

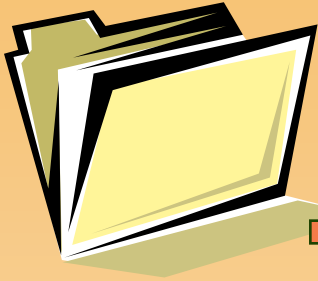
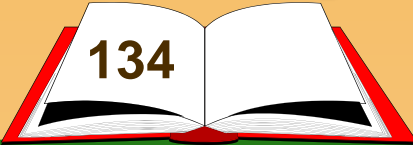
COMPLETING THE ACCOUNTING CYCLE

Atanas Atanasov

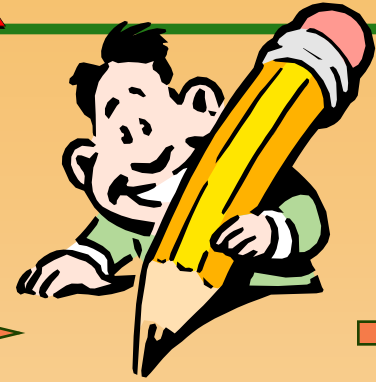
Assist.prof. University of Economics - Varna



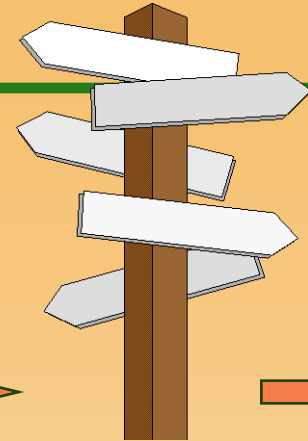
Steps in Accounting Cycle



Analyze source documents.



Journalize transactions in the journal.



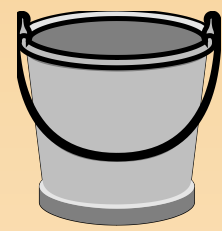
Post entries to the accounts in the ledger.



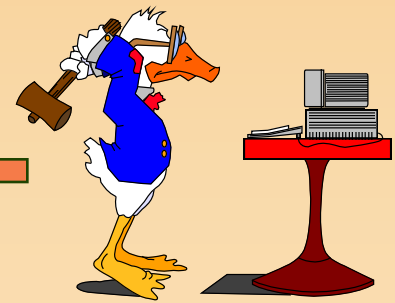
Prepare a trial balance.



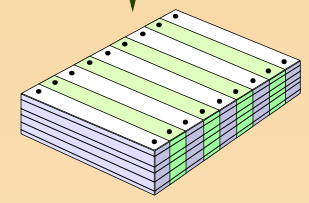
Do post-closing trial balance



Journalize and post closing entries



Journalize and post adjusting entries



Prepare financial statements.

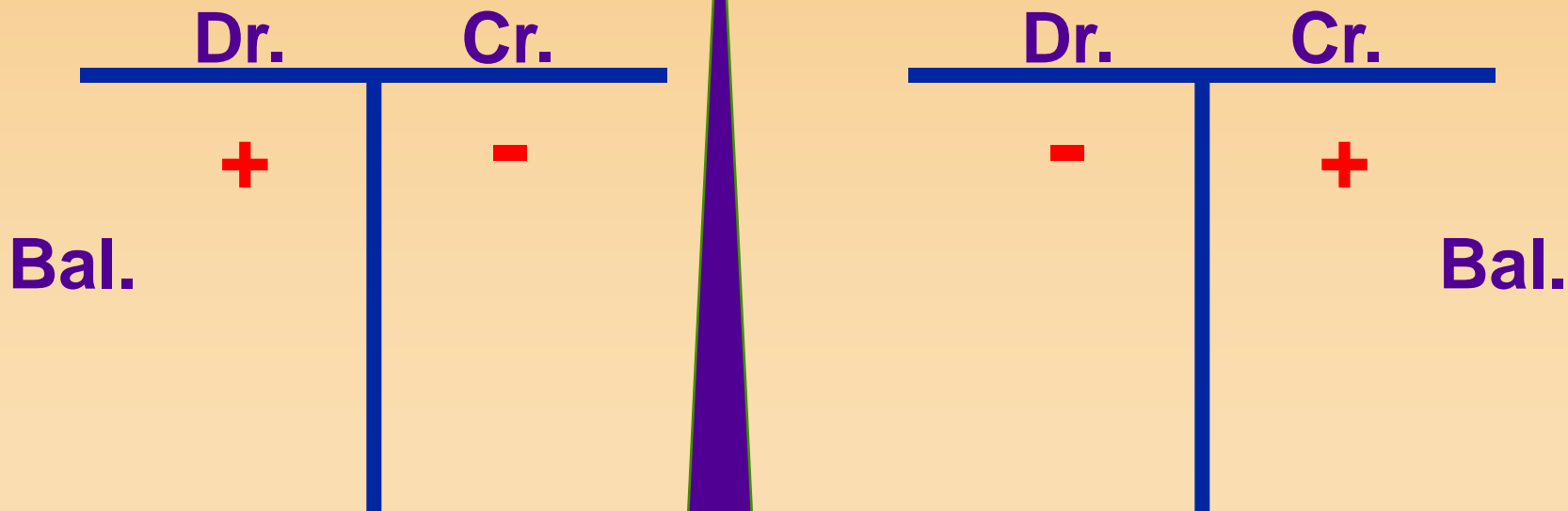


Expanded Accounting Equation

ASSETS + EXP. = LIAB. + S/H EQUITY + REV.

Permanent Temporary Permanent Permanent Temporary

A + E = L + S/E + R



A Norm, a Rule and a Question

Each revenue and expense account normally has a balance at year-end.



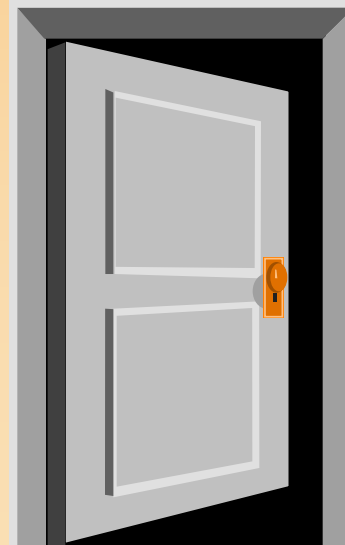
Each revenue and expense must have a \$0 balance at the beginning of the next year.



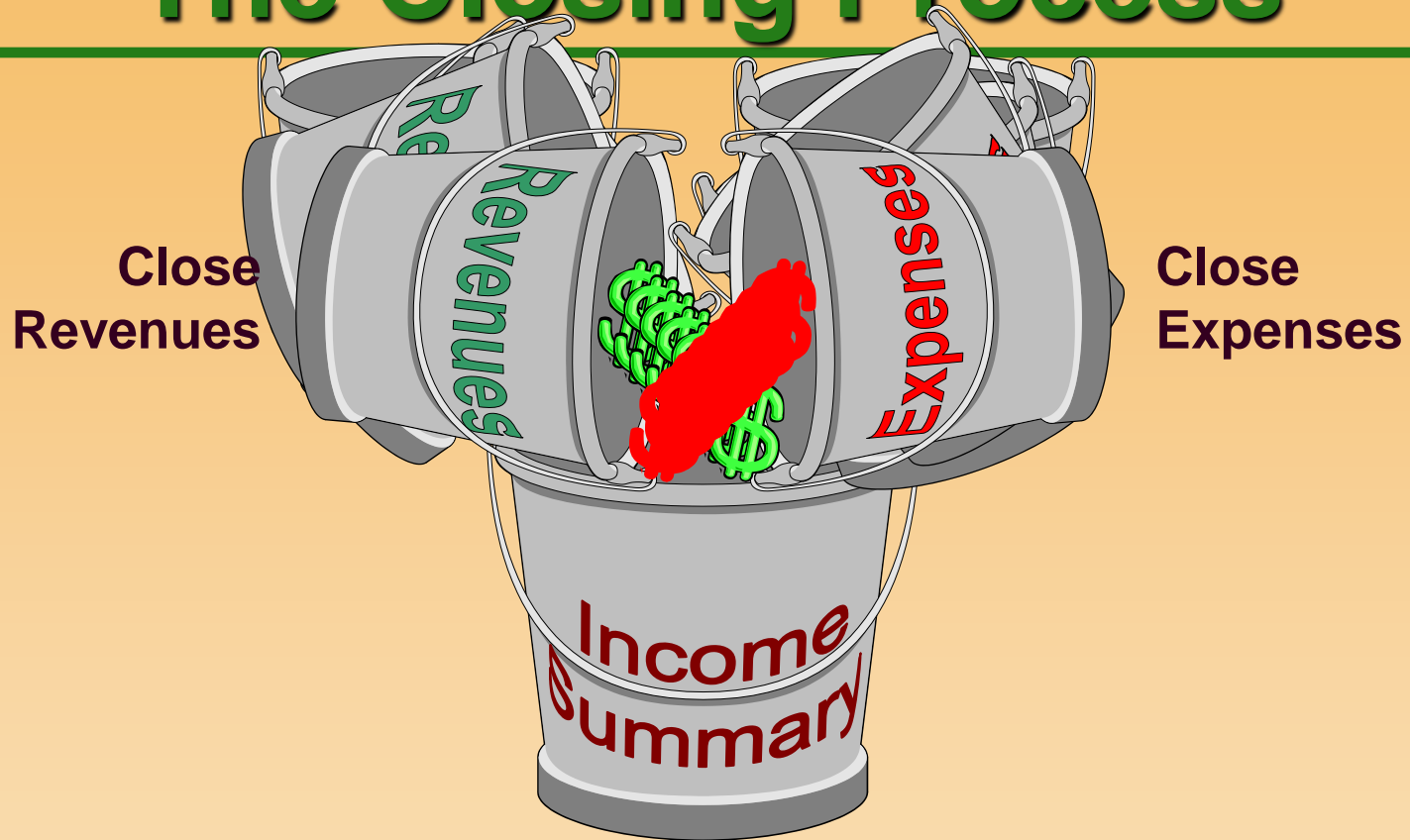
How do we get the revenues and expenses to \$0 balances for the beginning of the next year?

The Closing Process

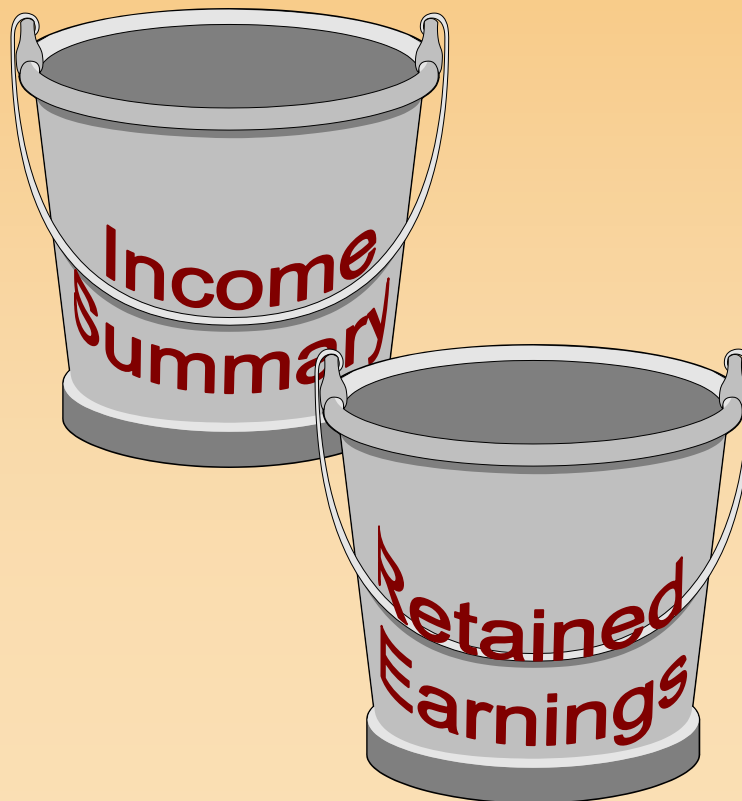
- **Transferring (“pouring”) the balances in revenue and expense accounts into the Income Summary account.**
- **Transferring the balance in Income Summary to Retained Earnings.**
- **Transferring the balance in the Dividends account to Retained Earnings.**



