx	x,xxx
	<u>xxx,xxx</u>	<u>xxx,xxx</u>
<b>Expenses</b>		
Salaries and bonuses .....	xx,xxx	xx,xxx
Advertising .....	xx,xxx	xx,xxx
Rent (Note 5) .....	x,xxx	x,xxx
Depreciation and amortization (Note 1) .....	x,xxx	x,xxx
State and local income taxes paid .....	x,xxx	x,xxx
Federal income taxes paid (Notes 1 and 4) .....	xx,xxx	xx,xxx
Other expenses paid .....	x,xxx	x,xxx
	<u>xxx,xxx</u>	<u>xxx,xxx</u>
Excess of revenues over expenses .....	xx,xxx	xx,xxx
<b>Retained earnings—cash basis</b>		
Balance, beginning of year .....	<u>x,xxx</u>	<u>x,xxx</u>
	xx,xxx	xx,xxx
Less cash dividends paid during the year .....	<u>(xx,xxx)</u>	<u>(xx,xxx)</u>
Balance, end of year .....	<u>\$ x,xxx</u>	<u>\$ x,xxx</u>

The accompanying notes are an integral part of the financial statements.

## **.05 Notes to Financial Statements—Cash Basis**

### Y and Z Corporation Notes to Financial Statements—Cash Basis

#### Note 1—Summary of Significant Accounting Policies

- Principles of Accounting

The Company prepares its financial statements on the cash basis but includes depreciation and amortization of capitalized assets. Under this basis, revenues are recognized when collected rather than when earned, and expenses are recognized when paid rather than when incurred. Consequently, accounts receivable due from customers, amounts due vendors and suppliers, and the unpaid portion of taxes at December 31, 19X2 and 19X1, are not included in the financial statements.

- Property and Equipment

If an expenditure results in an asset having an estimated useful life that extends beyond the year of acquisition, the expenditure is capitalized. Furniture, office equipment, and leasehold improvements are recorded at cost. Depreciation on furniture and office equipment is provided on the double declining-balance method over the estimated useful lives of the assets. Amortization of leasehold improvements is provided on the straight-line method over the term of the lease or the estimated useful lives of the improvements, whichever is shorter.

- Income Taxes

Income taxes are recognized as an expense when paid. Income taxes incurred are determined on a cash receipts and disbursements method. Investment tax credits are accounted for as a reduction of federal income taxes in the period the benefit is realized.

#### Note 2—Transactions With Related Parties

At December 31, 19X1, Officer A owed \$x,xxx to the Company. This amount was repaid with interest at 10 percent per annum. During the current year, the Company borrowed \$x,xxx from Officer B in exchange for a promissory note due November 30, 19X3, bearing interest at 10 percent per annum.

#### Note 3—Loan Payable to Bank

This debt consisted of the following:

	December 31, 19X2	December 31, 19X1
	<u>          </u>	<u>          </u>
Loan payable, bank		
Due in quarterly installments		
of \$x,xxx until December 31,		
19Y2, plus interest at xx% . . .	\$xx,xxx	\$xx,xxx
Less current maturities . . . . .	<u>(x,xxx)</u>	<u>(x,xxx)</u>
Long-term portion . . . . .	<u>\$ x,xxx</u>	<u>\$ x,xxx</u>



Long-term debt matures in the next five years as follows:

19X3	\$ x,xxx
19X4	x,xxx
19X5	x,xxx
19X6	x,xxx
19X7	x,xxx
	<u>\$ x,xxx</u>

#### Note 4—Income Taxes

The company benefited from investment tax credits of \$x,xxx in 19X2 and \$x,xxx in 19X1. At December 31, 19X2, investment tax credit carryforwards of \$xx,xxx are available to be applied against future taxable income. The amounts expire as follows:

<u>Expiration Year Ending</u>	<u>Investment Tax Credit Carryovers</u>
19X3	\$xx,xxx
19X4	\$xx,xxx
19X5	\$xx,xxx
19X6	\$xx,xxx
19X7	\$xx,xxx

#### Note 5—Leases

The Company leases office space and certain data processing and other equipment under leases for varying terms. At December 31, 19X2, the minimum rental payments under noncancellable leases with a term in excess of one year were as follows:

19X3	\$xx,xxx
19X4	\$xx,xxx
19X5	\$xx,xxx
19X6	\$xx,xxx
19X7	\$xx,xxx

#### Note 6—Contingencies

The Company is involved in litigation involving a claim for \$xx,xxx, which, in the opinion of the Company's legal counsel, is not expected to result in an award that would have a materially adverse effect on the Company's financial position.

The Internal Revenue Service has examined the Company's income tax returns through 19X0, or the period during which such returns could be examined has expired. No examinations were under way or completed during 19X2.

## Cash Basis—Financial Statements (a Partnership)

### .06 Statements of Assets and Liabilities—Cash Basis

Alpha and Bravo, a Partnership  
 Statements of Assets and Liabilities—Cash Basis  
 December 31, 19X2 and 19X1

	<u>19X2</u>	<u>19X1</u>
<b>Assets</b>		
Current assets		
Cash .....	\$xx,xxx	\$xx,xxx
U.S. treasury bill, at cost which approximates market .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Total current assets .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Property and equipment, at cost (Note 1)		
Furniture and equipment .....	xx,xxx	xx,xxx
Law books .....	xx,xxx	xx,xxx
Leasehold improvements .....	<u>xx,xxx</u>	<u>xx,xxx</u>
	xx,xxx	xx,xxx
Less accumulated depreciation and amortization (Note 1) .....	<u>(xx,xxx)</u>	<u>(xx,xxx)</u>
	<u>xx,xxx</u>	<u>xx,xxx</u>
Total assets .....	<u><u>\$xx,xxx</u></u>	<u><u>\$xx,xxx</u></u>
<b>Liabilities and Partners' Capital</b>		
Current liabilities		
Current portion of note payable (Note 2) .....	\$xx,xxx	\$xx,xxx
Payroll taxes withheld and accrued .....	xx,xxx	xx,xxx
Client advances .....	xx,xxx	xx,xxx
Pension contribution payable .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Total current liabilities .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Note payable due April 30, 19X6, less current portion included above (Note 2) .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Total liabilities .....	xx,xxx	xx,xxx
Partners' capital .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Total liabilities and partners' capital .....	<u><u>\$xx,xxx</u></u>	<u><u>\$xx,xxx</u></u>

The accompanying notes are an integral part of the financial statements.

## **.07 Statements of Revenues and Expenses—Cash Basis**

Alpha and Bravo, a Partnership  
Statements of Revenues and Expenses—Cash Basis  
For the Years Ended December 31, 19X2 and 19X1

	<u>19X2</u>	<u>19X1</u>
Revenues		
Professional fees .....	\$xxx,xxx	\$xxx,xxx
Interest .....	x,xxx	x,xxx
Other .....	x,xxx	x,xxx
Gain on involuntary conversion (Note 6) .....	—	x,xxx
	<u>xxx,xxx</u>	<u>xxx,xxx</u>
Expenses		
Salaries		
Professional .....	xx,xxx	xx,xxx
Other .....	xx,xxx	xx,xxx
Payroll taxes		
Professional .....	xx,xxx	xx,xxx
Other .....	xx,xxx	xx,xxx
Pension (Note 4)		
Professional .....	x,xxx	x,xxx
Other .....	x,xxx	x,xxx
Group insurance		
Professional .....	xx,xxx	xx,xxx
Other .....	xx,xxx	xx,xxx
Insurance—general .....	xx,xxx	xx,xxx
Outside professional services .....	xx,xxx	xx,xxx
Rent (Note 3) .....	xx,xxx	xx,xxx
Office supplies and expense .....	xx,xxx	xx,xxx
Telephone .....	xx,xxx	xx,xxx
Dues .....	xx,xxx	xx,xxx
Subscriptions and books .....	xx,xxx	xx,xxx
Travel and entertainment .....	xx,xxx	xx,xxx
Equipment rental .....	xx,xxx	xx,xxx
Maintenance and repairs .....	xx,xxx	xx,xxx
Depreciation and amortization (Note 1) .....	xx,xxx	xx,xxx
Use tax .....	xx,xxx	xx,xxx
Interest .....	xx,xxx	xx,xxx
Continuing legal education .....	xx,xxx	xx,xxx
Utilities .....	xx,xxx	xx,xxx
Miscellaneous .....	xx,xxx	xx,xxx
	<u>xxx,xxx</u>	<u>xxx,xxx</u>
Excess of revenues over expenses .....	<u>\$xxx,xxx</u>	<u>\$xxx,xxx</u>

The accompanying notes are an integral part of the financial statements.

