***Financial Management Wrap-Up***

**INCOME STATEMENT**

* The basic income statement formula is Revenue minus Expenses equals Net Income/Loss.
  + *Net Income/Loss = Revenue - Expenses*
* The terms income statement and financial statement are not interchangeable although they are often used that way. The income statement is only one part of the financial statement which also includes the balance sheet and supporting schedules.
* The simplified income statement format is comprised of seven major categories which are subtotals obtained by adding and subtracting the appropriate GLACs.
* The format prescribed in AR 215-5 is:

|  |  |  |  |
| --- | --- | --- | --- |
| **+** | SALES |  | 7,000 |
| **-** | COST OF GOODS SOLD | 4,900 | 70.0% |
| **=** | **GROSS INCOME FROM SALES** | 2,100 |  |
| **+** | OTHER OPERATING INCOME | 500 |  |
| **=** | **GROSS INCOME FROM OPERATIONS** | 2,600 |  |
| **-** | LABOR | 1,900 | 25.3% |
| **-** | OPERATING EXPENSES | 200 | 2.7% |
| **=** | **NET INCOME BEFORE DEPRECIATION (NIBD)** | 500 | 6.7% |
| **-** | DEPRECIATION | 275 |  |
| **=** | **NET INCOME/LOSS** | 225 | 3.0% |

* There are six steps in the trend analysis process

1. Select a type of trend analysis and lay out the data.
2. Determine where negative trends exist.
3. Select a single line where a negative trend exists and begin review of the data that is summarized to obtain the summary line of the income statement.
4. Display the GLACs that comprise the summary line in the same format as the original analysis. Determine which GLAC(s) caused the negative trend.
5. Identify the operational changes that may have caused the negative trend.
6. Decide on management action to improve performance.

**SALES**

* The single fact that distinguishes sales from other operating income is that there is always a product cost (cost of goods sold) associated with sales.
* The formula to calculate net sales is:

|  |  |
| --- | --- |
| **+** | Cash Sales |
| **+** | Credit Sales |
| **+** | Layaway Sales |
| **-** | Sales Returns and Allowances |
| **-** | Customer Discounts |
| **-** | Employee Discounts |
| **=** | **Net Sales** |

* Sales trends can be monitored in either “real” dollars or as a percent of Total Revenue. A decrease in either represents a negative trend.
* In order to prepare a Sales Analysis, management must be familiar with the source documents from which the information can be extracted. Often management must design systems which gurarantee needed data is not lost during the recording process or when entered in the accounting system. The base source documents are:
  + Daily Activity Report (DAR)
  + Cashier’s Report
  + Cash Register Reading and Detail Tapes (if applicable)
  + Scatter Sheets
  + Sales Accountability Inventories
* Full analysis of a negative and positive sales trend often requires use of several different analyses.

**OTHER OPERATING INCOME**

* Other Operating Income (OOI) is defined as the revenue collected for services provided or use of equipment/facilities. Also included in this definition is the commission paid to us by concessionaires who operate MWR related activities on the installation.
* There is never a direct cost of goods associated with OOI.
* Total OOI is computed by totaling all of the 500 series GLACs used by the activity or program.
* OOI trends can be monitored in either real dollars or as in percent of Total Revenue.

**OTHER INCOME**

* Other Income (OI) is defined as the revenue collected from other than normal operations. The funds are not generated directly from selling a product or service associated with the activities primary purpose.
* The major sources of OI are interest, gain on the sale of fund property, “grants” from higher headquarters, and charitable donations.
* Total OI is calculated by adding together all of the 800 series accounts.

**TOTAL REVENUE**

* Total Revenue is defined as the mathematical total of all of the income recorded on the income statement.
* The equation for calculating Total Revenue is the sum of Sales, Other Operating Income, and Other Income.
  + *TR = Sales + OOI + OI*
* Total Revenue is the base upon which all percentages (except COGS %) are computed.

**COST OF GOODS SOLD**

* Cost of Goods Sold (COGS) is defined as the cost associated with the purchase of merchandise which will be sold at retail. By definition, this cost includes any freight required to get the product to your location.
* The formula for calculating COGS is beginning inventory plus all purchases and receipts, minus all issues to other activities/departments, minus vendor returns, and minus ending inventory.
  + *COGS = beginning inventory + all purchases and receipts – all issues to other activities/departments – vendor returns – ending inventory.*
* COGS trends are monitored using the COGS Percentage:
  + *COGS% = COGS $ / Net Sales $ x 100*
* In order to undertand a specific problem, management must have a detailed understanding of the GLACs which are combined mathematically to calculate COGS.
* The causes of consistently low COGS% are:

1. Over Pricing
2. Under Portioning
3. Sales Recorded in the Wrong Department

* The causes of consistently high COGS% are:

1. Insufficient Pricing
2. Over Portioning
3. Employee Theft of Money or Inventory
4. Sales Recorded in the Wrong Department

* The causes for fluctuating COGS% are divided into subcategories:

1. Change in Sales Mix
2. Operational Problems
   1. Incorrect Inventory
   2. Receiving Report not Submitted
   3. Transfer Voucher not Prepared
   4. Sales Not Properly Documented
   5. Merchandise or Goods Diverted
   6. Over/Under Portioning
3. Administrative Problems
   1. Errors on Inventory Paperwork
   2. Errors on Transfer Vouchers
   3. Errors on Receiving Reports