The Closing Process



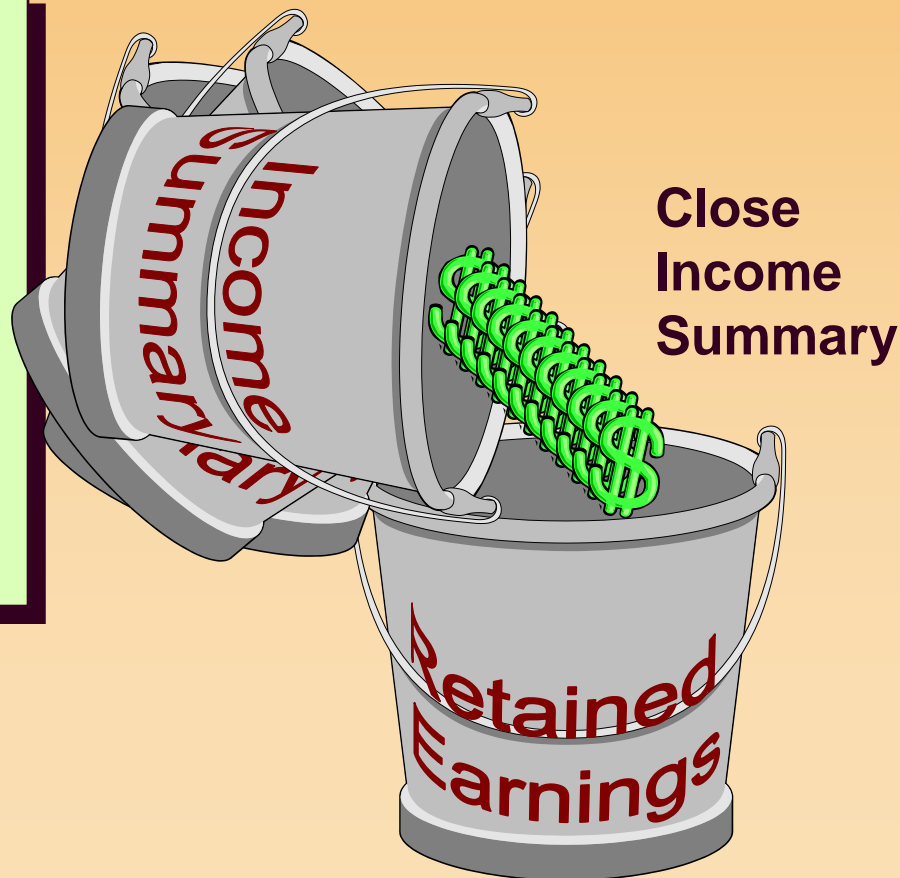
The Closing Process



The Closing Process

Income Summary

- ◆ Temporary account
- ◆ Exists only during the closing process
- ◆ Does not appear on any financial statement



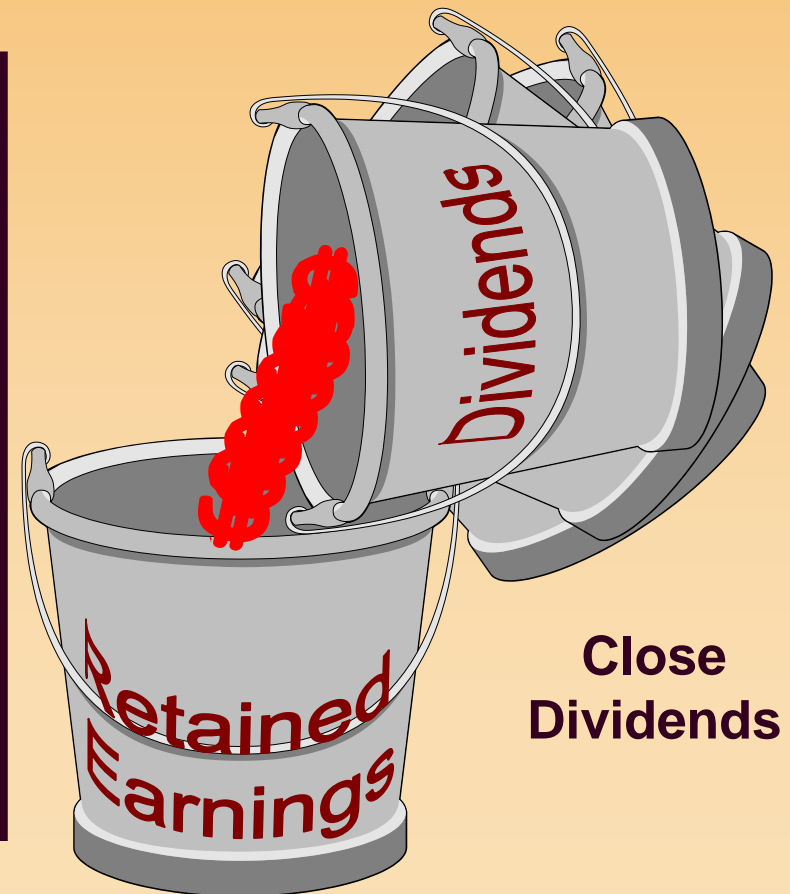
The Closing Process



The Closing Process

Summary of Steps

- ① Close Revenues to Income Summary
- ② Close Expenses to Income Summary
- ③ Close Income Summary to Retained Earnings
- ④ Close Dividends to Retained Earnings



Closing Journal Entries

T- Account Example

Used to bring revenue and expense accounts to \$0 balances for the start of the next fiscal year

Revenues have a normal balance on the credit side.

| Revenues | |
|----------|--------|
| | 25,000 |

Closing Journal Entries

T- Account Example

Used to bring revenue and expense accounts to \$0 balances for the start of the next fiscal year

How do we bring Revenues to a \$0 balance?

| Revenues | |
|----------|--------|
| | 25,000 |

Closing Journal Entries

T- Account Example

Used to bring revenue and expense accounts to \$0 balances for the start of the next fiscal year

How do we bring Revenues to a \$0 balance?

Remember: To reduce a credit balance account, debit the account.

| Revenues | |
|----------|--------|
| | 25,000 |

Closing Journal Entries

T- Account Example

Used to bring revenue and expense accounts to \$0 balances for the start of the next fiscal year

How do we bring Revenues to a \$0 balance?

We need to debit the account for \$25,000 to reduce the account to \$0.

Revenues

25,000

Closing Journal Entries

T- Account Example

Used to bring revenue and expense accounts to \$0 balances for the start of the next fiscal year

How do we bring Revenues to a \$0 balance?

We need to debit the account for \$25,000 to reduce the account to \$0.

| Revenues | |
|----------|--------|
| 25,000 | 25,000 |
| | 0 |

Closing Journal Entries

T- Account Example

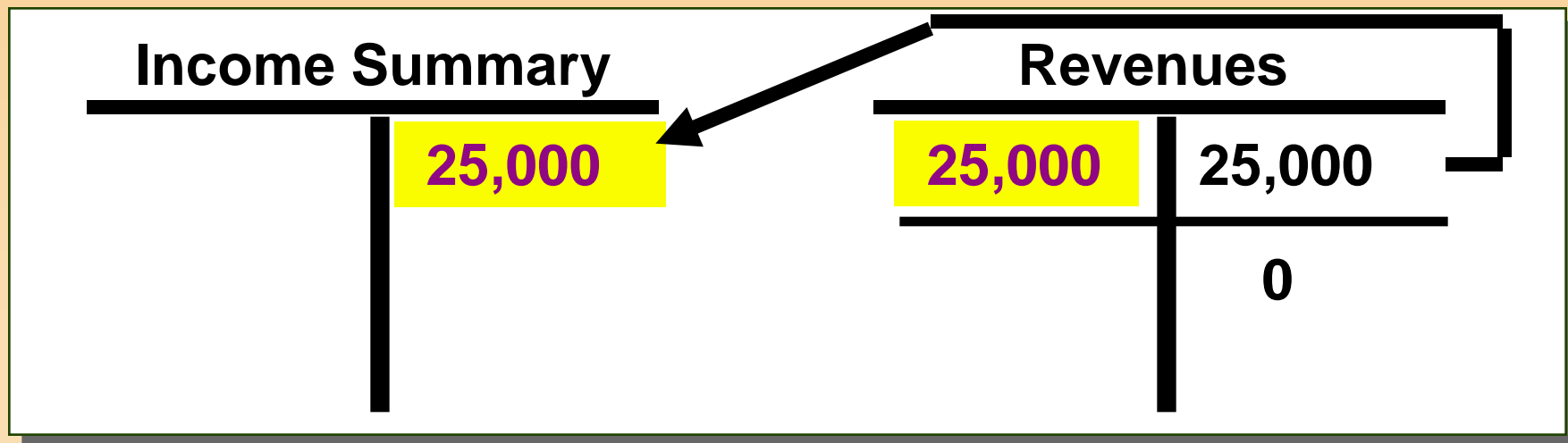
- In the previous example, a \$25,000 debit was made to close out Revenues.
- A corresponding \$25,000 credit must be made to **Income Summary**.

| Income Summary | Revenues |
|----------------|----------|
| | 25,000 |
| | 25,000 |
| | 0 |

Closing Journal Entries

T- Account Example

- In the previous example, a **\$25,000 debit** was made to close out Revenues.
- A corresponding **\$25,000 credit** must be made to **Income Summary**.



Closing Journal Entries

General Journal Example

Closing Journal Entries use the same format as other journal entries:

GENERAL JOURNAL

Page: _____ 1

| Date | Description | PR | Debit | Credit |
|-------|-------------------------|-----|--------|--------|
| MM/DD | Account Name | ### | \$\$\$ | |
| | Account Name | ### | | \$\$\$ |
| | To record closing entry | | | |
| | | | | |
| | | | | |

Closing Journal Entries

General Journal Example

On 12/31/99, Revenues has a \$25,000 balance at year-end. Prepare the journal entry to close the account.

GENERAL JOURNAL

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|------|-------------|----|-------|--------|
| | | | | |
| | | | | |
| | | | | |
| | | | | |
| | | | | |

Closing Journal Entries

General Journal Example

On 12/31/99, Revenues has a \$25,000 balance at year-end. Prepare the journal entry to close the account.

GENERAL JOURNAL

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|--------|--------------------------|----|--------|--------|
| 31-Dec | Revenues | | 25,000 | |
| | Income Summary | | | 25,000 |
| | <i>to close Revenues</i> | | | |
| | | | | |
| | | | | |

Closing Journal Entries

General Journal Example

Post the entry to the Revenue account.

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|---------------|--------------------------|----|---------------|---------------|
| 31-Dec | Revenues | | 25,000 | |
| | Income Summary | | | 25,000 |
| | <i>to close Revenues</i> | | | |

ACCOUNT NAME: REVENUES

ACCOUNT No. 400

| Date | Description | PR | Debit | Credit | Balance |
|------|----------------------------|----|-------|---------------|---------------|
| | End of Year Balance | | | 25,000 | 25,000 |
| | | | | | |
| | | | | | |
| | | | | | |
| | | | | | |

Closing Journal Entries

General Journal Example

Post the entry to the Revenue account.

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|--------|--------------------------|-----|--------|--------|
| 31-Dec | Revenues | 400 | 25,000 | |
| | Income Summary | | | 25,000 |
| | <i>to close Revenues</i> | | | |

ACCOUNT NAME: REVENUES

ACCOUNT No. 400

| Date | Description | PR | Debit | Credit | Balance |
|--------|-------------------------|-----|--------|--------|---------|
| | End of Year Balance | | | 25,000 | 25,000 |
| 31-Dec | Close to Income Summary | G97 | 25,000 | | 0 |
| | | | | | |
| | | | | | |
| | | | | | |

Closing Journal Entries

General Journal Example

Also, post to the Income Summary account.

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|--------|--------------------------|-----|--------|--------|
| 31-Dec | Revenues | 400 | 25,000 | |
| | Income Summary | 600 | | 25,000 |
| | <i>to close Revenues</i> | | | |

ACCOUNT NAME: INCOME SUMMARY ACCOUNT No. 600

| Date | Description | PR | Debit | Credit | Balance |
|--------|-------------------|-----|-------|--------|---------|
| 31-Dec | To close Revenues | G97 | | 25,000 | 25,000 |
| | | | | | |
| | | | | | |
| | | | | | |

Closing Journal Entries

General Journal Example

On 12/31/99, Rent Expense was \$8,000 and Salaries Expense was \$15,000. Prepare the closing journal entry.