## .08 Statements of Changes in Partners' Capital—Cash Basis

Alpha and Bravo, a Partnership  
 Statements of Changes in Partners' Capital—Cash Basis  
 For the Years Ended December 31, 19X2 and 19X1

	<u>Alan B. Alpha</u>	<u>Bertrand S. Bravo</u>	<u>Cynthia Q. Charlie</u>	<u>Total</u>
Balance, January 1, 19X1 .....	\$xx,xxx	\$xx,xxx	\$xx,xxx	\$xx,xxx
19X1				
Excess of revenues over expenses .....	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
Decreases in equity				
Withdrawals .....	xx,xxx	xx,xxx	xx,xxx	xx,xxx
Contribution to pension fund*	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
Total decreases .....	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
Balance, December 31, 19X1 ....	xx,xxx	xx,xxx	xx,xxx	xx,xxx
19X2				
Excess of revenues over expenses .....	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
Decreases in equity				
Withdrawals .....	xx,xxx	xx,xxx	xx,xxx	xx,xxx
Contribution to pension fund*	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
Total decreases .....	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>	<u>xx,xxx</u>
Balance, December 31, 19X2 ....	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

The accompanying notes are an integral part of the financial statements.

\*This represents one of the reporting alternatives available. Some partnerships may prefer to include partners' salaries and pension benefits among expenses for financial reporting purposes. The reporting classification of partners' salaries and pension benefits would be based on the specific facts and circumstances of each case. Where the facts and circumstances do not require inclusion in expenses for financial reporting purposes, some partnerships would combine partners' salaries and pension benefits with other withdrawals and reflect only one decrease in equity.

## .09 Notes to Financial Statements—Cash Basis

### Alpha and Bravo, a Partnership Notes to Financial Statements—Cash Basis

#### Note 1—Summary of Significant Accounting Policies

- Principles of Accounting

The Company prepares its financial statements on the cash basis but includes depreciation and amortization of capitalized assets, liabilities for payroll withholdings, and accrual of payroll taxes and pension plan contributions. Under this basis, revenues are recognized when collected rather than when earned, and expenses are generally recognized when paid rather than incurred. Consequently, the financial statements do not include accounts receivable due from clients, amounts due vendors and suppliers, and prepaid expenses and liabilities for accrued expenses other than those described above as of December 31, 19X2 and 19X1.

- Property and Equipment

If an expenditure results in an asset having an estimated useful life that extends beyond the year of acquisition, the expenditure is capitalized. Furniture, equipment, law books, and leasehold improvements are recorded at cost. Depreciation of furniture, equipment, and law books is provided on the double declining-balance method over the estimated useful lives of the assets. Amortization of leasehold improvements is provided on the straight-line method over the term of the lease or the estimated useful lives of the improvements, whichever is shorter.

- Income Taxes

The Company is not subject to income taxes as a separate entity. Taxes on income of the partnership are determined by the individual circumstances of each partner and based on the individual income tax returns of the partners. Consequently, partnership excess of revenues over expenses is presented without a provision for taxes on income.

#### Note 2—Note Payable

Note payable consisted of the following:

	December 31, <u>19X2</u>	December 31, <u>19X1</u>
Note payable, bank		
Due in quarterly installments of \$x,xxx until April 30, 19X6, plus interest at xx% . . . .	\$xx,xxx	\$xx,xxx
Less current maturities . . . . .	<u>(xx,xxx)</u>	<u>(xx,xxx)</u>
Long-term portion . . . . .	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

Long-term debt maturing in the next five years consists of the following:

19X3	\$xx,xxx
19X4	xx,xxx
19X5	xx,xxx
19X6	xx,xxx
19X7	<u>xx,xxx</u>
	<u>\$xx,xxx</u>

Note 3—Leases

The Company leases office space and certain data processing and other equipment under leases for varying terms. At December 31, 19X2, the minimum rental payments under noncancellable leases with a term in excess of one year were as follows:

19X3	\$xx,xxx
19X4	\$xx,xxx
19X5	\$xx,xxx
19X6	\$xx,xxx
19X7	\$xx,xxx

Note 4—Pension Plan

The Company maintains a defined benefit pension plan that covers substantially all employees. The pension plan expense was \$x,xxx in 19X2 and \$x,xxx in 19X1. The pension plan contribution was in accordance with the requirements of the pension plan trustee.

Note 5—Contingencies

The Company is involved in litigation involving a claim for \$xx,xxx, which, in the opinion of the Company's legal counsel, is not expected to result in an award that would have a materially adverse effect on the Company's financial position.

The Internal Revenue Service has examined the Company's income tax returns through 19X0, or the period during which such returns could be examined has expired. No examinations were under way or completed during 19X2.

Note 6—Unusual Item

Certain of the Company's assets were destroyed by fire on September 3, 19X1. The gain, recorded as a separate item in the income statement, represents the difference between the insurance proceeds received and the depreciated cost of the assets.

# Cash Basis—Financial Statements (a Professional Corporation)

## .10 Statements of Assets and Liabilities—Cash Basis

M, O and D, P.C.		
Statements of Assets and Liabilities—Cash Basis		
December 31, 19X2 and 19X1		
	<u>19X2</u>	<u>19X1</u>
Assets		
Current assets		
Cash .....	\$ xx,xxx	\$ xx,xxx
U.S. treasury bill, at cost, which approximates market. ....	xx,xxx	xx,xxx
Total current assets .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Equipment and leasehold improvements, at cost (Notes 1 and 3)		
Dental equipment .....	xxx,xxx	xxx,xxx
Office equipment .....	xx,xxx	xx,xxx
Leasehold improvements .....	xx,xxx	xx,xxx
	<u>xxx,xxx</u>	<u>xxx,xxx</u>
Less, accumulated depreciation and amortization ....	<u>(x,xxx)</u>	<u>(x,xxx)</u>
Net equipment and leasehold improvements. ....	<u>xx,xxx</u>	<u>xx,xxx</u>
Due from stockholder (Note 2) .....	<u>x,xxx</u>	<u>x,xxx</u>
Total assets .....	<u><u>\$xxx,xxx</u></u>	<u><u>\$xxx,xxx</u></u>
Liabilities		
Current liabilities		
Current portion of installment loan (Note 3). ....	\$ xx,xxx	\$ xx,xxx
Payroll taxes and withholdings .....	x,xxx	x,xxx
Accrued federal income taxes .....	x,xxx	x,xxx
Accrued profit sharing. ....	x,xxx	x,xxx
Total current liabilities .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Installment loan, less current portion included above (Note 3). ....	<u>xx,xxx</u>	<u>xx,xxx</u>
	<u>xx,xxx</u>	<u>xx,xxx</u>
Stockholders' equity		
Common stock \$10 par value; 1000 shares authorized; issued and outstanding 300 shares in 19X2, 200 shares in 19X1 .....	x,xxx	x,xxx
Additional paid-in capital .....	xx,xxx	xx,xxx
Retained earnings—cash basis .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Total stockholders' equity .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Total liabilities and stockholders' equity .....	<u><u>\$xxx,xxx</u></u>	<u><u>\$xxx,xxx</u></u>

The accompanying notes are an integral part of the financial statements.

