

INFO 7225

Module 1

5. Cash-basis vs. Accrual-basis Accounting

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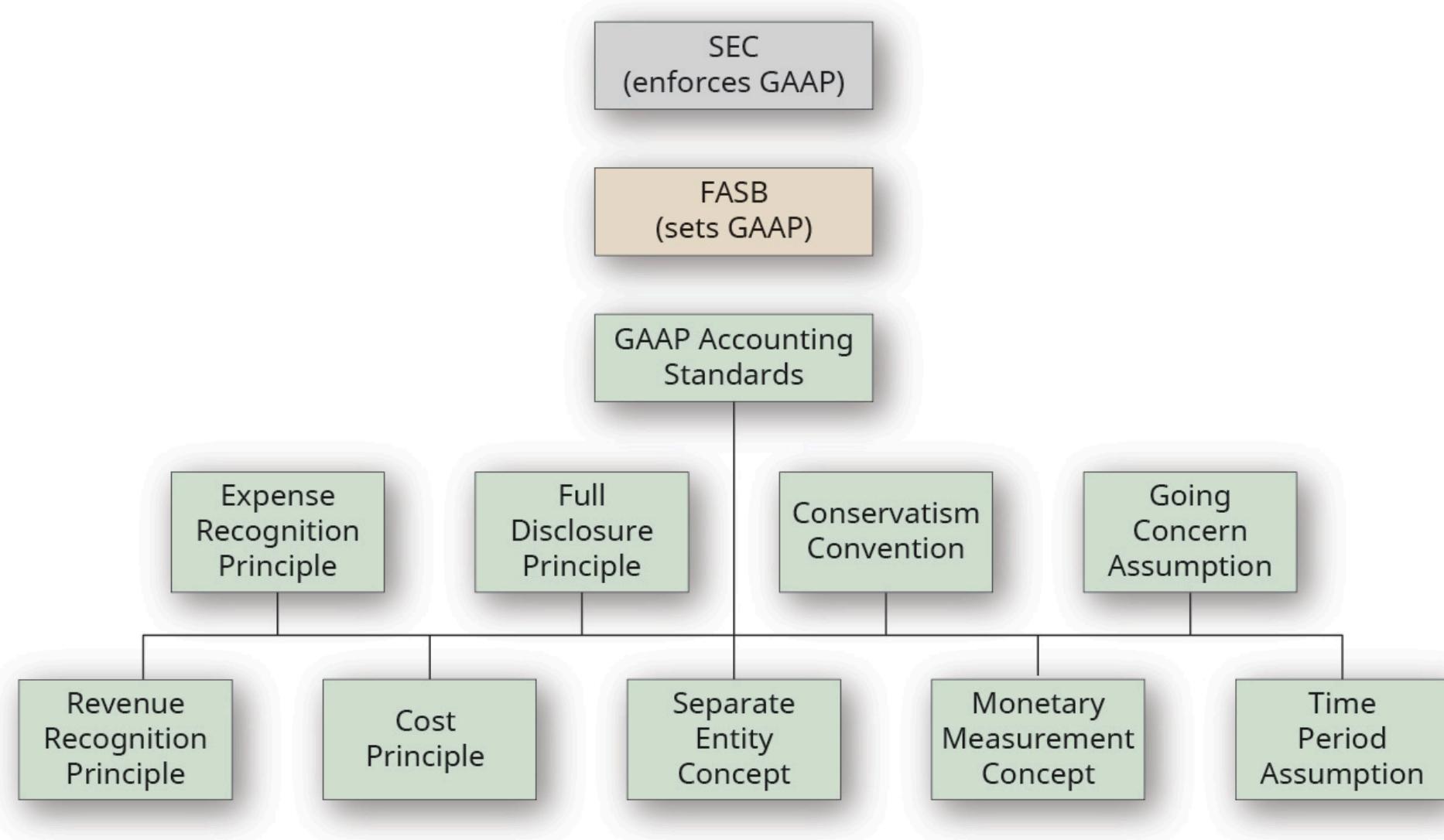
ACCRUAL ACCOUNTING

LEARNING OBJECTIVES

After completing this session, you should be able to

- Explain the difference between cash basis and accrual basis of accounting;
- Apply revenue recognition principle and expense matching principle in accrual basis accounting;

GAAP Accounting Standards Connection Tree



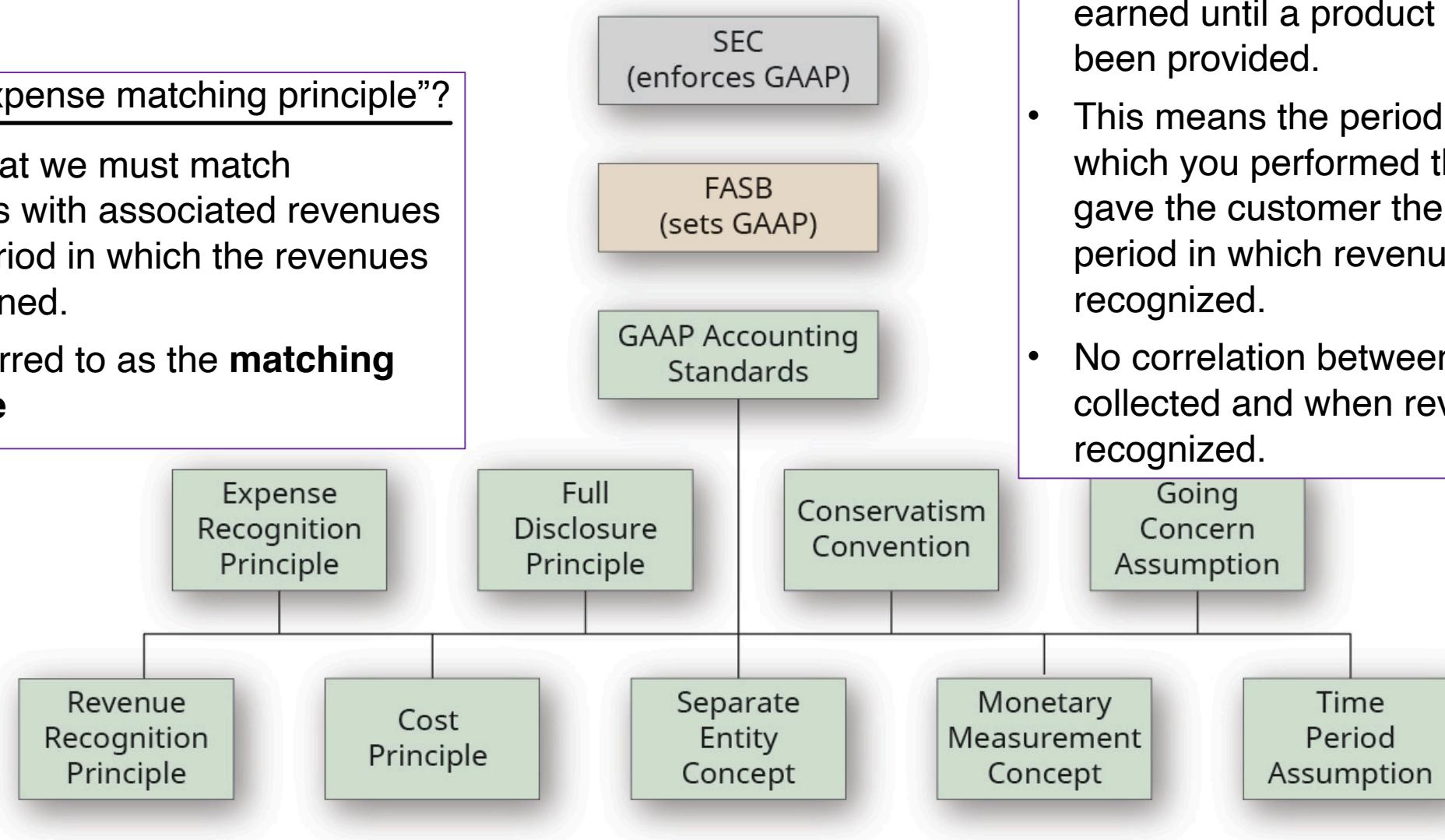
What is “revenue recognition principle”?