GENERAL JOURNAL

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|------|-------------|----|-------|--------|
| | | | | |
| | | | | |
| | | | | |
| | | | | |
| | | | | |

Closing Journal Entries

General Journal Example

On 12/31/99, Rent Expense was \$8,000 and Salaries Expense was \$15,000. Prepare the closing journal entry.

GENERAL JOURNAL

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|--------|--------------------------|----|--------|--------|
| 31-Dec | Income Summary | | 23,000 | |
| | Rent Expense | | | 8,000 |
| | Salaries Expense | | | 15,000 |
| | <i>to close expenses</i> | | | |
| | | | | |

Closing Journal Entries

General Journal Example

After posting, the Rent Expense and Salaries Expense accounts have \$0 balances.

ACCOUNT NAME: RENT EXPENSE

ACCOUNT No. 515

| Date | Description | PR | Debit | Credit | Balance |
|--------|----------------|-----|-------|--------|---------|
| 31-Dec | Balance | | 8,000 | | 8,000 |
| 31-Dec | Income Summary | G97 | | 8,000 | 0 |
| | | | | | |

ACCOUNT NAME: SALARIES EXPENSE

ACCOUNT No. 507

| Date | Description | PR | Debit | Credit | Balance |
|--------|----------------|-----|--------|--------|---------|
| 31-Dec | Balance | | 15,000 | | 15,000 |
| 31-Dec | Income Summary | G97 | | 15,000 | 0 |
| | | | | | |

Closing Journal Entries

General Journal Example

After posting, the Income Summary account has a \$2,000 balance that must be closed to Retained Earnings.

ACCOUNT NAME: INCOME SUMMARY ACCOUNT No. 600

| Date | Description | PR | Debit | Credit | Balance |
|--------|-------------------|-----|--------|--------|---------|
| 31-Dec | To close Revenues | G97 | | 25,000 | 25,000 |
| 31-Dec | To close Expenses | G97 | 23,000 | | 2,000 |
| | | | | | |
| | | | | | |

GENERAL JOURNAL

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|------|-------------|----|-------|--------|
| | | | | |
| | | | | |
| | | | | |

Closing Journal Entries

General Journal Example

After posting, the Income Summary account has a \$2,000 balance that must be closed to Retained Earnings.

ACCOUNT NAME: INCOME SUMMARY **ACCOUNT No. 600**

| Date | Description | PR | Debit | Credit | Balance |
|--------|-------------------|-----|--------|--------|---------|
| 31-Dec | To close Revenues | G97 | | 25,000 | 25,000 |
| 31-Dec | To close Expenses | G97 | 23,000 | | 2,000 |
| | | | | | |
| | | | | | |

GENERAL JOURNAL

Page: 97

| Date | Description | PR | Debit | Credit |
|--------|-------------------|-----|-------|--------|
| 31-Dec | Income Summary | 600 | 2,000 | |
| | Retained Earnings | | | 2,000 |
| | | | | |

Closing Journal Entries

General Journal Example

After posting, the Income Summary account has a \$2,000 balance that must be closed to Retained Earnings.

ACCOUNT NAME: INCOME SUMMARY ACCOUNT No. 600

| Date | Description | PR | Debit | Credit | Balance |
|--------|-------------------|-----|--------|--------|---------|
| 31-Dec | To close Revenues | G97 | | 25,000 | 25,000 |
| 31-Dec | To close Expenses | G97 | 23,000 | | 2,000 |
| 31-Dec | To close R/E | G97 | 2,000 | | 0 |

GENERAL JOURNAL

Page: 97

| Date | Description | PR | Debit | Credit |
|--------|-------------------|-----|-------|--------|
| 31-Dec | Income Summary | 600 | 2,000 | |
| | Retained Earnings | | | 2,000 |

Closing Journal Entries

General Journal Example

On 12/31/99, the Dividends account has a \$1,300 balance. Prepare the closing entry.

GENERAL JOURNAL

Page: _____ 97

| Date | Description | PR | Debit | Credit |
|------|-------------|----|-------|--------|
| | | | | |
| | | | | |
| | | | | |
| | | | | |
| | | | | |

Closing Journal Entries

General Journal Example

On 12/31/99, the Dividends account has a \$1,300 balance. Prepare the closing entry.

GENERAL JOURNAL

Page: 97

| Date | Description | PR | Debit | Credit |
|--------|---------------------------|----|-------|--------|
| 31-Dec | Retained Earnings | | 1,300 | |
| | Dividends | | | 1,300 |
| | <i>to close dividends</i> | | | |
| | | | | |
| | | | | |

Closing Journal Entries

General Journal Example

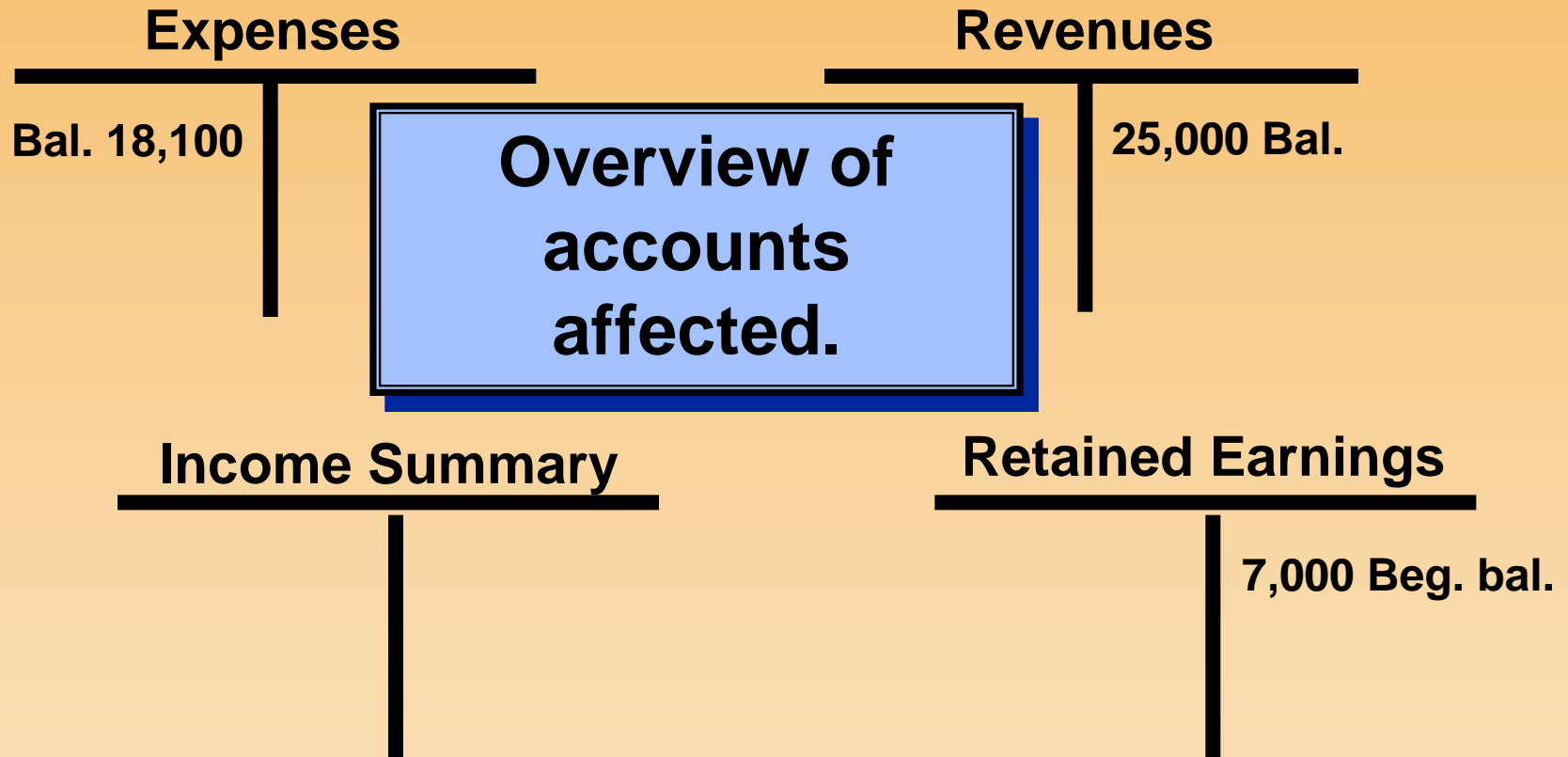
Assuming Retained Earnings had a pre-closing ending balance of \$7,000, ...

ACCOUNT NAME: Retained Earnings **ACCOUNT No. 310**

| Date | Description | PR | Debit | Credit | Balance |
|---------------|--------------------------------|------------|--------------|--------------|--------------|
| 31-Dec | Balance | | | 7,000 | 7,000 |
| 31-Dec | To close Income Summary | G97 | | 2,000 | 9,000 |
| 31-Dec | To close Dividends | G97 | 1,300 | | 7,700 |
| | | | | | |

... after posting the closing of the Income Summary and Dividends accounts, the ending balance is \$7,700.

Closing Journal Entries Once More!



Closing Journal Entries Once More!

Expenses

Bal. 18,100

Revenues

25,000 Bal.

Income Summary

Once more, close out Revenues with a **debit** to Revenues and a **credit** to Income Summary.

Closing Journal Entries Once More!

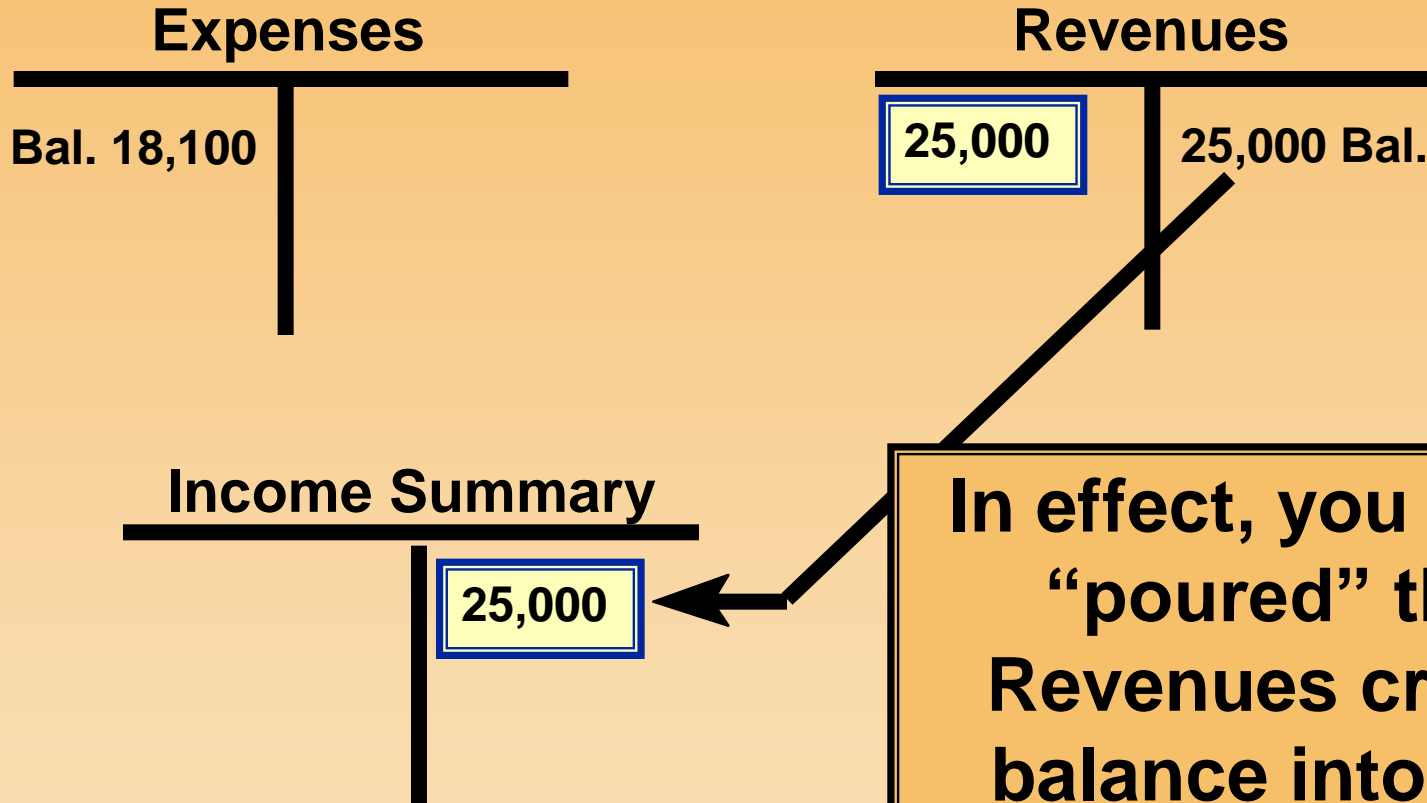
| Expenses | |
|-------------|--|
| Bal. 18,100 | |