**.11 Statements of Revenues and Expenses, and Retained Earnings—Cash Basis**

M, O and D, P.C.  
 Statements of Revenues and Expenses, and  
 Retained Earnings—Cash Basis  
 For Years Ended December 31, 19X2 and 19X1

	<u>19X2</u>	<u>19X1</u>
Revenues		
Fees .....	\$xxx,xxx	\$xxx,xxx
Interest income .....	x,xxx	x,xxx
	<u>xxx,xxx</u>	<u>xxx,xxx</u>
Expenses		
Dental supplies .....	x,xxx	x,xxx
Depreciation and amortization (Note 1) .....	x,xxx	x,xxx
Dues and licenses .....	xxx	xxx
Insurance .....	x,xxx	x,xxx
Interest .....	x,xxx	x,xxx
Laboratory fees .....	x,xxx	x,xxx
Maintenance and repairs—dental equipment .....	x,xxx	x,xxx
Maintenance and repairs—other .....	xxx	xxx
Medical reimbursement plan .....	x,xxx	x,xxx
Miscellaneous .....	x,xxx	x,xxx
Office supplies and expense .....	x,xxx	x,xxx
Pension (Note 6) .....	x,xxx	x,xxx
Profit sharing (Note 6) .....	x,xxx	x,xxx
Professional fees .....	x,xxx	x,xxx
Professional meetings and seminars .....	x,xxx	x,xxx
Rent (Note 5) .....	x,xxx	x,xxx
Salaries—officers .....	xxx,xxx	xxx,xxx
Salaries—other .....	xx,xxx	xx,xxx
Taxes—payroll .....	x,xxx	x,xxx
Taxes—other .....	x,xxx	x,xxx
Telephone .....	x,xxx	x,xxx
Travel .....	xxx	xxx
Utilities .....	x,xxx	x,xxx
	<u>xxx,xxx</u>	<u>xxx,xxx</u>
Excess of revenues over expenses before income		
taxes .....	x,xxx	x,xxx
Income taxes (Note 4) .....	<u>x,xxx</u>	<u>x,xxx</u>
Net earnings—cash basis .....	x,xxx	x,xxx
Retained earnings—cash basis		
Balance, beginning of year .....	xx,xxx	xx,xxx
Less cash dividends paid during the year .....	<u>(x,xxx)</u>	<u>(x,xxx)</u>
Balance, end of year .....	<u>\$ xx,xxx</u>	<u>\$ xx,xxx</u>

The accompanying notes are an integral part of the financial statements.



## **.12 Notes to Financial Statements—Cash Basis**

M, O and D, P.C.

Notes to Financial Statements—Cash Basis

### Note 1—Summary of Significant Accounting Policies

- Principles of Accounting

The Company prepares its financial statements on the cash basis but includes depreciation and amortization of capitalized assets, liabilities for payroll withholdings, and accruals of payroll taxes, profit sharing contributions, and income taxes payable. Under this basis, revenues are recognized when collected rather than when earned, and expenses are generally recognized when paid rather than when incurred. Consequently, accounts receivable due from patients, trade accounts payable, and accrued expenses other than those mentioned above are not included in the financial statements as of December 31, 19X2, and 19X1.

- Equipment and Leasehold Improvements

If an expenditure results in an asset having an estimated useful life that extends beyond the year of acquisition, the expenditure is capitalized and depreciated or amortized over the estimated useful life of the asset. Equipment and leasehold improvements are recorded at cost. Depreciation of equipment is provided on the double declining-balance method over the estimated useful lives of the assets. Amortization of leasehold improvements is provided on the straight-line method over the term of the lease or the estimated useful lives of the improvements, whichever is shorter.

- Income Taxes

Investment tax credits are accounted for as a reduction of federal income taxes in the period the tax benefit is realized.

### Note 2—Transactions With Related Parties

The amount due from the stockholder bears interest at 10 percent per annum and is due November 30, 19X4.

*“Notes to Financial Statements—Cash Basis” continue on following pages.*

**.12 Notes to Financial Statements—Cash Basis (cont.)**

**Note 3—Installment Loan**

This loan consisted of the following:

	<u>December 31,</u> 19X2	<u>December 31,</u> 19X1
Loan payable, bank		
Due in quarterly installments of \$x,xxx until December 31, 19Y2, plus interest at xx%, collateralized by dental equipment	\$xx,xxx	\$xx,xxx
Less current maturities .....	( xx,xxx)	( xx,xxx)
Long-term portion .....	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

Long-term debt maturing in the next five years consists of the following:

19X3	\$xx,xxx
19X4	xx,xxx
19X5	xx,xxx
19X6	xx,xxx
19X7	<u>xx,xxx</u>
	<u>\$xx,xxx</u>

**Note 4—Income Taxes**

The Company benefited from investment tax credits of \$x,xxx in 19X2 and \$x,xxx in 19X1. At December 31, 19X2, investment tax credit carryforwards of \$xx,xxx are available to be applied against future taxable income. The amounts expire as follows:

<u>Expiration Year</u> <u>Ending</u>	<u>Investment Tax</u> <u>Credit Carryovers</u>
19X3	\$xx,xxx
19X4	\$xx,xxx
19X5	\$xx,xxx
19X6	\$xx,xxx
19X7	\$xx,xxx

**Note 5—Leases**

The Company leases office space and certain data processing and other equipment under leases for varying terms. At December 31, 19X2, the minimum rental payments under noncancellable leases with a term in excess of one year were as follows:

19X3	\$xx,xxx
19X4	\$xx,xxx
19X5	\$xx,xxx
19X6	\$xx,xxx
19X7	\$xx,xxx

**.12 Notes to Financial Statements—Cash Basis (cont.)**

**Note 6—Pension Plans and Commitments**

The Company has a profit-sharing plan that covers nonunion employees.

The Company maintains a defined-benefit pension plan that covers substantially all union employees. The pension plan expense was \$x,xxx in 19X2 and \$x,xxx in 19X1. The pension plan contribution was in accordance with the requirements of the pension plan trustee.

**Note 7—Contingencies**

The Company is involved in litigation involving a claim for \$xx,xxx, which, in the opinion of the Company's legal counsel, is not expected to result in an award that would have a materially adverse effect on the Company's financial position.

The Internal Revenue Service has examined the Company's income tax returns through 19X0, or the period during which such returns could be examined has expired. No examinations were under way or completed during 19X2.