- Directs a company to recognize revenue in the period in which it is earned; revenue is not considered earned until a product or service has been provided.
- This means the period of time in which you performed the service or gave the customer the product is the period in which revenue is recognized.
- No correlation between when cash is collected and when revenue is recognized.

GAAP Accounting Standards Connection Tree

What is “expense matching principle”?

- States that we must match expenses with associated revenues in the period in which the revenues were earned.
- Also referred to as the **matching principle**



CASH ACCOUNTING VS. ACCRUAL ACCOUNTING

- Cash basis of accounting
 - Revenue and expenses are recorded only based on if there is an exchange of cash.
- Accrual basis of accounting
 - **Revenues** are recognized as soon as a product has been sold or a service has been performed, regardless of when the money is actually received.
 - All costs that match revenues reported in the present period are recorded as **expenses**, regardless of when the money is actually paid.



REVENUE RECOGNITION

REVENUE RECOGNITION ILLUSTRATED

- Revenue recognition is the process of recording revenue in the accounting period in which it was _____.
- This is not necessarily when cash is _____.
- Most corporations assume that revenue has been earned at an objectively-determined point in the accounting cycle.
 - For instance, it is often convenient to recognize revenue at the point when a sales invoice has been sent to a customer and the related goods have been received by a customer or services performed.

GAAP GUIDANCE ON REVENUE RECOGNITION

- GAAP provide guidance about when an economic activity should be recognized in financial accounting and reporting.
- An economic activity is recognized when it meets two criteria (whether payment has been received is **not** one of them):
 1. It is probable that any future economic benefit associated with the item will flow to the business; and
 2. It has a value that can be measured with reliability.

ACCRUAL BASIS OF ACCOUNTING: INTRODUCTION

- Under the accrual accounting principle, a company could earn and report \$1,000 of revenue in its first month of operation but receive \$0 in actual cash in that month.
- Example
 - ABC Consulting completes its service at an agreed price of \$1,000.
 - ABC should recognize \$_____ of revenue as soon as its work is done.
 - It does _____ matter whether the client pays the \$1,000 immediately or in 30 days.
- Do not confuse revenue with a cash receipt.

CASH ACCOUNTING VERSUS ACCRUAL ACCOUNTING

■ ACE Corp.'s transactions in October

- Service performed in October totaled \$20,000. \$18,000 cash payment was received in October; \$2,000 will be received in November.

■ BEE Corp.'s transactions in October

- Cash payment received in October totaled \$20,000; \$15,000 was for services that had been performed in October; \$5,000 payment was for services that would be performed in November.

	ACE Corp.	BEE Corp.
Revenue for October (Cash Basis)		
Revenue for October (Accrual Basis)		

REVENUE RECOGNITION ILLUSTRATED: THREE POSSIBLE SCENARIOS

Revenue was recognized _____ cash was received:

- 1) before
- 2) at the same time as, or
- 3) after

REVENUE RECOGNITION ILLUSTRATED (SCENARIO 1)

When revenue is earned and recognized *before* the receipt of cash payment from a customer.

Date	Account/Explanation	R	Debit	Credit
	To recognize revenue earned on (date).			

When cash payment is later received from the above customer:

Date	Account/Explanation	R	Debit	Credit
	To record payment received from customer #			

- Revenue is recognized in the _____ journal entry (the credit to revenue), prior to the receipt of cash.
- The second journal entry has _____ effect on revenue.

REVENUE RECOGNITION ILLUSTRATED (SCENARIO 2)

When cash is received at the same time when revenue is earned and recognized.

Date	Account/Explanation	R	Debit	Credit
	To recognize revenue earned and cash receipt			

A | L Eq - R | Ex
↑ ↑ ↑ ↑

REVENUE RECOGNITION ILLUSTRATED (SCENARIO 3)

When a cash deposit or advance payment is obtained *before* revenue is earned.

Date	Account/Explanation	R	Debit	Credit
	To recognize cash receipt and deferred revenue incurred on (date).			

Revenue is not recognized until the services have been performed. At that time, the following entry is made:

Date	Account/Explanation	R	Debit	Credit
	To record revenue earned on (date)			

- Revenue is recognized in the _____ journal entry (the credit to revenue), after the receipt of cash.
- The _____ journal entry has no effect on revenue.

REVENUE RECOGNITION: SUMMARY

	Revenues have been earned	Revenues <u>not</u> yet earned
Cash payments have been received from customers.	Revenues should be recognized (debit _____ / credit _____)	Revenue should not be recognized; A _____ is created (called unearned revenue or deferred revenue)
Cash payments have not been received from customers.	Revenues should be recognized (debit _____ / credit _____)	No transaction and no journal entry

A I L Eq - R I Ex
↑ ↑ ↑ ↑ ↑ ↑



EXPENSE MATCHING

EXPENSE MATCHING PRINCIPLE

- The matching principle requires that expenses be matched with revenues.
- Examples:

Example 1

Wages to employees are reported as an expense in the week when the employees worked and *not* in the week when the employees are paid.

Example 2

If a company agrees to give its employees 1% of its 2019 revenues as a bonus on January 15, 2020, the company should report the bonus as an expense in _____.