| Revenues | |
|----------|-------------|
| 25,000 | 25,000 Bal. |

| Income Summary | |
|----------------|--------|
| | 25,000 |

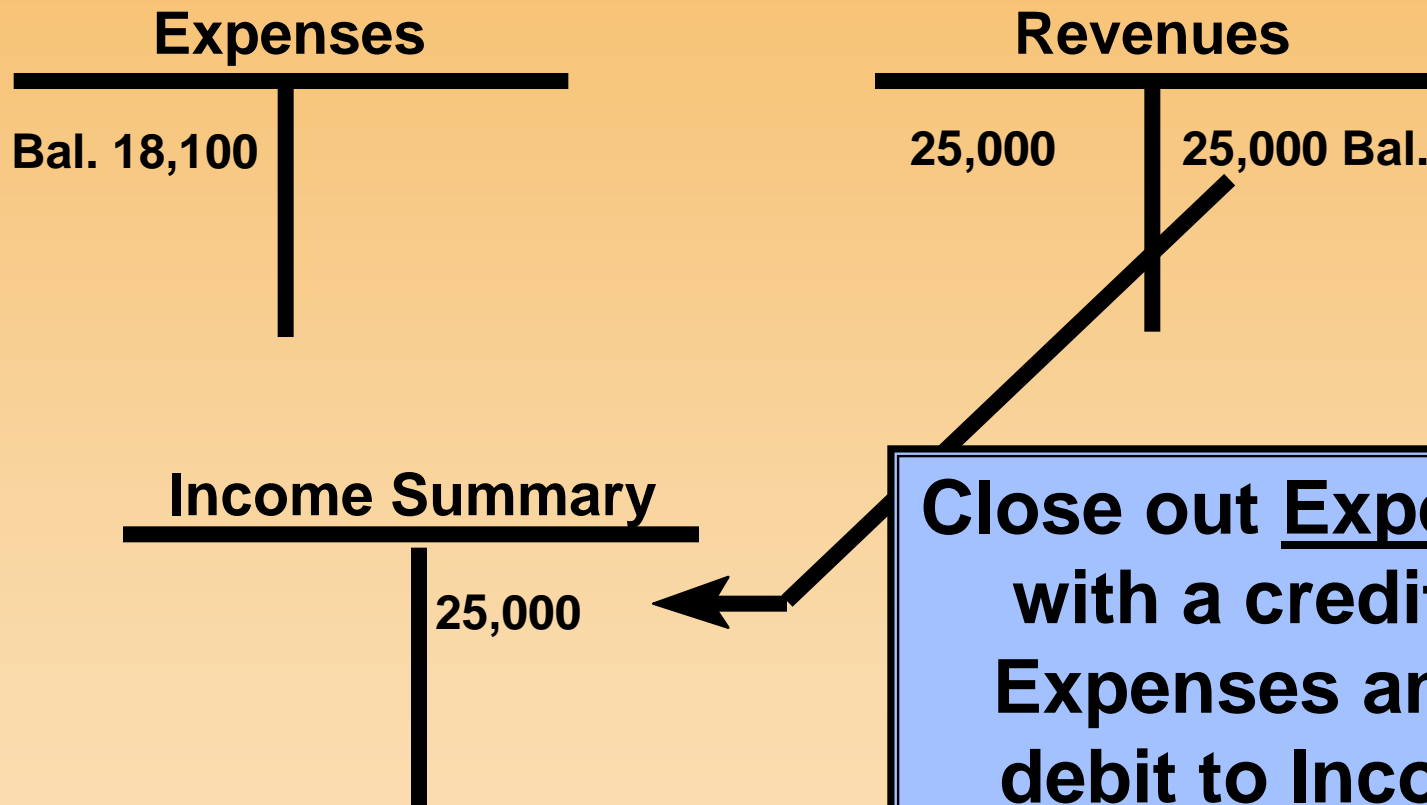
Once more, close out Revenues with a debit to Revenues and a credit to Income Summary.

Closing Journal Entries Once More!

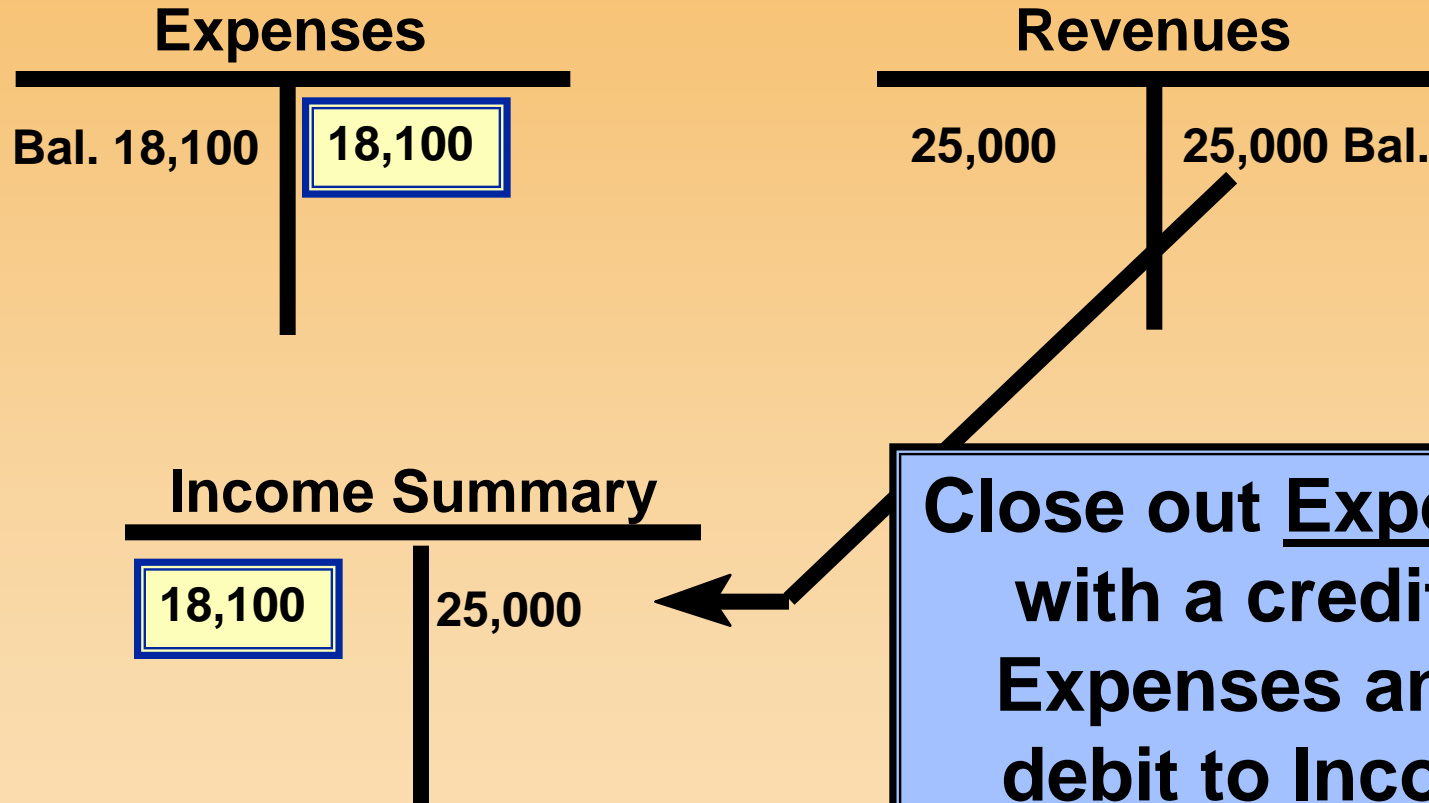


In effect, you have “poured” the Revenues credit balance into the Income Summary.

Closing Journal Entries Once More!

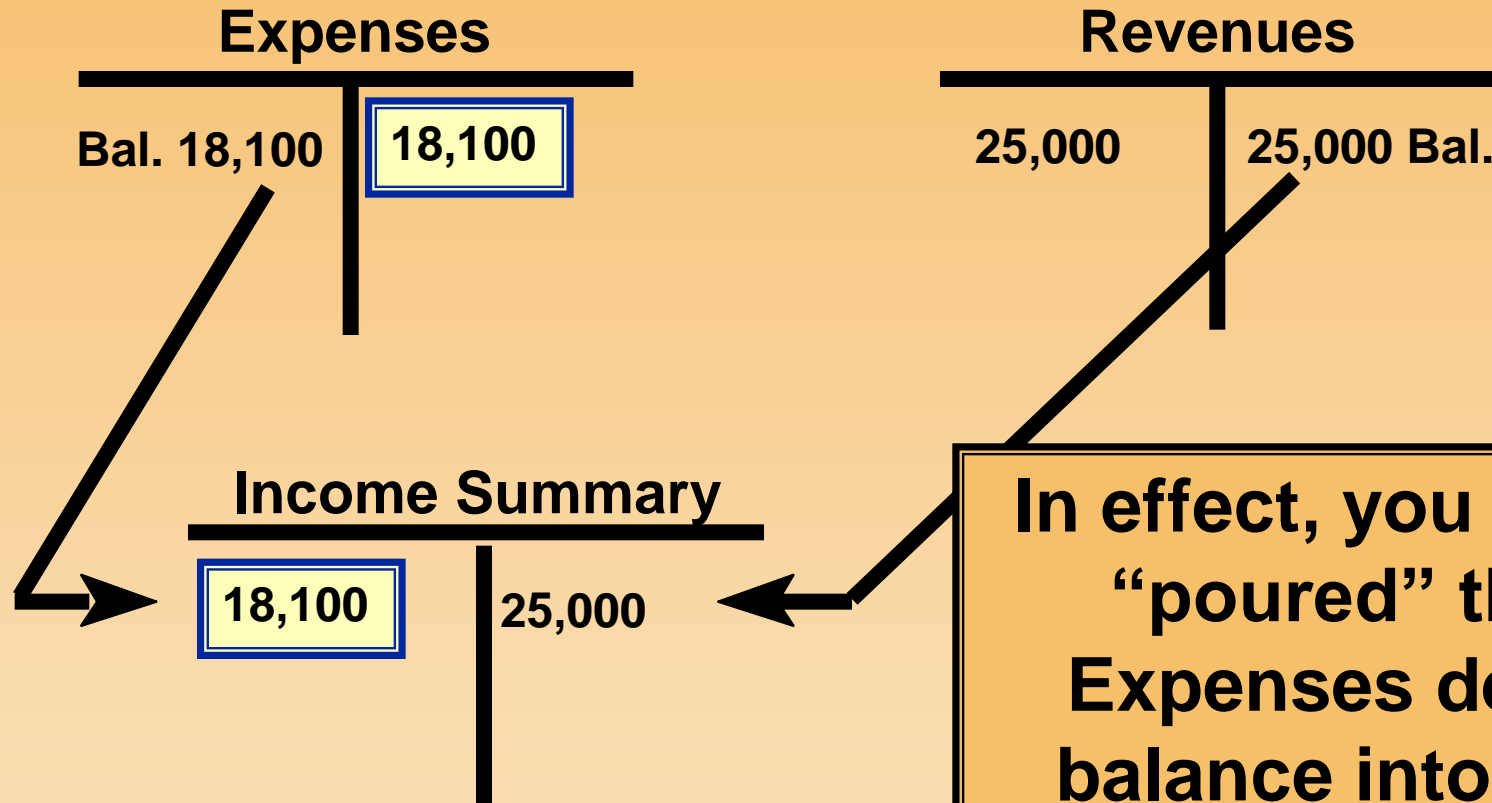


Closing Journal Entries Once More!