## Cash Basis—Financial Statements (an S Corporation)

### .13 Statements of Assets and Liabilities—Cash Basis

S Incorporated  
 Statements of Assets and Liabilities—Cash Basis  
 December 31, 19X2 and 19X1

Assets	<u>19X2</u>	<u>19X1</u>
Current assets		
Cash .....	\$ x,xxx	\$ x,xxx
Due from officer (Note 2) .....	—	x,xxx
Total current assets .....	<u>x,xxx</u>	<u>x,xxx</u>
Property and equipment, at cost (Notes 1 and 3)		
Furniture .....	xx,xxx	xx,xxx
Office equipment .....	xx,xxx	xx,xxx
Leasehold improvements .....	x,xxx	x,xxx
	<u>xx,xxx</u>	<u>xx,xxx</u>
Less, accumulated depreciation and amortization (Note 1) .....	( x,xxx)	( x,xxx)
Total assets .....	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>
Liabilities		
Current liabilities		
Note payable to bank (Note 3) .....	\$ xx,xxx	\$ xx,xxx
Accrued state and local income taxes (Note 1) .....	x,xxx	—
Total current liabilities .....	<u>x,xxx</u>	<u>x,xxx</u>
Note payable to bank less current portion included above (Note 3) .....	<u>xx,xxx</u>	<u>xx,xxx</u>
	<u>xx,xxx</u>	<u>xx,xxx</u>
Stockholders' equity		
Common stock, \$xxx par value, authorized xxx num- ber of shares, issued and outstanding xxx shares ..	x,xxx	x,xxx
Additional paid-in capital .....	xx,xxx	xx,xxx
Retained earnings—cash basis (Note 1) .....	x,xxx	x,xxx
	<u>xx,xxx</u>	<u>xx,xxx</u>
Total liabilities and stockholders' equity .....	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

The accompanying notes are an integral part of the financial statements.

**.14 Statements of Revenues and Expenses, and Retained Earnings—Cash Basis**

S Incorporated  
 Statements of Revenues and Expenses,  
 and Retained Earnings—Cash Basis  
 For the Years Ended December 31, 19X2 and 19X1

	<u>19X2</u>	<u>19X1</u>
Revenues		
Operating revenue .....	\$xx,xxx	\$xx,xxx
Miscellaneous .....	x,xxx	x,xxx
	<u>xx,xxx</u>	<u>xx,xxx</u>
Expenses		
Salaries and bonuses .....	xx,xxx	xx,xxx
Advertising .....	xx,xxx	xx,xxx
Rent (Note 4) .....	x,xxx	x,xxx
Depreciation and amortization (Note 1) .....	x,xxx	x,xxx
Other .....	x,xxx	x,xxx
	<u>xx,xxx</u>	<u>xx,xxx</u>
Excess of revenues over expenses before provision		
for income taxes .....	xx,xxx	xx,xxx
Provision for state and local income taxes (Note 1) .....	x,xxx	x,xxx
Excess of revenues over expenses .....	xx,xxx	xx,xxx
Retained earnings—cash basis (Note 1)		
Balance, beginning of year .....	x,xxx	x,xxx
	xx,xxx	xx,xxx
Less dividends (Note 6) .....	( xx,xxx)	( xx,xxx)
Balance, end of year .....	<u>\$ x,xxx</u>	<u>\$ x,xxx</u>

The accompanying notes are an integral part of the financial statements.

**.15 Notes to Financial Statements—Cash Basis**

S Incorporated  
Notes to Financial Statements—Cash Basis

Note 1—Summary of Significant Accounting Policies

● Principles of Accounting

The Company prepares its financial statements on the cash basis but includes depreciation and amortization of capitalized assets, and accrued liabilities for state and local income taxes payable. Under this basis, revenues are recognized when collected rather than when earned, and expenses are generally recognized when paid rather than when incurred. Consequently, commissions receivable, trade accounts payable, prepaid expenses, and certain accrued expenses at December 31, 19X2 and 19X1, are not included in the financial statements.

● Property and Equipment

If an expenditure results in the creation of an asset having an estimated useful life that extends beyond the year of acquisition, the expenditure is capitalized and depreciated or amortized over the estimated useful life of the asset. Property, equipment, and leasehold improvements are recorded at cost. Depreciation of property and equipment is provided on the straight-line method over the estimated useful lives of the assets. Amortization of leasehold improvements is provided on the straight-line method over the term of the lease or the estimated useful lives of the improvements, whichever is shorter.

● Income Taxes

The Company has elected by unanimous consent of its stockholders to be taxed under the provisions of Subchapter S of the Internal Revenue Code. Under those provisions, the Company does not pay federal corporate income taxes on its taxable income. [S Incorporated is allowed no net operating loss carryover or carryback as a deduction.\*] Instead, the stockholders are liable for individual federal income taxes on their respective shares of the Company's taxable income. [The stockholders include their respective shares of the Company's net operating loss in their individual income tax returns.\*]

Note 2—Transactions With Related Parties

At December 31, 19X1, Officer A owed \$x,xxx to the Company. This amount was repaid with interest at 10 percent per annum.

Note 3—Note Payable to Bank

This debt consisted of the following:

	December 31, <u>19X2</u>	December 31, <u>19X1</u>
Note payable, bank		
Due in quarterly installments of \$x,xxx until December 31, 19Y2, plus interest at xx%, collateralized by office equipment.....	\$xx,xxx	\$xx,xxx
Less current maturities.....	<u>(xx,xxx)</u>	<u>(xx,xxx)</u>
Long-term portion.....	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

\*Additional illustrative language in the event of an operating loss.

**.15 Notes to Financial Statements—Cash Basis (cont.)**

Long-term debt maturing in the next five years consists of the following:

19X3	\$xx,xxx
19X4	xx,xxx
19X5	xx,xxx
19X6	xx,xxx
19X7	xx,xxx
	<u>\$xx,xxx</u>

**Note 4—Leases**

The Company leases office space and certain data processing and other equipment under leases for varying terms. At December 31, 19X2, the minimum rental payments under noncancellable leases with a term in excess of one year were as follows:

19X3	\$xx,xxx
19X4	\$xx,xxx
19X5	\$xx,xxx
19X6	\$xx,xxx
19X7	\$xx,xxx

**Note 5—Contingencies**

The Company is involved in litigation involving a claim for \$xx,xxx, which, in the opinion of the Company's legal counsel, is not expected to result in an award that would have a materially adverse effect on the Company's financial position.

The Internal Revenue Service has examined the Company's income tax returns through 19X0, or the period during which such returns could be examined has expired. No examinations were under way or completed during 19X2.

Under certain circumstances, the Company's election can be retroactively terminated by the Internal Revenue Service and the Company may be required to pay federal income taxes.

**Note 6—Dividends**

A dividend of \$xx,xxx was declared and paid on February 15, 19X2.\*

---

\*S Corporations often pay substantial dividends after the end of the year. A dividend declared before the end of the year generally would be recorded as a liability and shown separately in the statement of assets and liabilities. A dividend declared after the end of the year would be disclosed as a subsequent event in conformity with FASB Statement No. 5, paragraph 11 (*FASB Current Text*, section C59.112) and SAS No. 1, section 560.01-.09 (AICPA, *Professional Standards*, vol. 1, AU section 560.01-09).

# Cash Basis—Financial Statement (Not-for-Profit)

## .16 Statement of Cash Receipts and Disbursements

ABC Charity—Dinner Fund  
Statement of Cash Receipts and Disbursements  
For the Year Ended December 31, 19X5

Cash receipts		
Contributions .....	\$xx,xxx	
Sales of raffle tickets .....	xx,xxx	
Advances from ABC Charity General Fund .....	x,xxx	
Interest on passbook savings accounts.....	<u>xxx</u>	
Total cash receipts .....		\$xx,xxx
Cash disbursements		
Food purchases .....	\$xx,xxx	
Refund of advances from ABC Charity— General Fund.....	x,xxx	
Advertising.....	x,xxx	
Professional fees .....	x,xxx	
Postage.....	x,xxx	
Travel.....	x,xxx	
Telephone .....	x,xxx	
Rental (Note 2) .....	x,xxx	
Raffle prizes .....	x,xxx	
Contribution to (Name of Recipient) .....	<u>xx,xxx</u>	
Total cash disbursements .....		<u>xx,xxx</u>
Excess of cash receipts over cash disbursements		xx,xxx
Cash balance, January 1, 19X5.....		<u>x,xxx</u>
Cash balance, December 31, 19X5 .....		<u>\$ x,xxx</u>
Cash balance as of December 31, 19X5, is accounted for as follows:		
Demand deposit, Tenth National Bank .....		\$ xxx
Passbook deposit, Penny Savings Bank .....		<u>x,xxx</u>
Total .....		<u>\$ x,xxx</u>

The accompanying notes are an integral part of the financial statements.



