

CHAPTER 4
COMPLETING THE ACCOUNTING CYCLE

Objectives: After studying this chapter you should be able to:

- . Prepare a worksheet
- . Explain the process of closing the books
- . Preparing Correction entries

I. Worksheet

To prepare accounting information and reports, accountants use a spreadsheet called work sheet. Accounting worksheets are most often used in the accounting cycle process to show an unadjusted **trial balance**, adjusting journal entries, adjusted **trial balance**, and financial statements.

It is an optional tool.

Work sheet format

	1 Trial Balance		2 Adjustments		3 Adjusted trial balance		4 Income statement		5 Statement of financial position	
Account title	Dr	Cr	Dr	Cr	Dr	Cr	Dr	Cr	Dr	Cr

1. Prepare a trial balance on the work sheet

2. Enter adjustment data

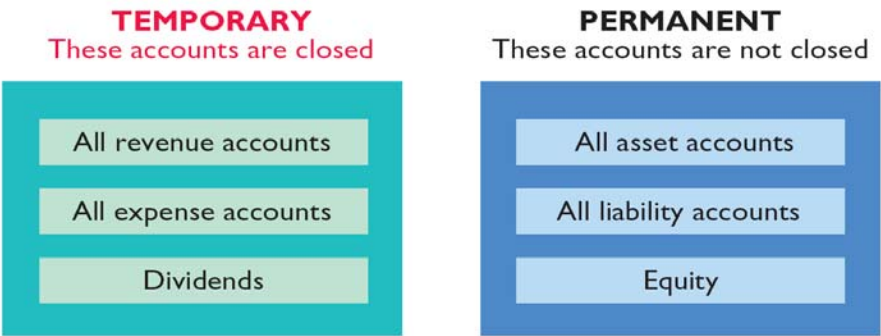
3. Enter adjusted balances

4. Extend adjusted balances to proper statement columns

5. Total the statement columns
Compute net income (or net loss), and complete work sheet

II. Closing entries

- At the end of the accounting period, the company makes the accounts ready for the next period.
- Entries made at the end of an accounting period to transfer the balances of temporary accounts, i.e., revenues, expenses and dividend, to a permanent equity, Retained Earnings account.
- Companies’ closes to **Income Summary** (*a temporary account used for closing revenues and expenses*) all accounts that affect net income. In journalizing, the company credits all temporary accounts with debit balances, and debits all temporary accounts with credit balances.



- **Closing entries** formally recognize, in the general ledger, the transfer of net income (or net loss) and dividends to **Retained Earnings**.

Closing Journal entries			
<div> <div>▪ <u>Close revenue accounts</u></div> <div> <div>Dr. Revenues xxx</div> <div>Cr. Income summary..... xxx</div> </div> </div>			
<div> <div>▪ <u>Close expense Accounts</u></div> <div> <div>Dr Income summary..... xxx</div> <div>Cr. Expenses..... xxx</div> </div> </div>			
<div> <div>▪ <u>Close Income summary account to retained earnings (net income)</u></div> <div> <div>Dr Income summary..... xxx</div> <div>Cr. Retained earnings..... xxx</div> </div> </div>			
<div> <div>▪ <u>Close Income Summary account to retained earnings (net loss)</u></div> <div> <div>Dr Retained earnings..... xxx</div> <div>Cr. Income summary..... xxx</div> </div> </div>			
<div> <div>▪ <u>Close Dividend account</u></div> <div> <div>Dr Retained earnings..... xxx</div> <div>Cr. Dividend..... xxx</div> </div> <div> <div>Note: Dividends are closed directly to Retained Earnings and <i>not</i> to Income Summary because Dividends are not an expense.</div> </div> </div>			

EXAMPLE OF CLOSING ENTRIES FOR SERVICE TYPE BUSINESS:

<u>Close Income statement accounts with credit balance (Revenues):</u>			
Dec. 31:	Service Revenue	200,000	
	Income Summary		200,000
<u>Close Income statement accounts with debit balance (Expenses):</u>			
	Income Summary	30,000	
	Salaries Expense		8,000
	Utilities Expense		900
	Repair Expense		1,900
	Gas &Oil Expense		7,200
	Insurance Expense		3,500
	Depreciation Expense-Building		6,000
	Depreciation Expense-Equipment		2,000
	Interest Expense		500

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<u>Close Income Summary account (Net Income)</u>		
Income Summary	170,000	
Retained earnings		170,000
<u>Close Dividends:</u>		
Retained earnings	1,000	
Dividends		1,000

III. Correction Entries

The accountants will prepare correcting entries when they find errors in their recordings. Since recordings have already been posted to the accounts, they cannot be corrected by using eraser or liquid paper. In accounting, errors cannot be corrected without clue or evidence. So, we have to prepare correcting entries to correct our errors.

Example 1: Purchase of supplies on account 490 Baht has been recorded as debit Supplies 490 Baht and credit Cash 490 Baht

Wrong entry			Correct entry			Correction entry		
Supplies	490		Supplies	490		Cash	490	
Cash		490	Accounts payable		490	Accounts Payable		490

Example 2: Purchase of supplies on account 490 Baht has been recorded as debit Supplies 390 Baht, and credit Accounts Payable 390 Baht.

Wrong entry			Correct entry			Correction entry		
Supplies	390		Supplies	490		Supplies	100	
Accounts payable		390	Accounts payable		490	Accounts Payable		100

Example 3: Purchase of supplies on account, 490 Baht, has been recorded as debit Equipment 490 Baht and credit Accounts Payable 490 Baht.

Wrong entry			Correct entry			Correction entry		
Equipment	490		Supplies	490		Supplies	490	
Accounts payable		490	Accounts payable		490	Equipment		490

Example 4: Purchase of supplies on account 490 Baht has been recorded as debit Equipment 390 Baht and credit Accounts Payable 390.