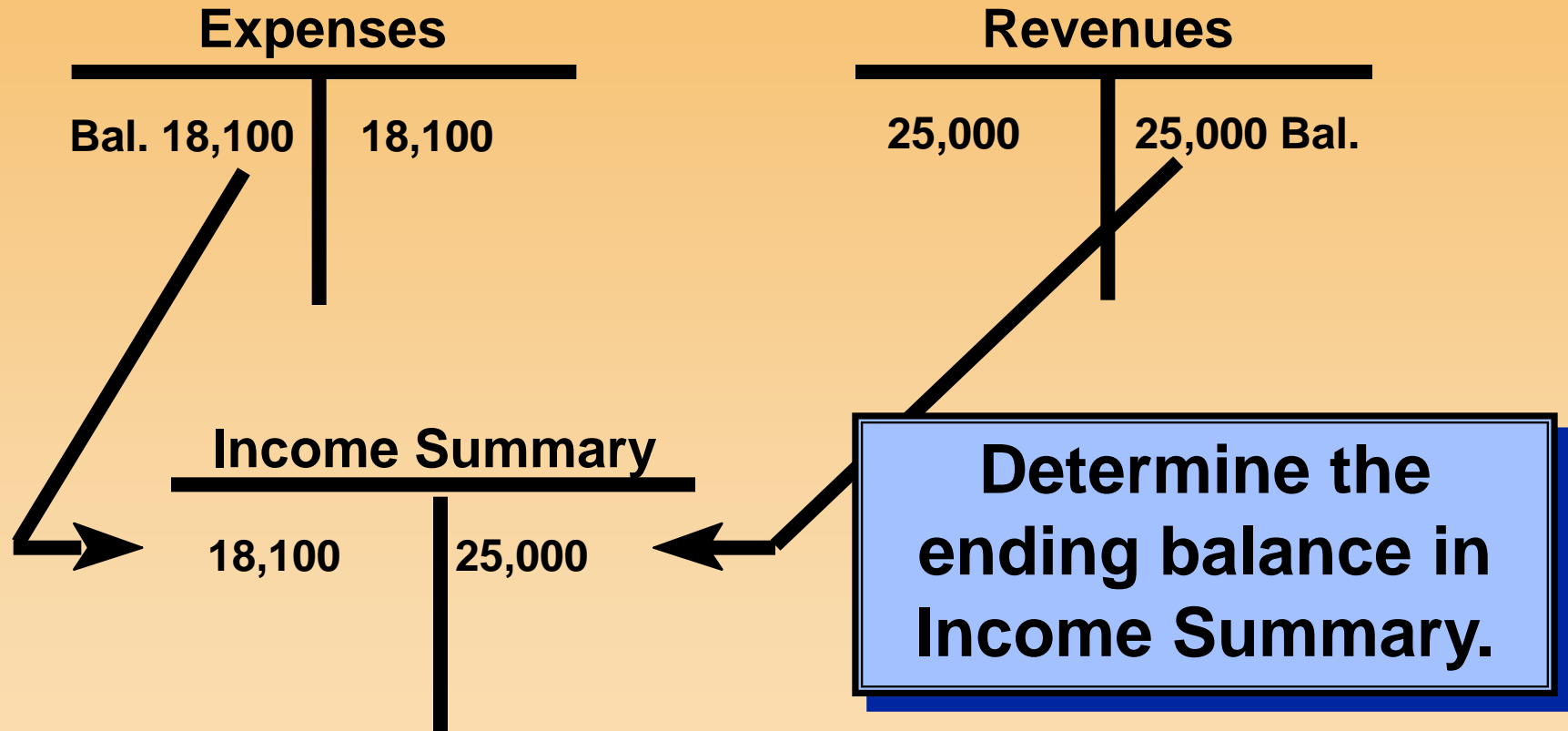
Close out Expenses with a credit to Expenses and a debit to Income Summary.

Closing Journal Entries Once More!

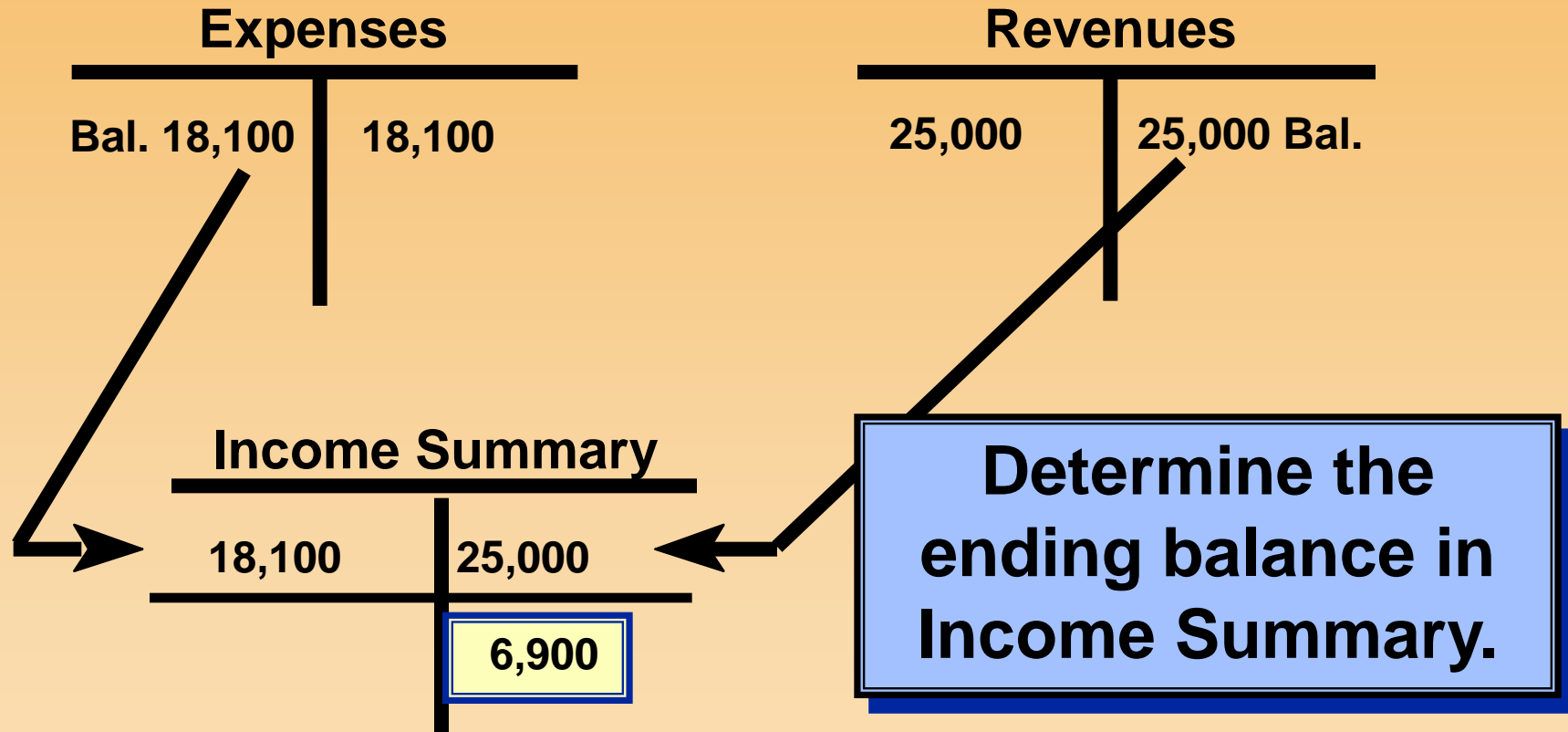


In effect, you have “poured” the Expenses debit balance into the Income Summary.

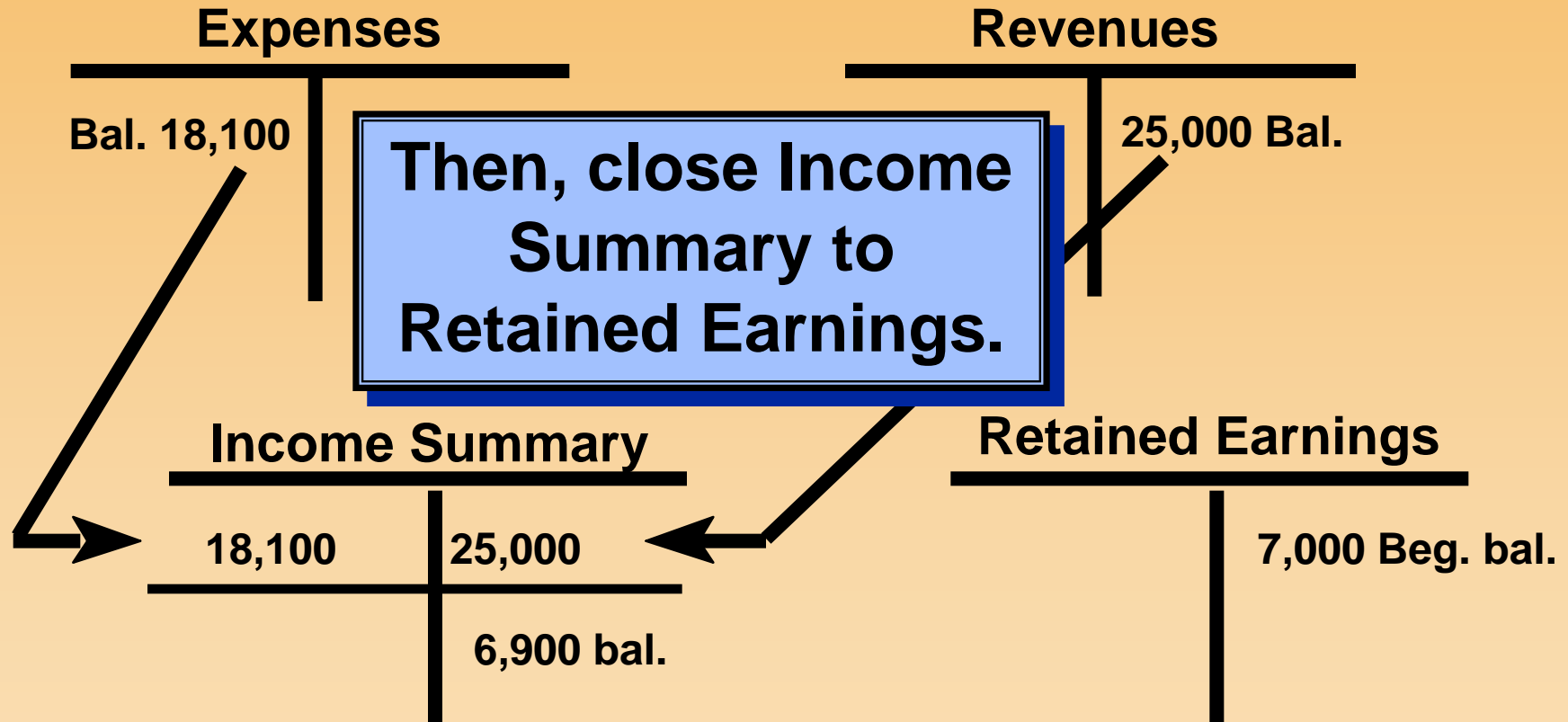
Closing Journal Entries Once More!