## **.17 Notes to Statement of Cash Receipts and Disbursements**

### ABC Charity–Dinner Fund Notes to Statement of Cash Receipts and Disbursements

#### Note 1—Accounting Policies

The ABC Charity–Dinner Fund financial statement presents cash receipts and cash disbursements in accordance with the resolution of April 1, 19XX, of the Board of Governors of ABC Charity. [Consequently, revenues are recognized when received rather than when earned, and expenses are recognized when paid rather than when the obligation is incurred.]\* It is the policy of the ABC Charity–Dinner Fund Committee to have no outstanding advances to or from the ABC Charity–General Fund at year-end.

#### Note 2—Leases

The Fund leases office space and certain data processing and other equipment under leases for varying terms. At December 31, 19X5, the minimum rental payments under noncancellable leases with a term in excess of one year were as follows:

19X6	\$xx,xxx
19X7	\$xx,xxx
19X8	\$xx,xxx
19X9	\$xx,xxx
19Y0	\$xx,xxx

#### Note 3—Commitments and Contingencies

The Fund is involved in litigation involving a claim for \$xx,xxx, which, in the opinion of the Fund's legal counsel, is not expected to result in an award that would have a materially adverse effect on the Fund's financial position.

---

\*Some accountants omit this sentence from the above note because the related statement merely presents cash receipts and cash disbursements, does not include the terms "revenue" and "expense," and does not purport to present financial position and results of operations.



## **AAM Section 12,400**

# ***Recommended Measurement and Disclosure Guidelines— Income Tax Basis***

### **General Comments**

.01 The measurement and disclosure guidelines for material items in financial statements presented on the income tax basis of accounting are set forth in this section. Guidance is provided on the measurements of assets and related revenues as well as liabilities and related expenses that do not enter into taxable income.

### **Measurement Guidelines**

.02 The income tax basis of accounting is based upon the principles and rules for accounting for transactions under the federal income tax laws and regulations. Few new measurement guidelines need to be established because this method is based upon federal tax laws. This method covers a range of alternative bases from cash to full accrual, depending on the nature of the taxpayer, and in some circumstances, the taxpayer's elections. It is believed that this basis of accounting is useful to small, nonpublic entities who find that the cost of GAAP financial statements is not beneficial in relation to the needs of likely users. Most users of financial statements can be expected to recognize and understand the nature of the income tax basis.

### **Nontaxable Revenues**

.03 Under the federal income tax laws, receipts from some sources, such as interest on obligations of state and local governments and proceeds from life insurance policies, are excluded from revenue for income tax purposes. In presenting financial statements on the income tax basis, nontaxable revenues should be recognized when they are received or when they are accruable and should be reported in the income statement.

### **Nondeductible Expenses**

.04 Costs incurred for some expense items, such as premiums paid on officers' life insurance policies, are not deductible for income tax purposes. In financial statements prepared on the income tax basis of accounting, nondeductible expenses should be reported and charged to expense in the period in which they are incurred. For example, charitable contributions in excess of IRS

limitations should be charged to expense in the year incurred. The amounts should be included in the income statement in the appropriate expense category.

### **Additional Income Taxes for Prior Years**

.05 Additional income taxes for prior years may be assessed as the result of an examination by the Internal Revenue Service (IRS). Two alternative methods may be used to account for additional taxes for prior years:

- a. The amount may be charged to expense in the current period if there are no corresponding adjustments to the balance sheet for expenses capitalized or revenue recognized.
- b. The amount may be treated as a prior period adjustment and charged to retained earnings.

Either method is considered acceptable in the preparation of financial statements on the income tax basis. The method used should be disclosed in the financial statements.

### **Adjustments to Balance Sheet for IRS Changes**

.06 The IRS may disallow amounts charged to expense in prior years and require those amounts to be capitalized and amortized or may require recognition of previously unreported revenue. Such amounts, net of income tax adjustments, should be treated as prior period adjustments.

### **Accounting Changes for Tax Purposes**

.07 For tax purposes, the effects of an accounting change may be recognized prospectively over a period of ten years. In income-tax-basis financial statements, the total effect should be recorded in the year of the change and amortized over the ten-year period.

### **S Corporations**

.08 Income of an S Corporation is taxable to its shareholders; consequently, such a corporation may be required to maintain information on distinct classes of retained earnings. However, in financial statements prepared on the income tax basis, S Corporations should report retained earnings as a single amount and should report distributions to stockholders as dividends.

## **Disclosure Guidelines**

### **General**

.09 Each financial statement should include prominent disclosure that it is prepared on the income tax basis of accounting. Each page of the financial statements would be enhanced by including, where applicable, a reference to the notes to the financial statements, which are an integral part of the financial statements. One such reference would state that "the accompanying notes are an integral part of the financial statements." Other wording may also be appropriate.

## **Significant Accounting Policies**

.10 The notes, preferably the first note, to the financial statements should contain a "Summary of Significant Accounting Policies." The note should disclose the following:

- a. Whether the basic method of accounting is cash or accrual
- b. The tax filing status of the entity if other than a normal taxable corporation
- c. That revenues and related assets and expenses and related obligations are recognized when they are reported or deducted for federal income tax purposes
- d. That nontaxable income and nondeductible expenses are included in the determination of net income
- e. The nature of any optional tax methods of accounting followed
- f. The nature of any important judgments or policies necessary for an understanding of the methods of recognizing revenue and allocating costs to current and future periods

However, this note need not repeat detailed information already presented on the face of the financial statements or elsewhere in the notes to the financial statements. The note should briefly state how the statements differ from generally accepted accounting principles.

.11 Disclosures made in interim financial statements should include information on how inventories and costs of sales were determined. These disclosures also should indicate that deferrals and accruals have been provided only when they would have been provided at year-end and, thus, the statements should not be viewed as an indicator of results for the year.

## **Accounting Changes**

.12 The nature and effect on income of an accounting change should be disclosed in the period in which the change is made. Accounting changes consist of changes in the methods of accounting and changes in accounting estimates.

## **Business Combinations**

.13 In the period in which a business combination occurs, information disclosed should include the following:

- a. The names and brief descriptions of the acquired or combined companies
- b. Information about any adjustments made to the carrying basis of the assets and liabilities of any of the companies as a result of the combination and the period for which the results of operations of the acquired or combined companies are included in the income statement
- c. The consideration given, including the number and type of any shares of stock issued
- d. Contingent payments, options, and commitments arising from the combination and specified in the related agreement

### **Related Party Transactions**

.14 The existence of related parties with which the reporting entity has participated in transactions that are material individually or in the aggregate and the nature and amounts of the transactions should be disclosed.

### **Pension Plans and Commitments and Contingencies**

.15 The existence and nature of a pension plan and material commitments and contingencies should be disclosed.

### **Subsequent Events**

.16 The nature and financial effects should be disclosed of material events and transactions that are unusual in nature or are of infrequent occurrence that occurred subsequent to the balance sheet date but before the financial statements are issued.