**LABOR**

* Labor cost is defined as the total expense for services rendered by employees to complete the particular mission of the program or activity for which they work.
* Labor cost includes all of the direct cost of wages and shift differentials as well as the indirect costs resulting from the employer’s contributions to FICA, health and life insurance, worker’s compensation, and retirement.
* Total Labor costs are calculated by adding together the GLACs which are used to record the parts of Labor cost. Review of these GLACs month to month may assist management in determining causes for increasing Labor costs.
* Incorrect estimates of Labor cost for the end of the month may skew reported financial data unless management is involved in providing input.
* Labor cost is monitored using absolute dollars and Labor cost %. While the Labor cost % is the most common tool used, absolute dollars are used when Labor cost is considered a fixed cost expense.
* The formula for calculating Labor cost % is:
  + *Labor Cost % = Labor Cost $ / Total Revenue $ x 100*
* There are four possible causes for increasing Labor cost

1. Scheduling Problems
2. Staffing Problems
3. Controlling Pay and Benefits Increases
4. Excess Use of Overtime

**OTHER OPERATING EXPENSE**

* Other Operating Expense (OOE) is defined as the cost of operation not associated with COGS or Labor that are consumed to provide a product or service to the customer.
* Total OOE is calculated by adding together the individual GLACs used to record the expenses. There are more than 70 different GLACs avaiable for use.
* OOE is monitored using both absolute dollars and the OOE%. In general, we treat OOE as a variable cost and that is why the percentage is the most used method of monitoring trends.
* There are several different types of operating expenses:
  + Fixed – Do not change as use or revenue change
  + Variable – Change proportionately with changes in use or revenue.
  + Discretionary – A required expense that can be postponed without a major impact to operations
  + Nondiscretionary – A required expense that cannot be postponed.
  + Emergency – An unplanned expense which cannot be postponed.
* The formulas for calcualting the OOE% and any individual operating expense:
  + *OOE% = OOE$ / Total Rev$ x 100*
  + *Individual Expense = Ind Exp $ / Total Rev$ x 100*
* The major causes for increases in OOE are:
  + Excessive Use (Poor Controls)
  + Increasing Costs
  + Cost Shifting from APF to NAF
  + Poor Procurement
  + Poor Administration of Expense Areas

**OTHER EXPENSE**

* Other Expense (OE) is defined as expenses incurred from other than normal operations. These expenses are not generated directly from selling a product or service.
* Most of the GLACs that comprise OE can be used only at the IMWRF level.
* Total OE is calculated by adding together all of the 800 series GLACs.
* OE is less periodic than other forms of expense. By the isolated nature of the expense, it is also relatively easy to determine causes for negative trends.

**DEPRECIATION**

* Depreciation is defined as a non-cash expense which allocates the cost of the asset over its expected useful life.
* Depreciation is treated as a cost of doing business and is charged to the activity using the asset.
* Total Depreciation is calculated by adding together all of the 850 series GLACs that are used by the activity.
* Depreciation Expense is monitored based on increases and decreases in dollars as compared to a standard. While the standard is normally the budget, previous month depreciation and the depreciation for the same period last year are also used.
* The potential causes for increased Depreciation costs are:
  + Purchase of Additional Fixed Assets
  + Depreciation Schedule is Shortened
* The potential causes for decreased Depreciation costs are:
  + An Asset is Completely Depreciated
  + Fixed Assets are Sold (or disposed of)
  + Depreciation Schedule is Lengthened

**NET INCOME/LOSS**

* Net Income (Loss) is defined as the difference between Total Revenue and Total Expenses. If the figure is positive it is Net Income, and if the figure is negative it is Net Loss.
* We monitor Net Income (Loss) in terms of both absolute dollars and as a percent of Total Revenue. Absolute dollar comparisons are important because it is Net Income dollars that gurantee the future of the fund. On the other hand, use of Net Income % is useful because it relates the return on investment to the Revenue which produced it.
* The Net Income % is calculated by dividing Net Income dollars by Total Revenue dollars and multiplying by 100.
  + *Net Income (Loss) % = NI$ / TR$ x 100*

**INVENTORY MANAGEMENT**

* Inventory Management is defined as the process by which you provide a variety of merchandise that meets customer needs and desires while safeguarding the fund’s assets from theft, obsolescence, and waste.
* The value of resale inventory is determined based on multiplying the physical count of the product by the cost price to determine the total value for each line item. All of the line items are then added together for the value of total inventory.
* We monitor inventory using one or more of the techniques below:
  + Total Dollar Value –Establishes a dollar ceiling for the total value of inventory.
  + Number of Units – Establishes a minimum and maximum number of products for each inventory line item. Computes a par stock for each item.
  + Inventory Turnover Ratio – Based on computing the ratio of COGS to average inventory. Tells you how much of inventory is used to support sales in a given month.
* The formula for computing par stock:
  + *Par Stock Level = Requisition Objective + Safety Level*
  + *Par Stock Level = Average Use Per Month / Desired Inv Turnover + (Avg Daily Use x Number of Days for Delivery)*
* The formula for Inventory Turnover Ratio is:
  + *Average Inventory = Begin Inv + End Inv / 2*
  + *Inventory Turnover Ratio = COGS/Avg Inventory*
* There are three types of generic inventory problems:

1. Low Turnover
   1. Over Ordering
   2. Dead Stock
   3. Too Many Lines of Product
   4. Buying Quantity to Reduct Price
2. High Turnover
   1. Stockage Level is set too low (Requistiion Objective)
   2. Safety Level is set too low
3. Inventory Accountability
   1. Administrative
      * 1. Posting errors
        2. Transfer documents not prepared
        3. Incorrect Inventory Count
   2. Operational
      * 1. Waste
        2. Pilferage