Cost Outlays

Incurred to produce revenue in the ***present*** accounting period

Record as _____

Examples:

- Rent expense
- Insurance expense
- Office supplies expense

Incurred to produce revenue in ***future*** accounting period

Record as _____

Examples:

- Prepaid rent
- Prepaid insurance
- Unused office supplies

EXPENSE RECOGNITION ILLUSTRATED

An example of when expenses are incurred **before** cash is paid occurs when the utilities expense for January is not paid until February.

In this case, an account payable is created in January as follows:

Description	Debit	Credit

On which financial statement and which month this utilities expense is reported?

When the January utilities are paid in February, the following is recorded:

Description	Debit	Credit

Does this entry have any effect on expenses reported on the February income statement?

EXPENSE RECOGNITION ILLUSTRATED (CONT'D)

Expenses can also be recorded *at the same time* when cash is paid.

For example, if salaries for January are paid on January 31, the entry on January 31 is:

Description	Debit	Credit

As a result of this entry, salaries expense is reported on the _____ income statement when cash is paid.

When a cash payment is made before the expense is incurred, such as insurance paid in advance:

Description	Debit	Credit

As the prepaid insurance is used, it is appropriate to report an expense on the income statement by recording the following entry:

Description	Debit	Credit

EXPENSE RECOGNITION SUMMARY

- The preceding examples illustrate how to match expenses to the appropriate accounting period.
- The matching principle requires that expenses be reported ***in the same period*** as the revenues they helped generate. That is, expenses are reported on the income statement:
 - When related revenue is recognized, or
 - During the appropriate time period when it is consumed, regardless of when cash is paid.
- To ensure the recognition and matching of revenues and expenses to the correct accounting period, account balances must be reviewed and **adjusted** prior to the preparation of financial statements.

REVENUE RECOGNITION & EXPENSE MATCHING SUMMARY

	Revenues has been earned	Revenues <u>not</u> yet earned
Cash payments have been received from customers.	Revenues should be recognized (debit _____/credit _____)	Revenue should not be recognized; A _____ is created (unearned revenue/deferred revenue)
Cash payments have not been received from customers.	Revenues should be recognized (debit _____/credit _____)	No transaction and no journal entry
	Costs Recorded as Expense	Costs Recorded as Assets
Cash payments have been made	Paid for <i>present</i> period revenue Expense are recognized (debit _____/credit _____)	Paid for <i>future</i> period revenue No expenses are recognized; An _____ is created (prepaid expense or deferred expense)
Cash payments have yet to be made	Expense are recognized (debit _____/credit _____)	N/A

INFO 7225

Module 1

6. Preparation of Financial Statements

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PREPARING FINANCIAL STATEMENTS

LEARNING OBJECTIVES

After completing this session, you should be able to

- Use an adjusted trial balance to prepare the following financial statements
 - ✓ The Income Statement
 - ✓ The Statement of Shareholders' Equity, and
 - ✓ The Balance Sheet

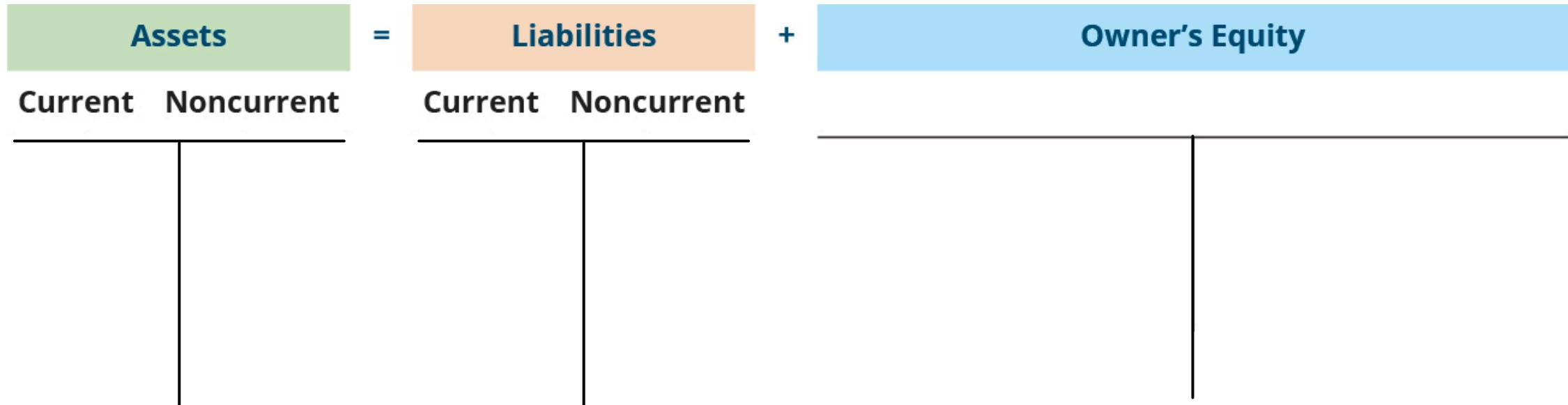
FOUR FINANCIAL STATEMENTS

1. The Income Statement
2. The Statement of Shareholders' Equity
3. The Balance Sheet
4. The Statement of Cash Flows

TEN ELEMENTS OF THE FINANCIAL STATEMENTS

1. **Revenue**—value of goods and services the organization sold or provided.
2. **Expenses**—costs of providing the goods or services for which the organization earns revenue.
3. **Gains**—gains are similar to revenue but relate to “incidental or peripheral” activities of the organization.
4. **Losses**—losses are similar to expenses but related to “incidental or peripheral” activities of the organization
5. **Assets**—items the organization owns, controls, or has a claim to.
6. **Liabilities**—amounts the organization owes to others (also called creditors).
7. **Equity**—the net worth (or net assets) of the organization.
8. **Investment by owners**—cash or other assets provided to the organization in exchange for an ownership interest.
9. **Distribution to owners**—cash, other assets, or ownership interest (equity) provided to owners.
10. **Comprehensive income**—defined as the “change in equity of a business enterprise during a period from transactions and other events and circumstances from non-owner sources”. While further discussion of comprehensive income is reserved for intermediate and advanced studies in accounting, it is worth noting that comprehensive income has four components, focusing on activities related to foreign currency, derivatives, investments, and pensions.

GRAPHICAL REPRESENTATION OF THE ACCOUNTING EQUATION



- | | |
|-------------|---------------------------|
| 1. Revenue | 6. Liabilities |
| 2. Expenses | 7. Equity |
| 3. Gains | 8. Investment by owners |
| 4. Losses | 9. Distribution to owners |
| 5. Assets | 10. Comprehensive income |

1. INCOME STATEMENT

Big Dog Carworks Corp.		
Income Statement		
For the Month Ended January 31, 2015		
<i>Revenues</i>		
Repair revenues		\$10,000
<i>Expenses</i>		
Rent expense	\$1,600	
Salaries expense	3,500	
Supplies expense	2,000	
Fuel expense	700	
Total expenses		7,800
Net income		<u>\$2,200</u>

The heading of the income statement includes three lines.