### **Assets and Liabilities**

.17 Information disclosed on assets and liabilities should include these items:

- a. Restricted cash, segregated from cash available for current operations with a description of the nature of the restriction
- b. The aggregate quoted market price of marketable securities
- c. Accounts and notes receivable from officers, employees, and affiliates, presented separately with disclosure of the effective interest rate on notes receivable
- d. The method of determining inventory cost (for example, LIFO, FIFO)
- e. The major classes of property, plant, and equipment, including assets recorded under lease purchase agreements, depreciation expense for the period, the method or methods used in computing depreciation, and the aggregate accumulated depreciation (lessors should make separate disclosure of leased property)
- f. For a lessee, a general description of leasing arrangements and future lease payments for five years
- g. Interest rates, maturities, and collateral of notes payable and other debt, including a five-year schedule of maturity

### **Stockholders' Equity**

.18 The financial statements should disclose information on stockholders' equity as follows:

- a. For each class of stock, the number of shares authorized, issued, and outstanding, the par or stated value, and, in summary form, the pertinent rights and privileges of each outstanding class if more than one class is outstanding
- b. The existence of stock option and stock purchase plans

- c. Restrictions on the payment of dividends
- d. Changes for the period in the separate components of stockholders' equity

**Income and Expense**

.19 The financial statements should disclose the following information relating to income and expense:

- a. An explanation, where applicable, if income tax is not provided or if there is an unusual relationship between income before income taxes and income taxes
- b. The amount of tax credits
- c. The amount of unused net operating loss and tax credit carryovers, together with their expiration dates
- d. The nature and financial effects of material events or transactions that are unusual in nature or are of infrequent occurrence





## **AAM Section 12,410**

# ***Illustrative Financial Statements— Income Tax Basis***

### **General Comments**

.01 This section presents illustrative financial statements prepared on the income tax basis. The titles used for the financial statements differ from those used for financial statements based on generally accepted accounting principles because both SAS No. 14 and SSARS 1 indicate that titles of financial statements prepared on an other comprehensive basis of accounting should differ from those used for GAAP statements.

*Illustrative financial statements are on following pages.*

## .02 Statements of Assets and Liabilities—Income Tax Basis

ABC Company  
Statements of Assets and Liabilities—Income Tax Basis  
December 31, 19X2 and 19X1

Assets	<u>19X2</u>	<u>19X1</u>
Current assets		
Cash .....	\$ xx,xxx	\$ xx,xxx
Temporary investments in municipal securities, at cost plus accrued interest (market 19X2, \$xx,xxx, 19X1, \$xx,xxx) .....	xx,xxx	xx,xxx
Accounts receivable, less allowances for bad debts 19X2, \$x,xxx, 19X1, \$x,xxx (Notes 3 and 5) ..	xx,xxx	xx,xxx
Installment accounts receivable, net of deferred income 19X2, \$x,xxx, 19X1, \$x,xxx (Note 1) .....	xx,xxx	xx,xxx
Inventories at LIFO (Notes 1, 2, and 5) .....	xx,xxx	xx,xxx
Prepaid expenses .....	xx,xxx	xx,xxx
Total current assets	<u>xx,xxx</u>	<u>xx,xxx</u>
Advances to affiliate (Note 3) .....	xx,xxx	xx,xxx
Investment in affiliate, at cost (Note 1) .....	xx,xxx	xx,xxx
Property, plant, and equipment, at cost less accumulated depreciation and amortization 19X2, \$x,xxx, 19X1, \$x,xxx (Notes 1, 4, 5, and 8) .....	xx,xxx	xx,xxx
Cash surrender value of life insurance on officers (face amount \$xxx,xxx) .....	x,xxx	x,xxx
Total assets .....	<u>\$xxx,xxx</u>	<u>\$xxx,xxx</u>
Liabilities		
Current liabilities		
Accounts payable .....	\$ xx,xxx	\$ xx,xxx
Construction loan payable (Note 1) .....	xx,xxx	xx,xxx
Current maturities of long-term debt .....	xx,xxx	xx,xxx
Accrued expenses .....	xx,xxx	xx,xxx
Income taxes payable (Notes 1, 6, and 8) .....	xx,xxx	xx,xxx
Total current liabilities .....	<u>x,xxx</u>	<u>x,xxx</u>
Long-term debt, less current maturities (Note 5) .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Stockholders' equity		
Common stock, \$xx par value, authorized x,xxx shares, issued and outstanding xxx shares .....	x,xxx	x,xxx
Additional paid-in capital .....	xx,xxx	xx,xxx
Retained earnings—income tax basis .....	xx,xxx	xx,xxx
Total stockholders' equity .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Total liabilities and equity .....	<u>\$xxx,xxx</u>	<u>\$xxx,xxx</u>

The accompanying notes are an integral part of the financial statements.

### **.03 Statements of Revenues and Expenses—Income Tax Basis**

ABC Company  
Statements of Revenues and Expenses—Income Tax Basis  
For the Years Ended December 31, 19X2 and 19X1

	<u>19X2</u>	<u>19X1</u>
Revenues		
Sales, less returns and allowances		
19X2, \$x,xxx, 19X1, \$x,xxx (Note 3) .....	\$xx,xxx	\$xx,xxx
Deferred income on installment sales .....	(x,xxx)	(x,xxx)
Deferred income recognized .....	x,xxx	x,xxx
Dividends received from affiliate .....	x,xxx	x,xxx
Interest .....	x,xxx	x,xxx
Gain on sale of building .....	x,xxx	x,xxx
Nontaxable interest .....	x,xxx	x,xxx
	<u>xx,xxx</u>	<u>xx,xxx</u>
Expenses (Notes 1 and 4)		
Cost of sales .....	xx,xxx	xx,xxx
General and administrative .....	xx,xxx	xx,xxx
Selling .....	xx,xxx	xx,xxx
Premium on officers' life insurance .....	x,xxx	x,xxx
	<u>xx,xxx</u>	<u>xx,xxx</u>
Income before federal income taxes .....	xx,xxx	xx,xxx
Federal income taxes (Notes 1, 6, and 8) .....	<u>xx,xxx</u>	<u>xx,xxx</u>
Net income—income tax basis .....	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

The accompanying notes are an integral part of the financial statements.

### **.04 Statements of Retained Earnings—Income Tax Basis**

ABC Company  
Statements of Retained Earnings—Income Tax Basis  
For the Years Ended December 31, 19X2 and 19X1

	<u>19X2</u>	<u>19X1</u>
Balance, beginning of year .....	\$xx,xxx	\$xx,xxx
Net income .....	xx,xxx	xx,xxx
Less dividends .....	( xx,xxx)	( xx,xxx)
Balance, end of year .....	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

The accompanying notes are an integral part of the financial statements.

## **.05 Notes to Financial Statements—Income Tax Basis**

### ABC Company

#### Notes to Financial Statements—Income Tax Basis

##### Note 1—Summary of Significant Accounting Policies

- **Basis of Accounting**

The accompanying financial statements have been prepared on the accrual method of accounting used for federal income tax purposes. Consequently, as indicated below, certain revenues and expenses are recognized in the determination of income in different reporting periods than they would be if the financial statements were prepared in conformity with generally accepted accounting principles. Although income tax rules are used to determine the timing of the reporting of revenues and expenses, nontaxable revenues and nondeductible expenses are included in the determination of net income.

- **Installment Sales and Related Receivables**

Gross profit on certain installment sales is presented as deferred income in the balance sheet and recognized as income when collected. If the accompanying financial statements were prepared in conformity with generally accepted accounting principles, the gross profit would be recognized when the sale is made and deferred income taxes would be provided for the timing difference between recognition of income for financial reporting purposes and determination of income taxes.