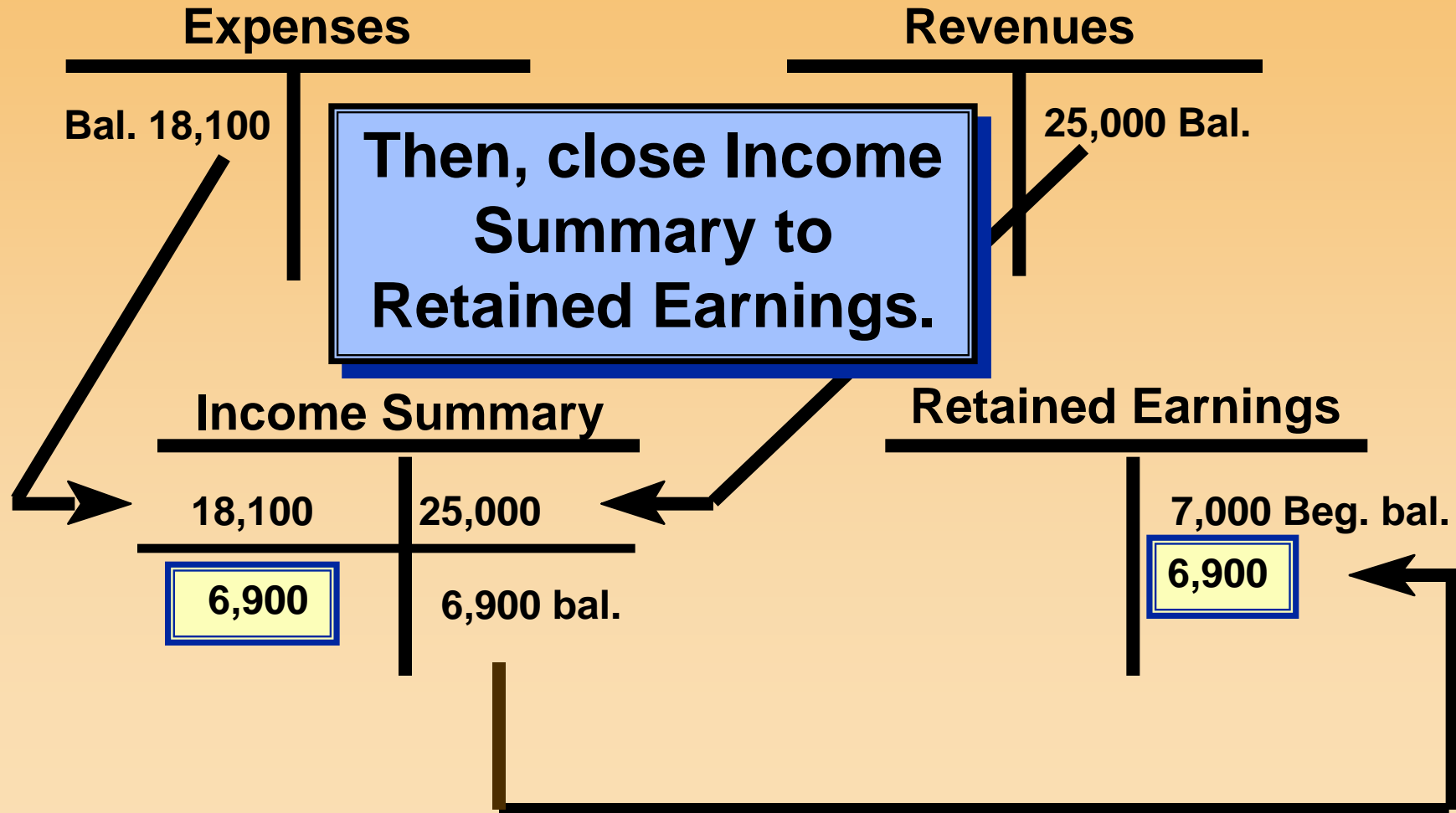
Closing Journal Entries Once More!



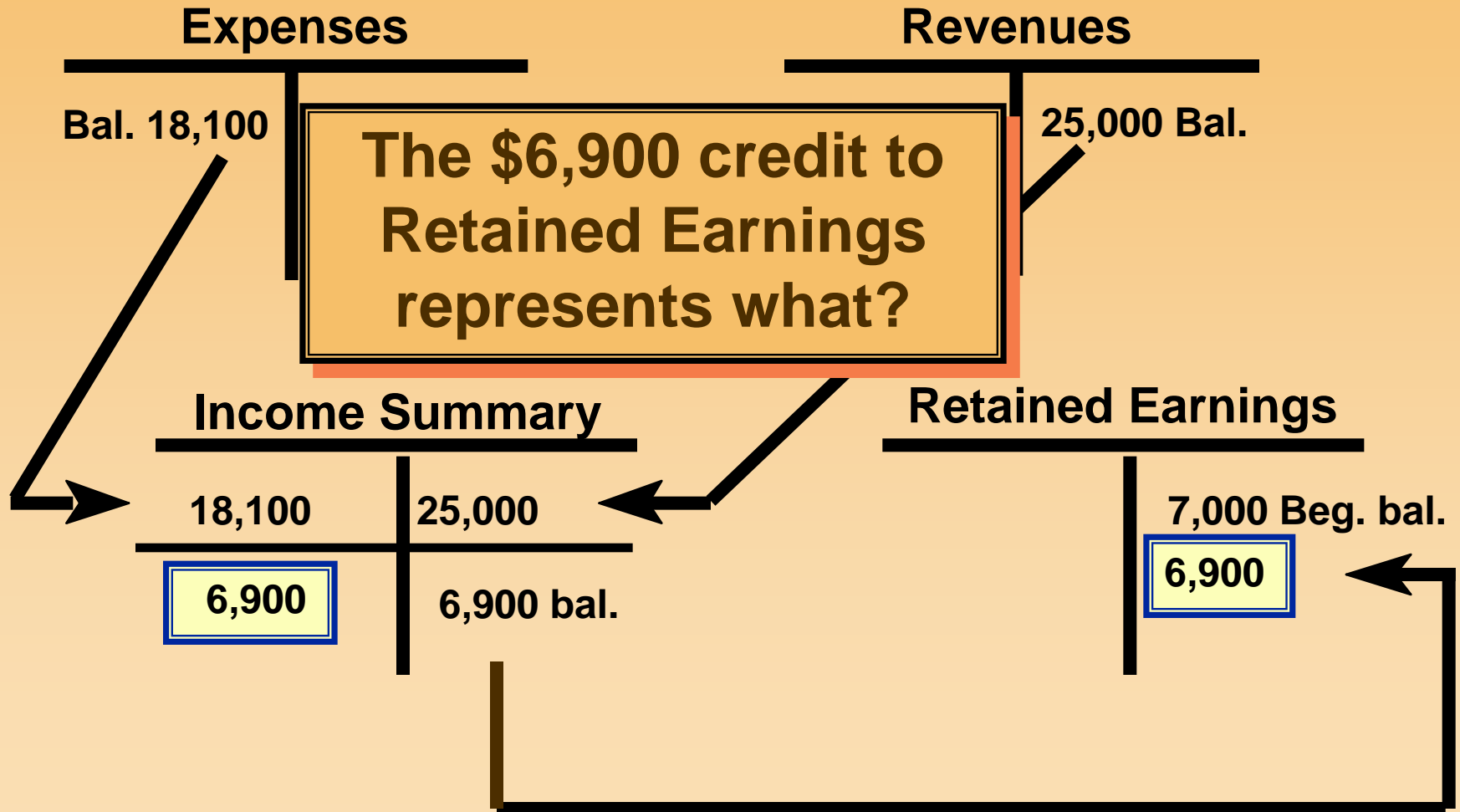
Closing Journal Entries Once More!



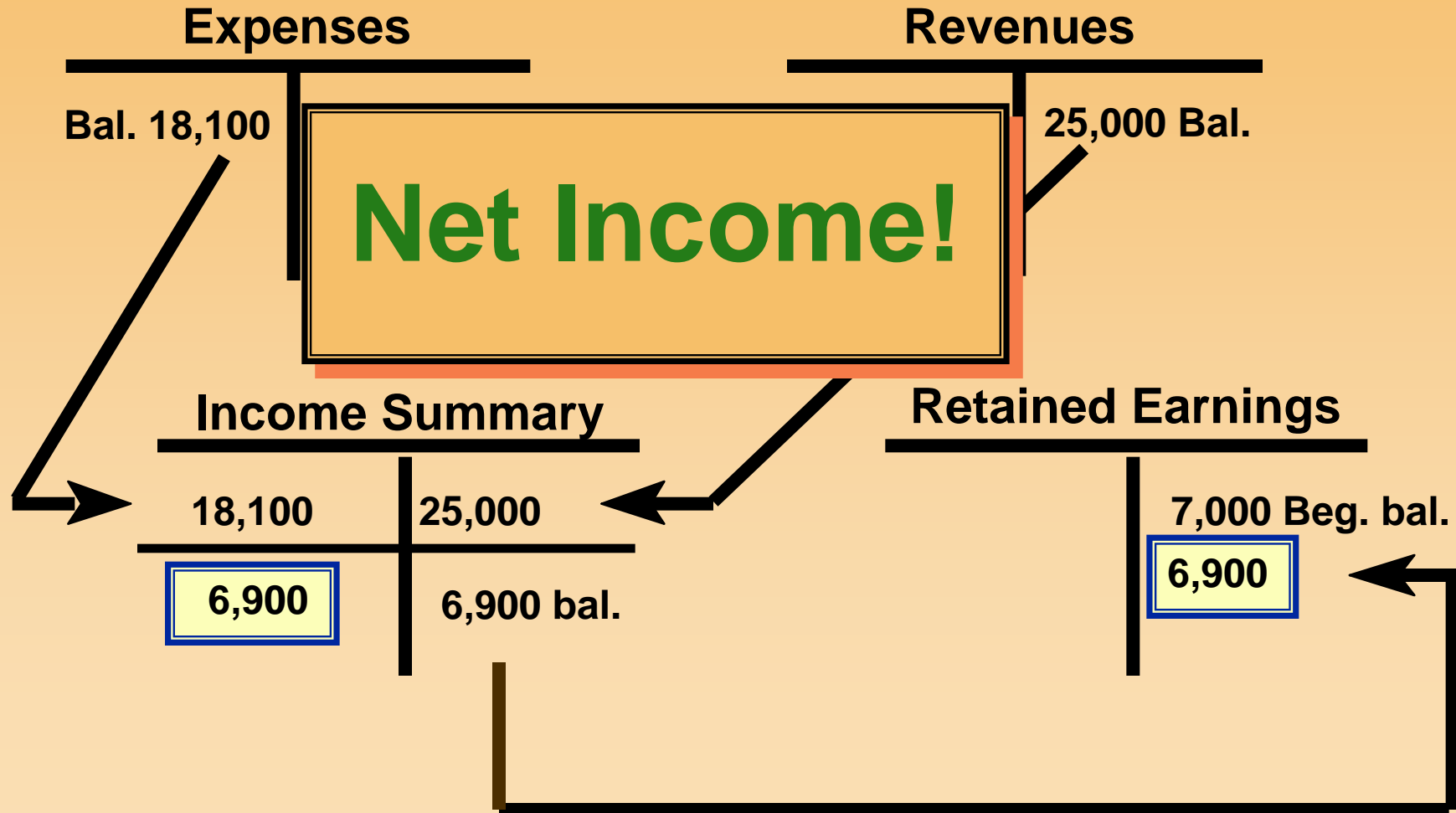
Closing Journal Entries Once More!



Closing Journal Entries Once More!



Closing Journal Entries Once More!



Closing Journal Entries Once More!