- i. The first line lists the business name.
- ii. The middle line indicates the financial statement that is being presented.
- iii. The last line indicates the time frame of the financial statement. Do not forget the income statement is for a period of time (the month of January in our example).

There are three columns.

- i. Going from left to right, the first column is the category heading or account.
- ii. The second column is used when there are numerous accounts in a particular category (Expenses, in our example).
- iii. The third column is a total column. In this illustration, it is the column where subtotals are listed and net income is determined (subtracting Expenses from Revenues).

1. INCOME STATEMENT

Big Dog Carworks Corp.

Income Statement

For the Month Ended January 31, 2015

Revenues

Repair revenues	\$10,000
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Expenses

Rent expense	\$1,600
Salaries expense	3,500
Supplies expense	2,000
Fuel expense	700
Total expenses	<u>7,800</u>
Net income	<u><u>\$2,200</u></u>

The net income is transferred to this financial statement:

2. THE STATEMENT OF STOCKHOLDERS' EQUITY

Big Dog Carworks Corp.
Statement of Stockholders' Equity
For the Month Ended January 31, 2015

	Common Stock	Retained Earnings	Total Equity
Opening balance	\$ -0-	\$ -0-	\$ -0-
Stock issued	10,000		10,000
Net income		2,200	2,200
Dividends		(200)	(200)
Ending balance	<u>\$10,000</u>	<u>\$2,000</u>	<u>\$12,000</u>

2. THE STATEMENT OF STOCKHOLDERS' EQUITY

Big Dog Carworks Corp.
Statement of Stockholders' Equity
For the Month Ended January 31, 2015

	Common Stock	Retained Earnings	Total Equity
Opening balance	\$ -0-	\$ -0-	\$ -0-
Stock issued	10,000		10,000
Net income		2,200	2,200
Dividends		(200)	(200)
Ending balance	<u>\$10,000</u>	<u>\$2,000</u>	<u>\$12,000</u>

These totals are transferred
to the _____.



Apple Inc.

CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (Unaudited)

(In millions, except per share amounts)

	Three Months Ended	
	December 28, 2019	December 29, 2018
Total shareholders' equity, beginning balances	<u>\$ 90,488</u>	<u>\$ 107,147</u>
Common stock and additional paid-in capital:		
Beginning balances	45,174	40,201
Common stock issued	2	—
Common stock withheld related to net share settlement of equity awards	(951)	(822)
Share-based compensation	1,747	1,591
Ending balances	<u>45,972</u>	<u>40,970</u>
Retained earnings:		
Beginning balances	45,898	70,400
Net income	22,236	19,965
Dividends and dividend equivalents declared	(3,485)	(3,526)
Common stock withheld related to net share settlement of equity awards	(536)	(594)
Common stock repurchased	(20,000)	(8,236)
Cumulative effects of changes in accounting principles	(136)	2,501
Ending balances	<u>43,977</u>	<u>80,510</u>
Accumulated other comprehensive income/(loss):		
Beginning balances	(584)	(3,454)
Other comprehensive income/(loss)	30	(223)
Cumulative effects of changes in accounting principles	136	89
Ending balances	<u>(418)</u>	<u>(3,588)</u>
Total shareholders' equity, ending balances	<u>\$ 89,531</u>	<u>\$ 117,892</u>
Dividends and dividend equivalents declared per share or RSU	\$ 0.77	\$ 0.73

See accompanying Notes to Condensed Consolidated Financial Statements.

In-class Exercise 1. Determining Missing Financial Information

Required: Complete the following calculations for each individual company:

- a. If ColorMePink Ltd. has a retained earnings opening balance of \$50,000 at the beginning of the year, and an ending balance of \$40,000 at the end of the year, what would be the net income/loss, if dividends paid were \$20,000?
- b. If ForksAndSpoons Ltd. has net income of \$150,000, dividends paid of \$40,000 and a retained earnings ending balance of \$130,000, what would be the retained earnings opening balance?
- c. If CupsAndSaucers Ltd. has a retained earnings opening balance of \$75,000 at the beginning of the year, and an ending balance of \$40,000 at the end of the year, what would be the dividends paid, if the net loss was \$35,000?

In-class Exercise 2. Equity – What Causes It to Change

	Assets	=	Liabilities	+	Equity
Balances at April 1, 2015	\$100,000		\$60,000		\$40,000

? Shares issued in April

? April net income(loss)

? Dividends paid in April

Balances at April 30, 2015	<u>\$180,000</u>	=	<u>\$130,000</u>	+	<u> ?</u>
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Required: Using the information provided above, calculate the net income or net loss realized during April under each of the following independent assumptions.

- a. No shares were issued in April and no dividends were paid.
- b. \$50,000 of shares were issued in April and no dividends were paid.
- c. No shares were issued in April and \$4,000 of dividends were paid in April.

3. THE BALANCE SHEET

Big Dog Carworks Corp. Balance Sheet At January 31, 2015			
Assets		Liabilities	
Cash	\$ 3,700	Accounts payable	\$ 700
Accounts receivable	2,000	Unearned revenue	400
Prepaid insurance	2,400	Notes payable	<u>6,000</u>
Equipment	3,000	Total liabilities	<u>\$ 7,100</u>
Truck	8,000		
		Equity	
		Common stock	\$10,000
		Retained earnings	<u>2,000</u>
		Total equity	<u>12,000</u>
Total assets	<u>\$19,100</u>	Total liabilities and equity	<u>\$19,100</u>

Total assets (\$19,100 here) always equal Total liabilities (\$7,100) plus Equity (\$12,000).



THE CLASSIFIED BALANCE SHEET

THE CLASSIFIED BALANCE SHEET

- A classified balance sheet organizes the asset and liability accounts into categories.
- The classification of asset and liability accounts into meaningful categories is designed to facilitate the analysis of balance sheet information by external users.

Assets	Liabilities
Current assets	Current liabilities
Long-term assets:	Long-term liabilities
Long-term investments Property, plant, & equipment Intangible assets Other assets	

CURRENT ASSETS

- Current assets are those resources that the entity expects to convert to cash, or to consume during the next year or within the operating cycle of the entity, whichever is longer:
 - ✓ Cash; short-term investments; notes receivable; merchandise inventory; supplies; prepaid expenses
- On the balance sheet, current assets are normally reported before non-current assets. They are listed by decreasing levels of *liquidity* — their ability to be converted into cash. Therefore, cash appears first under the current asset heading since it is already liquid..