- **Inventories**

Inventories are generally stated at cost determined by the last-in, first-out (LIFO) method, which is not in excess of market.

- **Investment in L Corporation**

The Company's investment in 30 percent of the common stock of L Corporation is stated at cost. Dividends thereon are recognized as income when received. If the investment were presented in conformity with generally accepted accounting principles, it would also include the Company's share of the undistributed earnings of L Corporation since acquisition. The Company's share of the current earnings of L Corporation would be recognized as an increase of the investment and as income when earned by L Corporation. Deferred income taxes would be provided for the timing difference between recognition of income for financial reporting purposes and for determination of income taxes. Dividends received from L Corporation would be recognized as a reduction in the investment with related reduction of deferred taxes provided thereon.

- **Property, Plant, and Equipment**

Property, plant, and equipment are recorded at cost. Depreciation of property, plant, and equipment placed in service prior to January 1, 19X1, is provided on the double declining-balance method over the estimated useful lives of the assets. For property, plant, and equipment placed in service after December 31, 19X0, depreciation is based on the Accelerated Cost Recovery System (ACRS).

Interest on the construction loan to finance construction of the combined shopping center and headquarters facility in East Wherever is expensed as incurred. Real estate taxes on that property are also expensed as incurred. The accompanying financial statements would be modified in the following ways had they been prepared in conformity with generally accepted accounting principles. Interest costs and real estate taxes would be capitalized as part of the cost of the asset. Deferred income taxes would

**.05 Notes to Financial Statements—Income Tax Basis (cont.)**

be provided thereon for the timing difference between the recognition of such costs as a component of depreciation provided over the estimated useful life of the asset and recognition as a deduction for determination of taxable income.

● **Net Income—Income Tax Basis**

In accordance with the Company's policy, net income—income tax basis includes nontaxable revenue and nondeductible expenses in addition to taxable revenues, deductible expenses, and income taxes.

(Other matters that would be disclosed in the Summary of Significant Accounting Policies include the accounting followed for matters such as involuntary conversions, severance awards, exchanges of similar property, and tax elections that have a material effect on the financial statements.)

**Note 2—Inventories**

Inventories at December 31, 19X2 and 19X1, consist of the following:

	<u>19X2</u>	<u>19X1</u>
Raw materials	\$xx,xxx	\$xx,xxx
Work in process	xx,xxx	xx,xxx
Finished goods	<u>xx,xxx</u>	<u>xx,xxx</u>
	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

**Note 3—Transactions With Related Parties**

Accounts receivable included \$x,xxx at December 31, 19X2, and \$x,xxx at December 31, 19X1, due from L Corporation, an affiliated company, and sales included \$x,xxx in 19X2 and \$x,xxx in 19X1 resulting from transactions with L Corporation.

Advances to affiliate consist of \$xx,xxx, advanced to L Corporation at an effective interest rate of xx percent.

*.05 Notes to Financial Statements—Income Tax Basis (cont.)*

Note 4—Property, Plant, and Equipment

Property, plant, and equipment consisted of the following:

	December 31, 19X2	December 31, 19X1
Land .....	\$xx,xxx	\$xx,xxx
Building .....	xx,xxx	xx,xxx
Equipment .....	xx,xxx	xx,xxx
Leasehold improvements .....	x,xxx	x,xxx
Construction in process .....	<u>xx,xxx</u>	<u>xx,xxx</u>
	xx,xxx	xx,xxx
Less accumulated depreciation and amortization .....	( x,xxx)	( x,xxx)
	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

Depreciation expense was \$x,xxx in 19X2 and \$x,xxx in 19X1.

Note 5—Long-Term Debt

Long-term debt consisted of the following:

	December 31, 19X2	December 31, 19X1
Notes payable, bank		
Due in quarterly installments of \$x,xxx until December 31, 19Y2, plus interest at xx%, collateralized by receivables and inventory .....	\$xx,xxx	\$xx,xxx
Mortgage payable		
Due in quarterly payments of \$x,xxx until December 31, 19Z2, including interest at xx%, collateralized by land and building	<u>xx,xxx</u>	<u>xx,xxx</u>
	xx,xxx	xx,xxx
Less current maturities .....	( xx,xxx)	( xx,xxx)
Long-term portion .....	<u>\$xx,xxx</u>	<u>\$xx,xxx</u>

Long-term debt maturing in the next five years consists of the following:

19X3	\$xx,xxx
19X4	xx,xxx
19X5	xx,xxx
19X6	xx,xxx
19X7	<u>xx,xxx</u>
	<u>\$xx,xxx</u>

*.05 Notes to Financial Statements—Income Tax Basis (cont.)*

Note 6—Income Taxes

The Company benefited from investment tax credits of \$x,xxx in 19X2 and \$x,xxx in 19X1. At December 31, 19X2, there are investment tax credit carryforwards of \$xx,xxx available to be applied against future taxable income. The amounts expire as follows:

<u>Expiration Year Ending</u>	<u>Investment Tax Credit Carryovers</u>
19X3	\$xx,xxx
19X4	\$xx,xxx
19X5	\$xx,xxx
19X6	\$xx,xxx
19X7	\$xx,xxx

Note 7—Leases

The Company leases office space and certain data processing and other equipment under leases for varying terms. At December 31, 19X2, the minimum rental payments under noncancellable leases with a term in excess of one year were as follows:

19X3	\$xx,xxx
19X4	\$xx,xxx
19X5	\$xx,xxx
19X6	\$xx,xxx
19X7	\$xx,xxx

Note 8—Pension Plans and Commitments and Contingencies

The Company has a commitment of \$xx,xxx for completion of a building.

The Company maintains a defined benefit pension plan that covers substantially all employees. The pension plan expense was \$x,xxx in 19X2 and \$x,xxx in 19X1. The pension plan contribution was in accordance with requirements of the pension plan trustee.

The Company is involved in litigation involving a claim for \$xx,xxx, which, in the opinion of the Company's legal counsel, is not expected to result in an award that would have a materially adverse effect on the Company's financial position.

The Internal Revenue Service has examined the Company's income tax returns through 19X0, or the period during which such returns could be examined has expired. No examinations were under way or completed during 19X2.

Note 9—Subsequent Event

In February 19X3, a fire at the Company's plant destroyed \$xx,xxx of inventory. The Company has filed a claim with its insurance carrier for the full amount of the loss.





## AAM Section 12,500

# ***Types of Accountants' Reports***

### **Overview**

.01 These examples illustrate various audit, review, and compilation reports on financial statements prepared on a comprehensive basis of accounting other than GAAP.

.02 Examples that are assembled from illustrative reporting language set forth in Statements on Auditing Standards and Statements on Standards for Accounting and Review Services include citation of the particular source and its location in the AICPA's *Professional Standards*.

*Illustrative reports are on following pages.*

## **Audit Reports**

### .03 Cash Basis Statements

We have examined the statement of assets and liabilities arising from cash transactions of XYZ Company as of December 31, 19XX, and the related statement of revenue collected and expenses paid for the year then ended. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As described in Note X, the Company's policy is to prepare its financial statements on the basis of cash receipts and disbursements; consequently, certain revenue and the related assets are recognized when received rather than when earned, and certain expenses are recognized when paid rather than when the obligation is incurred. Accordingly, the accompanying financial statements are not intended to present financial position and results of operations in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly the assets and liabilities arising from cash transactions of XYZ Company as of December 31, 19XX, and the revenue collected and expenses paid during the year then ended, on the basis of accounting described in Note X, which basis has been applied in a manner consistent with that of the preceding year.