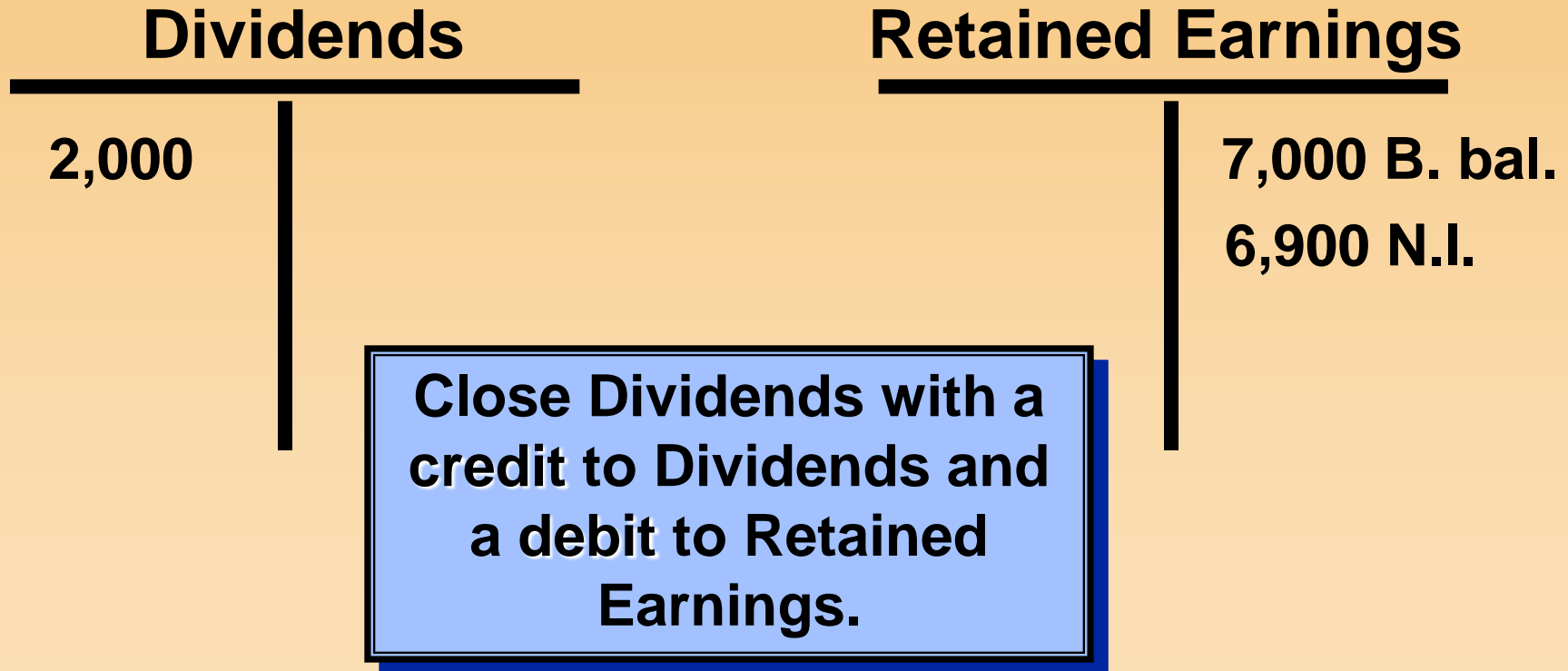
- Dividends must also be closed to Retained Earnings at the end of the year.

| Dividends | |
|------------------|--|
| 2,000 | |

| Retained Earnings | |
|--------------------------|---------------|
| | 7,000 B. bal. |
| | 6,900 N.I. |

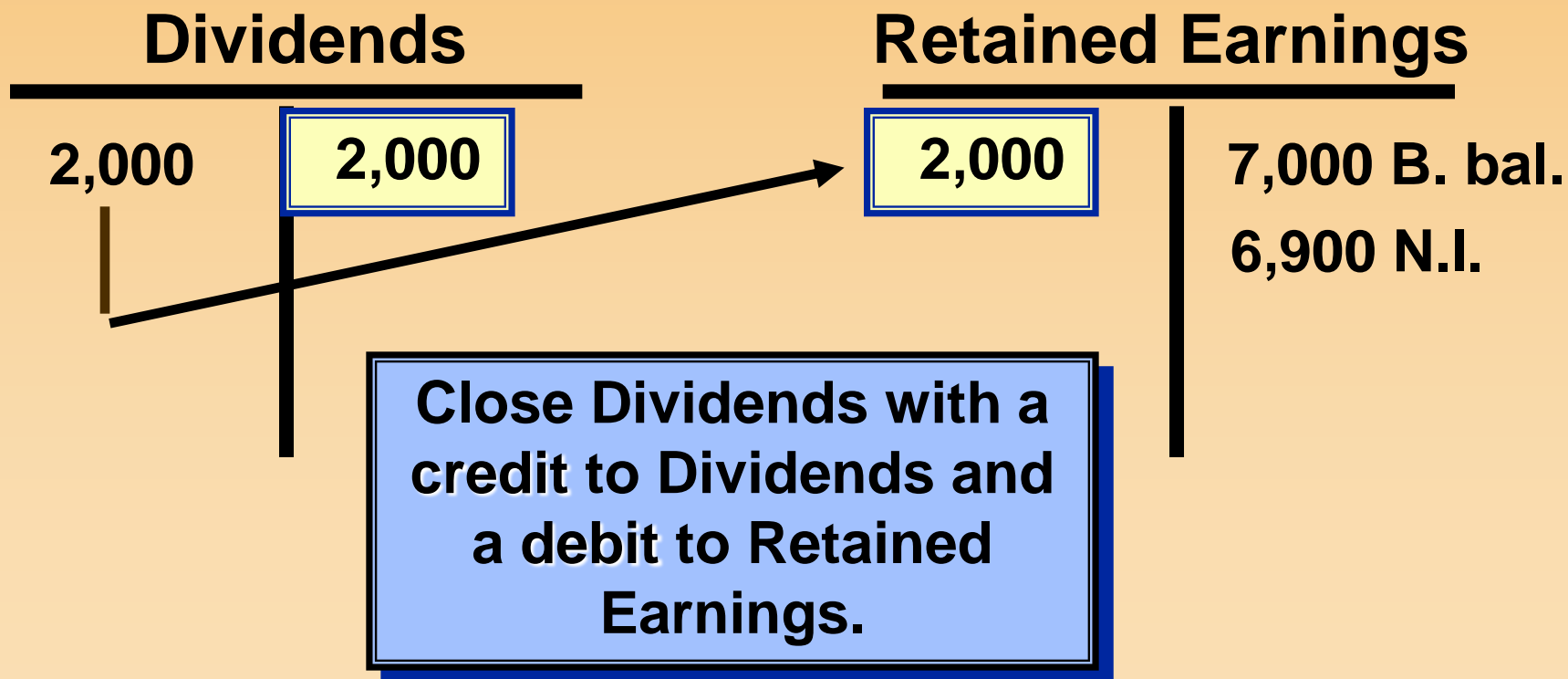
Closing Journal Entries Once More!

- Dividends must also be closed to Retained Earnings at the end of the year.



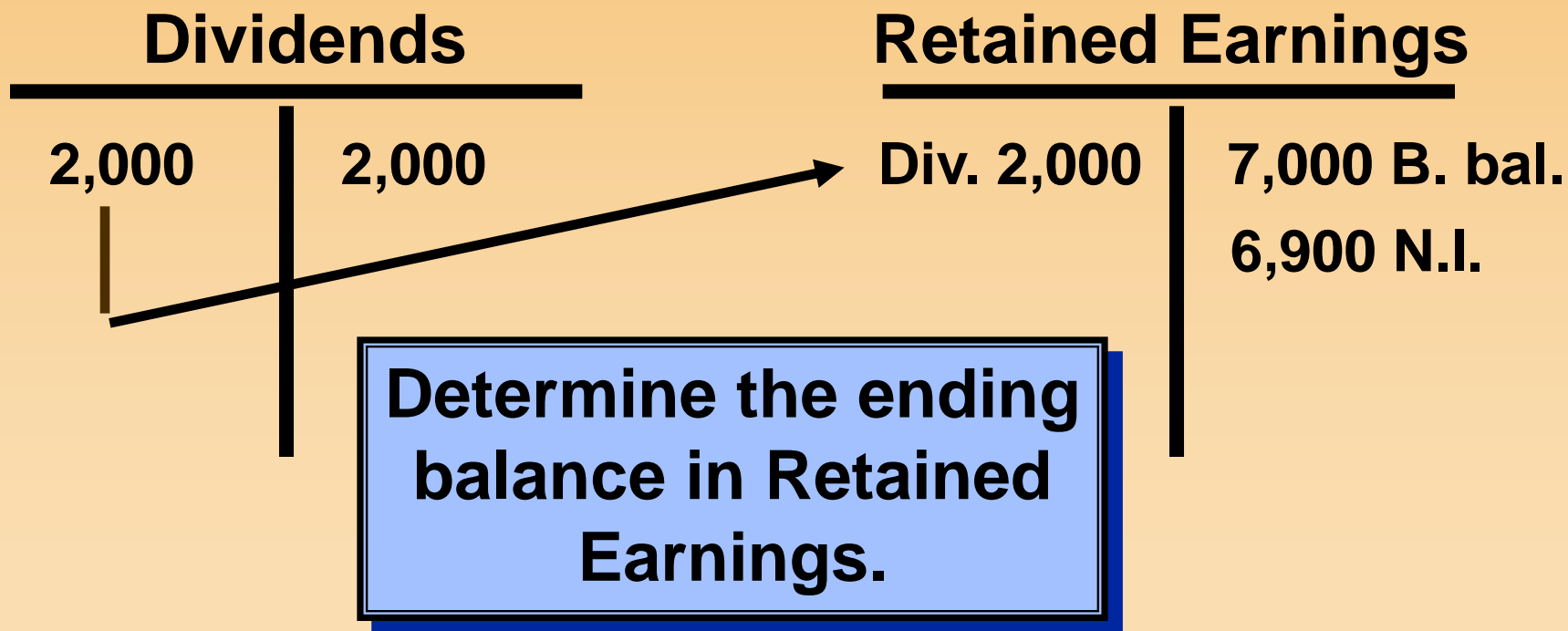
Closing Journal Entries Once More!

- Dividends must also be closed to Retained Earnings at the end of the year.



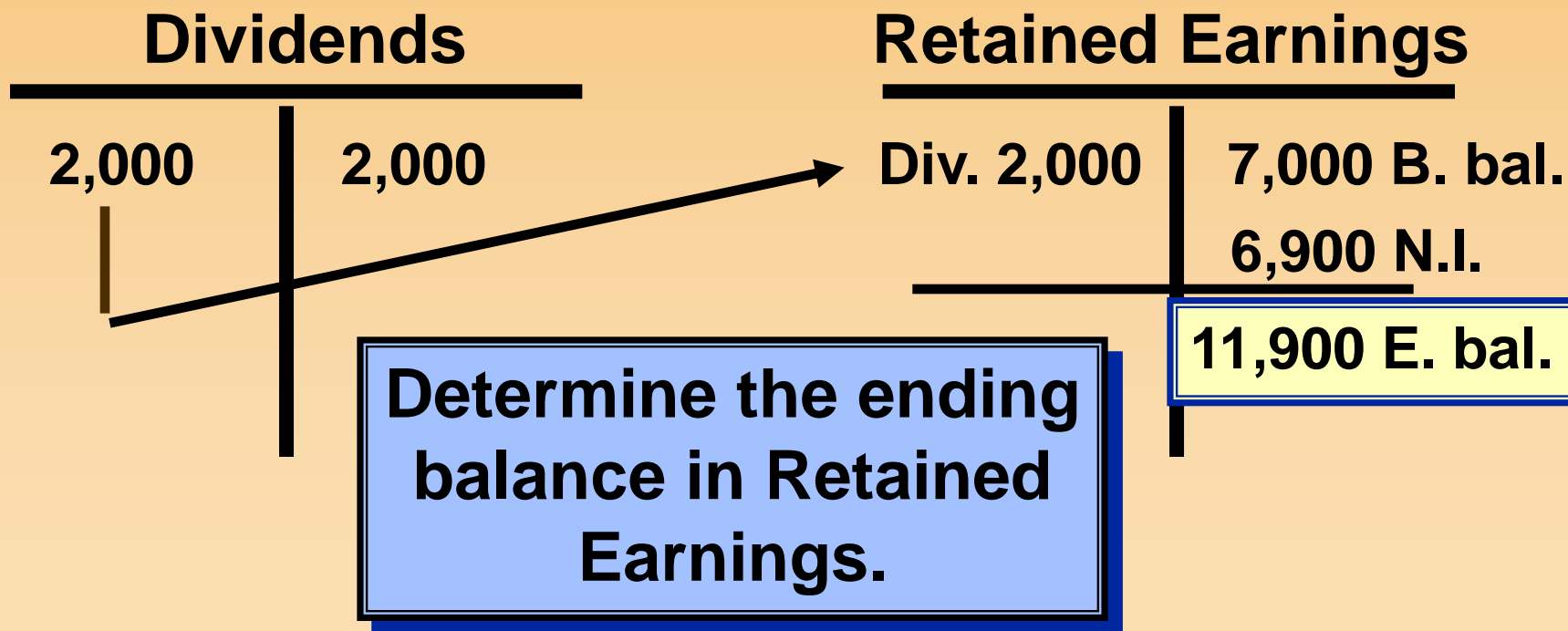
Closing Journal Entries Once More!

- Dividends must also be closed to Retained Earnings at the end of the year.



Closing Journal Entries Once More!

- Dividends must also be closed to Retained Earnings at the end of the year.



**Maybe I'll just do a
little account
closing of my own!**



The Work Sheet

- It is a columnar spreadsheet for summarizing information needed to adjust and close the books.
- It is only an accounting tool and not part of the formal accounting records.
- When completed, information for preparing financial statements can be taken directly from the Work Sheet.