Wrong entry			Correct entry			Correction entry		
Equipment	390		Supplies	490		Supplies	490	
Accounts payable		390	Accounts payable		490	Equipment		390
						Accounts Payable		100

Problems

Problem 4-1:

- 1. A collection of \$ 1,000 from a client on account was debited to Cash \$700 and credited to Service Revenue \$700. Record the correction entry.
- 2. A payment of \$3,000 cash dividend was debited to Salaries and Wages Expense \$3,000 and credited to Cash \$3,000. Record the correction entry.
- 3. A collection of \$1,000 from a client (Mr.Chen) on account was debited to cash and credited to accounts receivable \$2,000. Prepare the correcting entry.
- 4. Discovered an error in recording of payment of utility expense. Payment of \$107 was recorded as \$170. Record correction entry.
- 5. Collection of cash \$4,500 from a credit customer was mistakenly credited to accounts payable account. Record correction entry.
- 6. A payment of Salaries and Wages Expense of \$1,200 was debited to Utilities Expense and credited to Cash both for \$1,200. Record the correction entry.
- 7. The purchase of equipment on account for \$760 was debited to Equipment \$670 and credited to Accounts Payable \$670

1.		
2.		
3.		
4.		
5.		
6.		
7.		

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Problem 4-2:

Herald Agency began operations as a private investigator on January 1, 2019. The trial balance columns of the worksheet for Herald Agency at March 31 are as follows.

Herald Agency, P.I., Inc.
Worksheet
For the Quarter Ended March 31, 2019
Trial Balance

<u>Account Titles</u>	<u>Dr.</u>	<u>Cr.</u>
Cash	\$11,410	
Accounts Receivable	5,920	
Supplies	1,250	
Prepaid Insurance	2,400	
Equipment	30,000	
Notes Payable		\$10,000
Accounts Payable		12,350
Share Capital – Ordinary		20,000
Dividends	600	
Service Revenue		14,200
Salaries and Wages Expense	2,240	
Travel Expense	1,300	
Rent Expense	1,200	
Miscellaneous Expense	<u>230</u>	
	<u>\$56,550</u>	<u>\$56,550</u>

Other data:

1. Supplies on hand total \$480.
2. Depreciation is \$720 per quarter.
3. Interest accrued on 6-month note payable, issued January 1, \$300.
4. Insurance expires at the rate of \$200 per month.
5. Service provided but unbilled at March 31 total \$1,080.


Instructions:

- (a) Partial worksheet is given below. Complete the worksheet.
- (b) Prepare an income statement and a retained earnings statement for the quarter and a classified statement of financial position at March 31.
- (c) Journalize the adjusting entries from the adjustments columns of the worksheet.
- (d) Journalize the closing entries from the financial statement columns of the worksheet.

Herald Agency, P.I., INC.
Worksheet
For the Quarter Ended March 31, 2019

(a)

Account titles	Unadjusted Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	\$11,410									
Accounts Receivable	5,920									
Supplies	1,250									
Prepaid Insurance	2,400									
Equipment	30,000									
Notes Payable		\$10,000								
Accounts Payable		12,350								
Share Capital—Ordinary		20,000								
Dividends	600									
Service Revenue		14,200								
Salaries and Wages Expense	2,240									
Travel Expense	1,300									
Rent Expense	1,200									
Miscellaneous Expense	230									
Totals	<u>\$56,550</u>	<u>\$56,550</u>								

b) Income statement

Retained earnings statement

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Statement of Financial Position

c) Adjusting entries

Date	Account title	Debit	Credit

d) Closing entries

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Problem 4-3: The trial balance columns of the worksheet for Nerolax Roofing at March 31, 2019, are as follows.

**Nerolax Roofing
Trial Balance
For the Month Ended March 31, 2019**

<u>Account Titles</u>	<u>Dr.</u>	<u>Cr.</u>
Cash	\$2,720	
Accounts Receivable	2,700	
Supplies	1,500	
Equipment	11,000	
Accumulated Depreciation – Equipment		\$1,250
Accounts Payable		2,500
Unearned Service Revenue		550
Share Capital – Ordinary		10,000
Dividends	1,100	
Service Revenue		6,300
Salaries and Wages Expense	1,300	
Miscellaneous Expense	<u>280</u>	
	<u>\$20,600</u>	<u>\$20,600</u>

Other data:

1. A physical count reveals only \$550 of roofing supplies on hand.
2. Depreciation for March is \$250.
3. Unearned revenue amounted to \$290 at March 31.
4. Accrued salaries are \$480.

Instructions:

- (a) Partial worksheet is given below. Complete the worksheet.
- (b) Prepare an income statement and a retained earnings statement for the month of March and a classified statement of Financial Position at March 31.
- (c) Journalize the adjusting entries from the adjustment columns of the worksheet.
- (d) Journalize the closing entries from the financial statement columns of the worksheet

Nerolax Roofing
Work Sheet
For the month ended March 31, 2019

(a)


Account titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Statement of Financial Position	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	\$2,720									
Accounts Receivable	2,700									
Supplies	1,500									
Equipment	11,000									
Acc. Depreciation-Equipment		\$1,250								
Accounts Payable		2,500								
Unearned Service Revenue		550								
Share Capital - Ordinary		10,000								
Dividends	1,100									
Service Revenue		6,300								
Salaries and Wages Expense	1,300									
Miscellaneous Expense	280									
Totals	\$20,600	\$20,600								

b) Income statement

Retained earnings statement

[illegible]

Statement of Financial Position



c) Adjusting entries

Date	Account title	Debit	Credit

d) Closing entries