[Source: SAS No. 14, paragraph 8 (AICPA, *Professional Standards*, vol. 1, AU section 621.08)]

### .04 Income Tax Basis Statements

We have examined the accompanying statements of assets and liabilities— income tax basis of ABC Company as of December 31, 19X2 and 19X1, and the related statements of revenues and expenses— income tax basis and retained earnings— income tax basis for the years then ended. Our examination was made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

The accompanying financial statements have been prepared on the accounting basis used by the company for federal income tax purposes as described in Note X and are not intended to be a presentation in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to above present fairly the assets, liabilities, and capital of ABC Company as of December 31, 19X2 and 19X1, and its revenue and expenses and changes in retained earnings for the years then ended, on the basis of accounting described in Note X, which basis has been applied in a consistent manner.

## **Review Reports\***

### .05 Cash Basis Statements

I (we) have reviewed the accompanying statement of assets and liabilities arising from cash transactions of XYZ Company as of December 31, 19XX, and the related statement of revenue collected and expenses paid for the year ended, in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of XYZ Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an examination in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the cash basis of accounting, as described in Note X.

### .06 Income Tax Basis Statements

I (we) have reviewed the accompanying statements of assets and liabilities—income tax basis of ABC Company as of December 31, 19X2 and 19X1, and the related statements of the revenues and expenses—income tax basis and retained earnings—income tax basis for the years then ended, in accordance with standards established by the American Institute of Certified Public Accountants. All information included in these financial statements is the representation of the management (owners) of ABC Company.

A review consists principally of inquiries of company personnel and analytical procedures applied to financial data. It is substantially less in scope than an examination in accordance with generally accepted auditing standards, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, I (we) do not express such an opinion.

Based on my (our) review, I am (we are) not aware of any material modifications that should be made to the accompanying financial statements in order for them to be in conformity with the accounting basis, as described in Note X.

---

\*When financial statements are prepared in accordance with a comprehensive basis of accounting other than generally accepted accounting principles, the notes ordinarily would state the basis of presentation and describe how that basis differs from generally accepted accounting principles. [Source: Accounting and Review Services Interpretation No. 12 of SSARS 1 (AICPA, *Professional Standards*, vol. 2, AR section 9100.41-.45)]

## **Compilation Reports\***

### .07 Cash Basis Statements—Full Disclosure

I (we) have compiled the accompanying statement of assets and liabilities arising from cash transactions of XYZ Company as of December 31, 19XX, and the related statement of revenue collected and expenses paid for the year then ended, in accordance with standards established by the American Institute of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements information that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

### .08 Cash Basis Statements—Omission of Substantially All Disclosures

I (we) have compiled the accompanying statement of assets and liabilities arising from cash transactions of XYZ Company as of December 31, 19X4, and the related statement of revenue collected and expenses paid for the year then ended, in accordance with standards established by the American Institute of Certified Public Accountants. The financial statements have been prepared on the cash basis of accounting, which is a comprehensive basis of accounting other than generally accepted accounting principles.

A compilation is limited to presenting information in the form of financial statements that is the representation of management (owners). I (we) have not audited or reviewed the accompanying financial statements and, accordingly, do not express an opinion or any other form of assurance on them.

Management has elected to omit substantially all of the informative disclosures ordinarily included in financial statements. If the omitted disclosures were included in the financial statements, they might influence the user's conclusions about the Company's assets, liabilities, equity, revenue, and expenses. Accordingly, these financial statements are not designed for those who are not informed about such matters.

---

\*When financial statements are prepared in accordance with a comprehensive basis of accounting other than generally accepted accounting principles, the notes ordinarily would state the basis of presentation and describe how that basis differs from generally accepted accounting principles. [Source: Accounting and Review Services Interpretation No. 12 of SSARS 1 (AICPA, *Professional Standards*, vol. 2, AR section 9100.41–.45)]

#### .09 Income Tax Basis Statements—Full Disclosure

I (we) have compiled the accompanying statements of assets and liabilities—  
income tax basis of ABC Company as of December 31, 19X2 and 19X1, and  
the related statements of revenues and expenses—income tax basis for the years  
then ended, in accordance with standards established by the American Institute  
of Certified Public Accountants.

A compilation is limited to presenting in the form of financial statements  
information that is the representation of management (owners). I (we) have not  
audited or reviewed the accompanying financial statements and accordingly do  
not express an opinion or any other form of assurance on them.

#### .10 Income Tax Basis Statements—Omission of Substantially All Disclosures

I (we) have compiled the accompanying statements of assets and liabilities—  
income tax basis of ABC Company as of December 31, 19X2 and 19X1, and  
the related statements of revenues and expenses—income tax basis for the years  
then ended, in accordance with standards established by the American Institute  
of Certified Public Accountants. The financial statements have been prepared  
on the accounting basis used by the Company for federal income tax purposes,  
which is a comprehensive basis of accounting other than generally accepted  
accounting principles.

A compilation is limited to presenting in the form of financial statements  
information that is the representation of management (owners). I (we) have not  
audited or reviewed the accompanying financial statements and accordingly do  
not express an opinion or any form of assurance on them.

Management has elected to omit substantially all of the disclosures ordinarily  
included in financial statements prepared on the income tax basis of accounting.  
If the omitted disclosures were included in the financial statements, they might  
influence the user's conclusions about the Company's assets, liabilities, equity,  
revenue, and expenses. Accordingly, these financial statements are not designed  
for those who are not informed about such matters.

## **Other Reports**

### .11 Report for a Change From Generally Accepted Accounting Principles to an Other Comprehensive Basis of Accounting

(explanatory paragraph)

As discussed in Note X to the financial statements, in 19X3 the Company adopted the policy of preparing its financial statements on the accrual method of accounting used for federal income tax purposes; consequently, buildings, with an estimated economic useful life of thirty-five years, are being amortized over fifteen years in accordance with the accelerated cost recovery system (ACRS) provided under the Internal Revenue Code, rather than over the estimated economic useful life of the buildings. Accordingly, the accompanying financial statements are not intended to present financial position and results of operations in conformity with generally accepted accounting principles. The financial statements for 19X2 have been restated on the income tax basis-accrual method of accounting adopted in 19X3.

(opinion paragraph)

In our opinion, the financial statements referred to in the first paragraph present fairly the assets, liabilities, and stockholders' equity of XYZ Company as of December 31, 19X3 and 19X2, and its revenue and expenses for the years then ended, on the basis of accounting described in Note X, which basis has been applied in a consistent manner.

---

Note: The above represents the concepts referred to in section 12.100.06-.07.

### .12 Report on Statements of Cash Receipts and Disbursements

We have examined the statements of cash receipts and disbursements of ABC Association for the years ended December 31, 19X2 and 19X1. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

As described in Note X, the statements of cash receipts and disbursements are summaries of the cash activity of the Association and do not present transactions that would be included in financial statements of the Association presented on the accrual basis of accounting, as contemplated by generally accepted accounting principles. Accordingly, the accompanying statements are not intended to present financial position or results of operations in conformity with generally accepted accounting principles.

In our opinion, the accompanying statements present fairly the cash receipts and disbursements of ABC Association for the years ended December 31, 19X2 and 19X1.

---

Note: This type of report would be used for the financial statement referred to in section 12.310.

## **TECHNICAL HOTLINE**

**The AICPA Technical Information Service answers inquiries about specific audit or accounting problems.**

**Call Toll Free**

**(800) 223-4158 (Except New York)  
(800) 522-5430 (New York Only)**

**This service is free to AICPA members.**