**Income Statement & Profits**

Name and date submitted (3 pts):

Instructions: Using this as a template, respond to each question. Turn in your completed work by the due date.

(10 questions, 5 points each)

In year two of operation, your Chocolate-covered jalapeno business generates $1,000,000 in sales revenue, has cost of goods sold of $500,000, and has overhead expense (sales, marketing, and administrative) of $350,000. Your combined State-and-Federal income tax rate is 30%.

1. What is your Gross Profit in dollars?
2. What is your Net Profit before taxes in dollars?
3. What is your tax expense in dollars?
4. What is your Net Profit after taxes in dollars?

What will you do with your Net Profit? State the PROS and CONS of each of these possibilities. I’m looking for good analysis! Engage your brain and think about these before answering. Each of these has potential PITFALLS as well as VIRTUES!

1. Reinvest it in machinery & equipment needed for the business? (this is called “plowing-back” your earnings)

What will be the long term effect of this? Explain the GOOD and BAD:

1. Pay it out to your shareholders who got you started in the first place? (this is called “paying dividends”)

What will be the long term effect of this? Explain the GOOD and BAD:

1. Put it in the bank for a rainy day? (this would be called “building a cash reserve”)

What will be the long term effect of this? Explain the GOOD and BAD:

1. Pay out some portion of it to shareholders, and reinvest the other portion in the business?

What will be the long term effect of this? Explain the GOOD and BAD:

1. Tell your shareholders they need to be patient, reinvest it all in the business, and risk having a shareholder revolt?

What will be the long term effect of this? Explain the GOOD and BAD:

1. Instead of paying a portion to shareholders (i.e. dividends), or buying new equipment, just give your employees a big raise across the board?

What will be the long term effect of this? Explain the GOOD and BAD:

Income statement example:

Sales revenue $100

Less: cost of goods sold ($80)

Gross profit $20

Less: overhead expense ($10)

Net profit before tax $10

Tax expense 40% ($4)

Net profit after tax $6