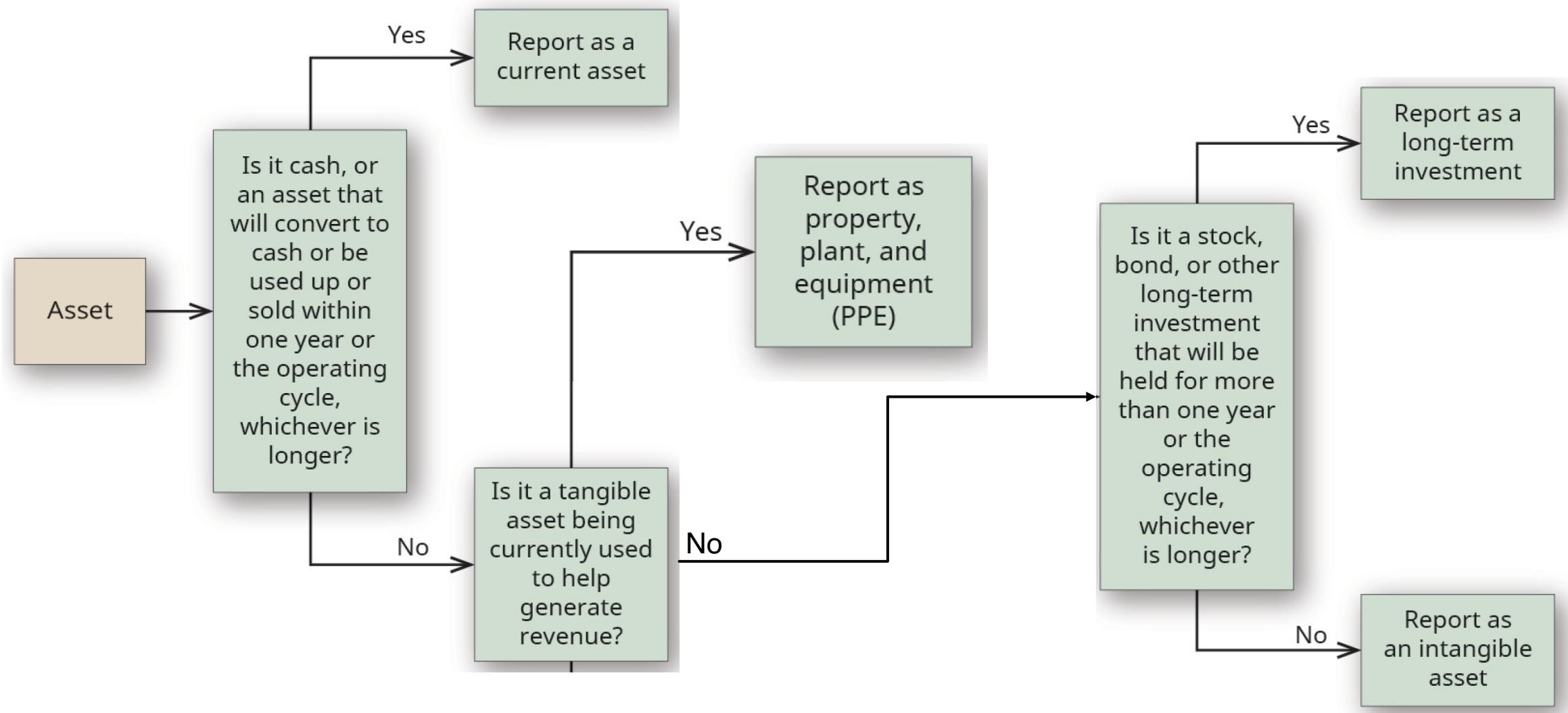
NON-CURRENT ASSETS: PPE

- Assets that will be useful for more than one year; they are sometimes referred to as long-lived assets.
 - Include property, plant, and equipment (PPE) items used in the operations of the business.
 - Some examples of PPE are:
 - a) land
 - b) buildings
 - c) equipment, and
 - d) motor vehicles such as trucks

NON-CURRENT ASSETS: INTANGIBLE ASSETS

- Other types of non-current assets include long-term investments and intangible assets.
 - ▶ Intangible assets are resources that do not have a physical form and whose value comes from the rights held by the owner.
 - ▶ They are used over the long term to produce or sell products and services and include:
 - ✓ copyrights
 - ✓ patents
 - ✓ trademarks, and
 - ✓ franchises

ASSET CLASSIFICATION FLOWCHART



CURRENT LIABILITIES

- Obligations that must be paid within the next 12 months or within the entity's next operating cycle, whichever is longer.
- They are shown first in the liabilities section of the balance sheet and generally listed in order of maturity (their due dates).
- The order of liabilities is not as structured as that of assets and may vary somewhat from company to company.
- Examples:
 - ✓ AP, unearned revenue, accrued liabilities such as interest payable and wages payable, income taxes payable, the current portion of long-term liabilities

NON-CURRENT LIABILITIES

- Also referred to as long-term liabilities
- Borrowings that do not require repayment for more than one year, such as the long-term portion of a bank loan or a mortgage.
 - A mortgage is a liability that is secured by real estate.

3. THE CLASSIFIED BALANCE SHEET

Big Dog Carworks Corp. Balance Sheet At December 31, 2018					
	Assets		Liabilities		
	2018	2017		2018	2017
<i>Current assets</i>			<i>Current liabilities</i>		
Cash	\$ 10,800	\$ 12,000	Accounts payable	\$ 24,000	\$ 22,000
Accounts receivable	26,000	24,000	Income taxes payable	15,000	10,000
Merchandise inventories	120,000	100,000	Current portion of long-term notes	39,000	82,250
Prepaid expenses	1,200	570	Total current liabilities	\$ 78,000	\$114,250
Total current assets	\$158,000	\$136,570			
<i>Property, plant, and equipment (Note 4)</i>	126,645	10,430			
			<i>Long-term liabilities</i>		
			Notes payable (Note 5)	163,145	-0-
			Total liabilities	\$241,145	\$114,250
			<i>Equity</i>		
			Common stock (Note 6)	\$ 11,000	\$ 11,000
			Retained earnings	32,500	21,750
			Total equity	43,500	32,750
Total assets	\$284,645	\$147,000	Total liabilities and equity	\$284,645	\$147,000

Notes are included at the end of the financial statements. Among other purposes, they provide details about a particular category on the balance sheet or income statement.

Apple Inc.

CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)

(In millions, except number of shares which are reflected in thousands and par value)

	December 28, 2019	September 28, 2019
ASSETS:		
Current assets:		
Cash and cash equivalents	\$ 39,771	\$ 48,844
Marketable securities	67,391	51,713
Accounts receivable, net	20,970	22,926
Inventories	4,097	4,106
Vendor non-trade receivables	18,976	22,878
Other current assets	12,026	12,352
Total current assets	163,231	162,819
Non-current assets:		
Marketable securities	99,899	105,341
Property, plant and equipment, net	37,031	37,378
Other non-current assets	40,457	32,978
Total non-current assets	177,387	175,697
Total assets	\$ 340,618	\$ 338,516

LIABILITIES AND SHAREHOLDERS' EQUITY:			
Current liabilities:			
Accounts payable	\$ 45,111	\$ 46,236	
Other current liabilities	36,263	37,720	
Deferred revenue	5,573	5,522	
Commercial paper	4,990	5,980	
Term debt	10,224	10,260	
Total current liabilities	102,161	105,718	
Non-current liabilities:			
Term debt	93,078	91,807	
Other non-current liabilities	55,848	50,503	
Total non-current liabilities	148,926	142,310	
Total liabilities	251,087	248,028	
Commitments and contingencies			
Shareholders' equity:			
Common stock and additional paid-in capital, \$0.00001 par value: 12,600,000 shares authorized; 4,384,959 and 4,443,236 shares issued and outstanding, respectively	45,972	45,174	
Retained earnings	43,977	45,898	
Accumulated other comprehensive income/(loss)	(418)	(584)	
Total shareholders' equity	89,531	90,488	
Total liabilities and shareholders' equity	\$ 340,618	\$ 338,516	



THE STATEMENT OF CASH FLOWS

4. THE STATEMENT OF CASH FLOWS

Name of Company
Statement of Cash Flows
For the Period Ended

Cash flows from operating activities:

[Each operating inflow/outflow is listed]

Net cash inflow/outflow from operating activities \$ XX

Cash flows from investing activities:

[Each investing inflow/outflow is listed]

Net cash inflow/outflow from investing activities XX

Cash flows from financing activities:

[Each financing inflow/outflow is listed]

Net cash inflow/outflow from financing activities XX

Net increase/decrease in cash

\$ XX

XX

Cash at beginning of period

\$ XX

Cash at end of period

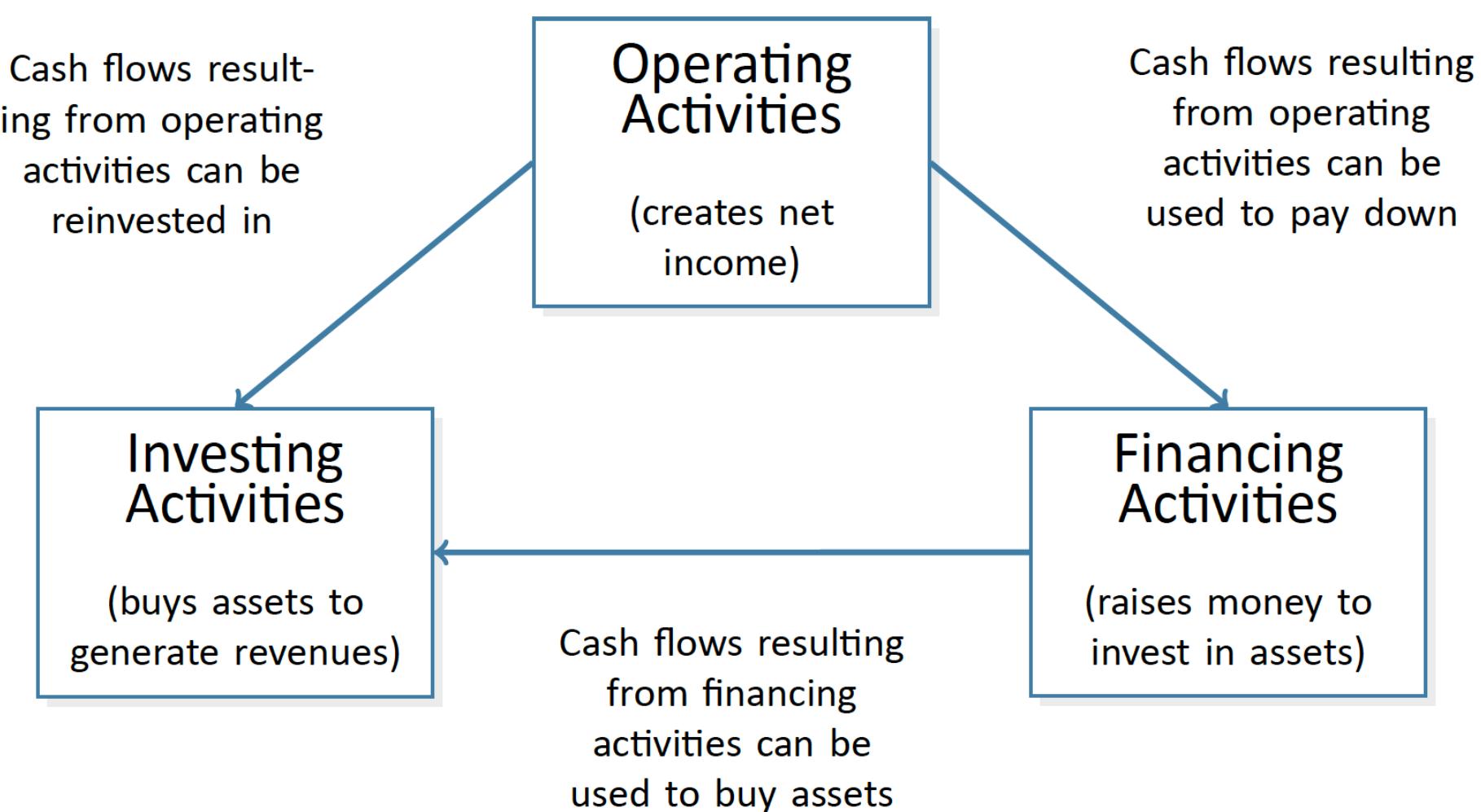
\$ XX

Apple Inc.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)
(In millions)

	Three Months Ended	
	December 28, 2019	December 29, 2018
Cash, cash equivalents and restricted cash, beginning balances	\$ 50,224	\$ 25,913
Operating activities:		
Net income	22,236	19,965
Adjustments to reconcile net income to cash generated by operating activities:		
Depreciation and amortization	2,816	3,395
Share-based compensation expense	1,710	1,559
Deferred income tax expense/(benefit)	(349)	53
Other	(142)	(54)
Changes in operating assets and liabilities:		
Accounts receivable, net	2,015	5,130
Inventories	(28)	(1,076)
Vendor non-trade receivables	3,902	6,905
Other current and non-current assets	(7,054)	(886)
Accounts payable	(1,089)	(8,501)
Deferred revenue	985	(370)
Other current and non-current liabilities	5,514	570
Cash generated by operating activities	30,516	26,690