The Work Sheet

The work sheet format is illustrated below:

| COMPANY NAME | | | | | | |
|--------------------------------------|---------------|--------|-------------|--------|--------------|--------|
| Work Sheet | | | | | | |
| For the Year Ended December 31, 1999 | | | | | | |
| Account Title | Trial Balance | | Adjustments | | Adjusted T/B | |
| | Debit | Credit | Debit | Credit | Debit | Credit |
| | | | | | | |
| | | | | | | |
| | | | | | | |
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| | | | | | | |

The information in these columns comes from the general ledger.

The Work Sheet

The work sheet format is illustrated below:

| COMPANY NAME | | |
|---------------|--------------|--------|
| Work Sheet | | |
| Account Title | Adjusted T/B | |
| | Debit | Credit |
| | | |
| | | |
| | | |
| | | |
| | | |
| | | |
| | | |
| | | |
| | | |
| | | |
| | | |

This information is determined mathematically from the previous two sets of columns.

The Work Sheet

There are three additional sets of columns that are normally present on the work sheet for a corporation.

| COMPANY NAME | | | | |
|------------------------|--------|-------------|--------|--|
| Work Sheet | | | | |
| For the Year Ended Dec | | | | |
| Adjusted T/B | | Income Stmt | | |
| Debit | Credit | Debit | Credit | |
| | | | | |
| | | | | |
| | | | | |
| | | | | |
| | | | | |
| | | | | |
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The Income Statement columns are used to facilitate preparation of the formal Income Statement.

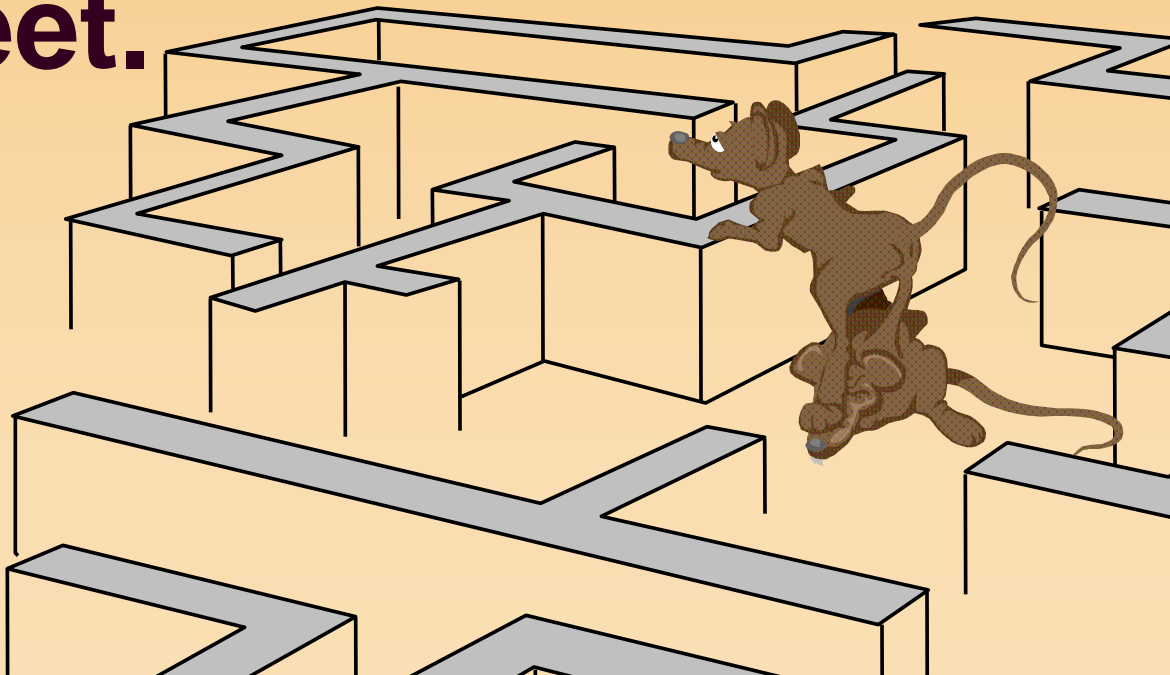
The Work Sheet

There are three additional sets of columns that are normally present on the work sheet for a corporation.

| Adjusted T/B | | | Balance Sheet | |
|--------------|--------|--|---------------|--------|
| Debit | Credit | | Debit | Credit |
| | | | | |
| | | | | |
| | | | | |
| | | | | |
| | | | | |
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Are work sheets used when accounting is computerized?

**Let's move on
to a discussion
of the Classified
Balance Sheet.**



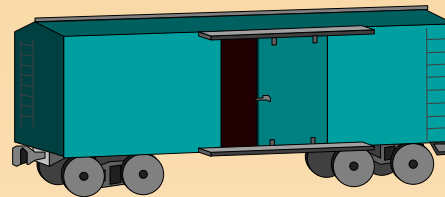
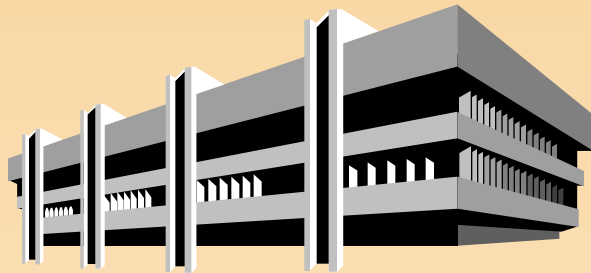
Classified Balance Sheet

- **Contains the same three major categories as before:**
 - ◆ **Assets**
 - ◆ **Liabilities**
 - ◆ **Stockholders' Equity**
- **However, the major categories are subdivided to provide more useful information.**

Classified Balance Sheet

Subdivisions of Assets

- Current Assets
- Property, Plant, and Equipment
- Long-Term Investments
- Intangibles





Classified Balance Sheet

Current Assets

Cash and other assets that a business can convert to cash or use up within one year (or one operating cycle, whichever is longer).

Short-term
Investment

Cash

Accounts
Receivable

Examples ?

Shown in what order on the
Balance Sheet?

Classified Balance Sheet

Property, Plant & Equipment

Assets with useful lives of more than one year acquired for use in the business rather than for resale.

Alternative, informal term used for Property, Plant & Equipment?

Examples 2 and

Natural
Resources

“Fixed Assets”

Equipment

Buildings

Classified Balance Sheet Long-Term Investments

Consists of securities of another company held with the intention of holding the securities for more than one year.

Classified Balance Sheet

Intangible Assets

Rights or economic benefits that are not physical in nature.

Patents

Goodwill

Examples ?

emarks

Classified Balance Sheet

Assets Section Example

ASSETS



Similar p.149

Current Assets

| | |
|---------------------------|------------|
| Cash | \$ 75,000 |
| Accounts Receivable (net) | 100,000 |
| Merchandise Inventories | 80,000 |
| | <hr/> |
| Total Current Assets | \$ 255,000 |

Property and Equipment

| | |
|--------------------------------|------------|
| Land | \$ 200,000 |
| Buildings | 300,000 |
| Less: Accumulated Depreciation | (150,000) |
| | <hr/> |

| | |
|----------------------------|------------|
| Net Property and Equipment | \$ 350,000 |
|----------------------------|------------|

Investment in Other Company

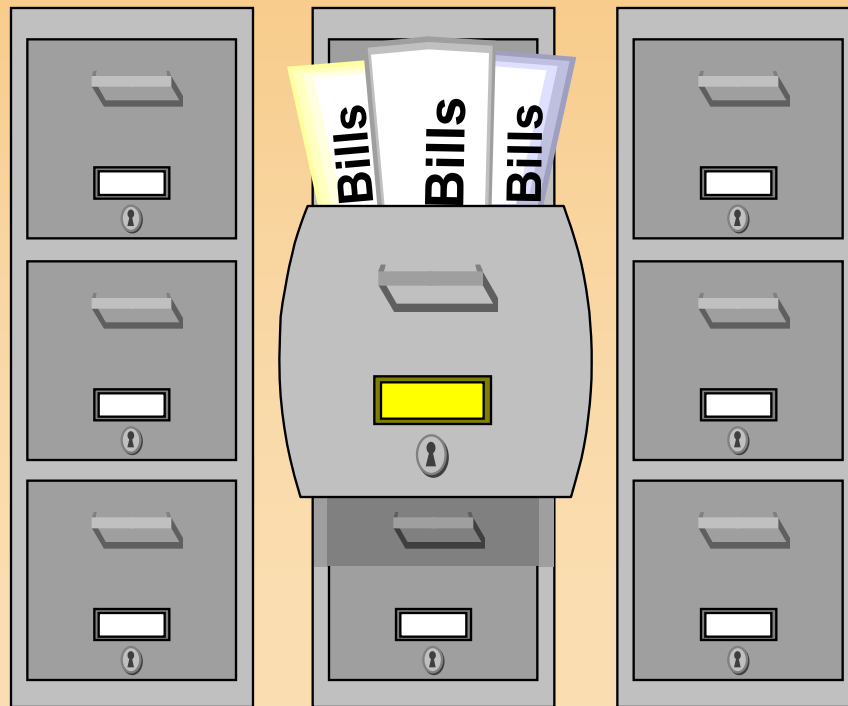
| | |
|---------|---------|
| Patents | 250,000 |
| | <hr/> |
| | 10,000 |

| | |
|--------------|------------------------|
| Total Assets | <hr/> <hr/> \$ 865,000 |
|--------------|------------------------|

Classified Balance Sheet

Liabilities

- Current Liabilities
- Long-Term Liabilities





Classified Balance Sheet

Current Liabilities

Debts due within one year (or one operating cycle, whichever is longer).

Usually paid with current assets.

**Accounts
Payable**

**Wages
Payable**

**Taxes
Payable**

**Shown in what order on the
Balance Sheet? (p. 152)**

**Notes
Payable**

Revenues

Classified Balance Sheet

Long-Term Liabilities

Debts that are due more than one year after the Balance Sheet date.

Due dates should appear on the Balance Sheet.

Mortgage
Payable

Examples ?

Bonds
Payable

Long-term
Notes
Payable

Classified Balance Sheet

Liabilities Section Example



Similar p.149

LIABILITIES

Current Liabilities

| | |
|----------------------------------|-------------------|
| Accounts Payable | \$ 125,000 |
| Unearned Revenues | 1,000 |
| Wages Payable | 10,000 |
| Total Current Liabilities | \$ 136,000 |

Long-Term Liabilities

| | |
|------------------------------------|-------------------|
| Notes Payable (Due 12/31/99) | \$ 90,000 |
| Bonds Payable (Due 12/31/2021) | 200,000 |
| Total Long-Term Liabilities | \$ 290,000 |

| | |
|--------------------------|-------------------|
| Total Liabilities | \$ 426,000 |
|--------------------------|-------------------|

Classified Balance Sheet

Stockholders' Equity

- **Paid-In Capital**

- ◆ Amounts paid into the company by the owners as investments.
- ◆ Includes: Common Stock and Preferred Stock.



- **Retained Earnings**

- ◆ The cumulative income of the company since its inception less the amounts distributed to the owners in the form of dividends since its inception.

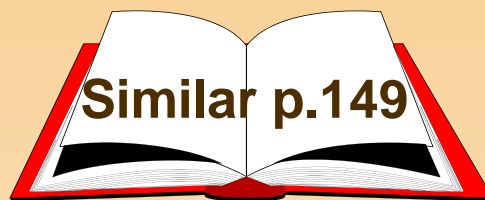


Classified Balance Sheet

Stockholders' Equity Section Example

STOCKHOLDERS' EQUITY

| | | |
|----------------------------|----|---------|
| Common Stock | \$ | 300,000 |
| Additional Paid-In Capital | | 95,000 |
| Retained Earnings | | 44,000 |
| Total Stockholders' Equity | \$ | 439,000 |



Classified Balance Sheet

Stockholders' Equity Section Example

| STOCKHOLDERS' EQUITY | |
|----------------------------|-------------------|
| Common Stock | \$ 300,000 |
| Additional Paid-In Capital | 95,000 |
| Retained Earnings | 44,000 |
| Total Stockholders' Equity | <u>\$ 439,000</u> |



$$A = L + SE$$

$$865,000 = 426,000 + 439,000$$

The End