Investing activities:		
Purchases of marketable securities	(37,416)	(7,077)
Proceeds from maturities of marketable securities	19,740	7,203
Proceeds from sales of marketable securities	7,280	9,723
Payments for acquisition of property, plant and equipment	(2,107)	(3,355)
Payments made in connection with business acquisitions, net	(958)	(167)
Purchases of non-marketable securities	(77)	(427)
Other	(130)	(56)
Cash generated by/(used in) investing activities	(13,668)	5,844
Financing activities:		
Proceeds from issuance of common stock	2	—
Payments for taxes related to net share settlement of equity awards	(1,379)	(1,318)
Payments for dividends and dividend equivalents	(3,539)	(3,568)
Repurchases of common stock	(20,706)	(8,796)
Proceeds from issuance of term debt, net	2,210	—
Repayments of term debt	(1,000)	—
Proceeds from/(Repayments of) commercial paper, net	(979)	6
Other	(16)	—
Cash used in financing activities	(25,407)	(13,676)
Increase/(Decrease) in cash, cash equivalents and restricted cash	(8,559)	18,858
Cash, cash equivalents and restricted cash, ending balances	\$ 41,665	\$ 44,771

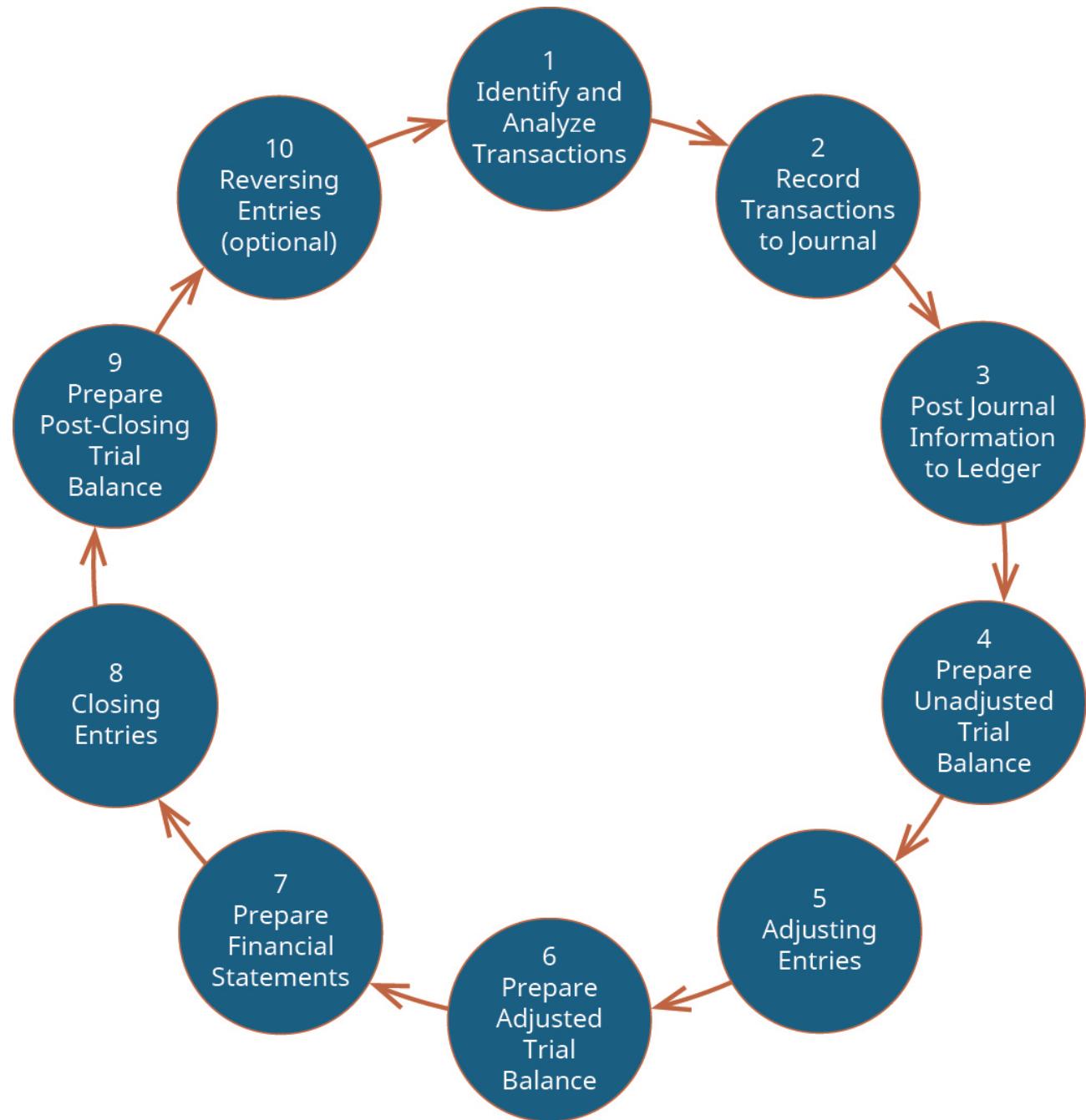
RELATIONSHIPS AMONG THE THREE TYPES OF BUSINESS ACTIVITIES





PREPARING FINANCIAL STATEMENTS

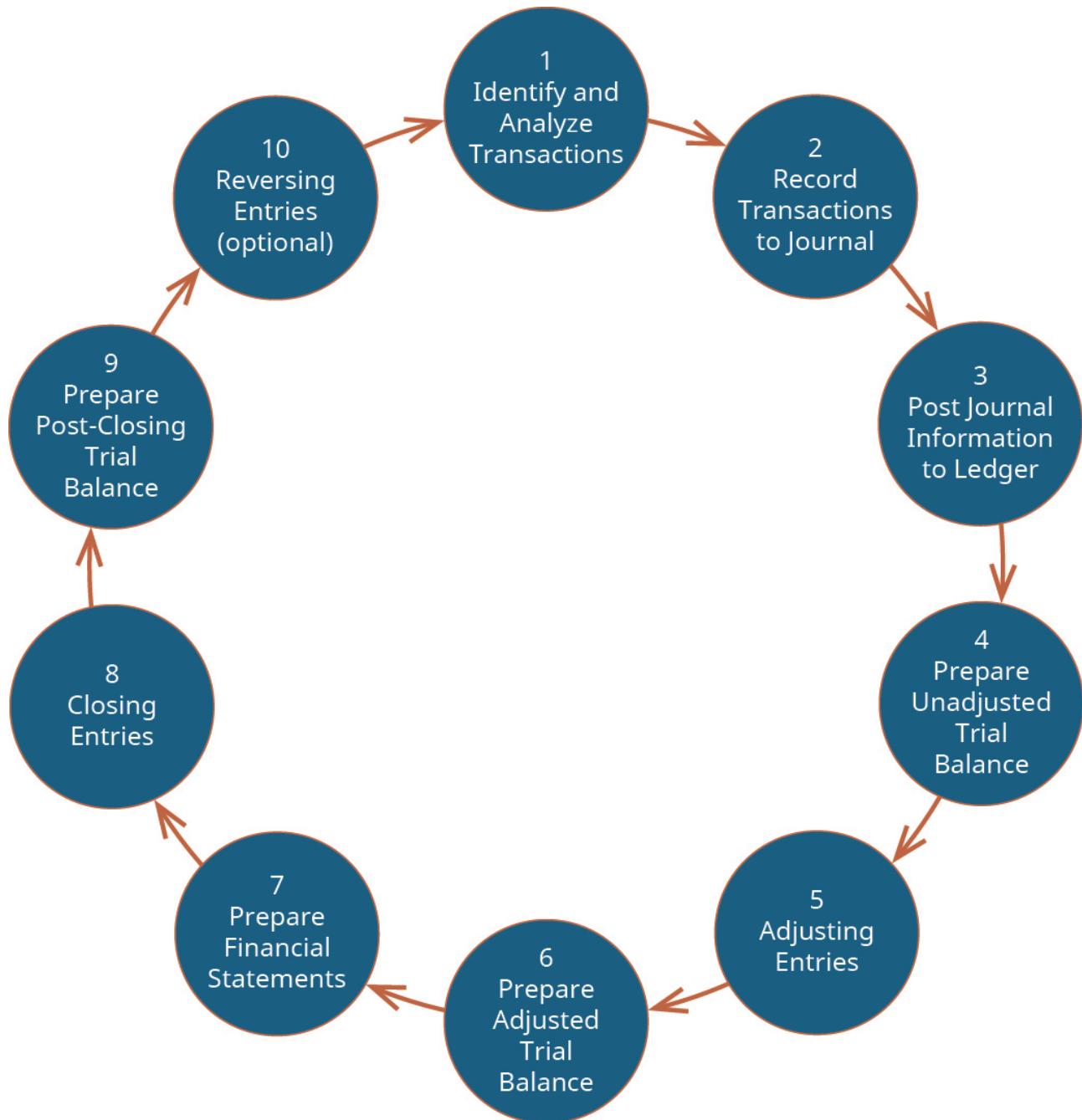
The Accounting Cycle: Review



The Accounting Cycle: Review

Big Dog Carworks Corp.
Unadjusted Trial Balance
At January 31, 2015

<u>Acct.</u>	<u>Account</u>	<u>Debit</u>	<u>Credit</u>
101	Cash	\$3,700	
110	Accounts receivable	2,000	
161	Prepaid insurance	2,400	
183	Equipment	3,000	
184	Truck	8,000	
201	Bank loan		
210	Accounts payable		
247	Unearned revenue		
320	Share capital		
330	Dividends	200	
450	Repair revenue		
654	Rent expense	1,600	
656	Salaries expense	3,500	
668	Supplies expense	2,000	
670	Truck operation expense	700	
		<u>\$27,100</u>	<u>\$27,100</u>



Big Dog Carworks Corp.
Unadjusted Trial Balance
At January 31, 2015

Big Dog Carworks Corp.
Adjusted Trial Balance
At January 31, 2015

<u>Acct.</u>	<u>Account</u>	<u>Debit</u>	<u>Credit</u>
101	Cash	\$3,700	
110.	Accounts receivable	2,000	
161	Prepaid insurance	2,400	→
183	Equipment	3,000	
184.	Truck	8,000	
201	Bank loan		\$6,000
210	Accounts payable		700
247	Unearned revenue		400
320	Share capital		10,000
330	Dividends	200	
450	Repair revenue		10,000
654	Rent expense	1,600	
656	Salaries expense	3,500	
668	Supplies expense	2,000	
670	Truck operation expense	700	
		<u>\$27,100</u>	<u>\$27,100</u>

Big Dog Carworks Corp.
Unadjusted Trial Balance
At January 31, 2015

Big Dog Carworks Corp.
Adjusted Trial Balance
At January 31, 2015

<u>Acct.</u>	<u>Account</u>	<u>Debit</u>	<u>Credit</u>
101	Cash	\$3,700	
110.	Accounts receivable	2,000	
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330	Dividends	200	
450	Repair revenue		10,000
654	Rent expense	1,600	
656	Salaries expense	3,500	
668	Supplies expense	2,000	
670	Truck operation expense	700	
		<u>\$27,100</u>	<u>\$27,100</u>

Big Dog Carworks Corp.
Unadjusted Trial Balance
At January 31, 2015

Big Dog Carworks Corp.
Adjusted Trial Balance
At January 31, 2015

<u>Acct.</u>	<u>Account</u>	<u>Debit</u>	<u>Credit</u>
101	Cash	\$3,700	
110.	Accounts receivable	2,000	
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201	Bank loan	\$6,000	
210	Accounts payable		700
247	Unearned revenue		400
320	Share capital		10,000
330	Dividends	200	
450	Repair revenue		10,000
654	Rent expense	1,600	
656	Salaries expense	3,500	
668	Supplies expense	2,000	
670	Truck operation expense	700	
		<u>\$27,100</u>	<u>\$27,100</u>

Big Dog Carworks Corp.
Unadjusted Trial Balance
At January 31, 2015

Big Dog Carworks Corp.
Adjusted Trial Balance
At January 31, 2015

<u>Acct.</u>	<u>Account</u>	<u>Debit</u>	<u>Credit</u>
101	Cash	\$3,700	
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320	Share capital		10,000
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450	Repair revenue		10,000
654	Rent expense	1,600	
656	Salaries expense	3,500	
668	Supplies expense	2,000	
670	Truck operation expense	700	
		<u>\$27,100</u>	<u>\$27,100</u>



The Accounting Cycle: Review

Big Dog Carworks Corp.
Unadjusted Trial Balance
At January 31, 2015

<u>Acct.</u>	<u>Account</u>	<u>Debit</u>	<u>Credit</u>
101	Cash	\$3,700	
110	Accounts receivable	2,000	
161	Prepaid insurance	2,400	
183	Equipment	3,000	
184	Truck	8,000	
201	Bank loan		\$6,000
210	Accounts payable		700
247	Unearned revenue		400
320	Share capital		10,000
330	Dividends	200	
450	Repair revenue		10,000
654	Rent expense	1,600	
656	Salaries expense	3,500	
668	Supplies expense	2,000	
670	Truck operation expense	700	
		<u>\$27,100</u>	<u>\$27,100</u>



Big Dog Carworks Corp.
Adjusted Trial Balance
At January 31, 2015

<u>Account</u>	<u>Debit</u>	<u>Credit</u>
Cash	\$3,700	
Accounts receivable	2,400	
Prepaid insurance	2,200	
Equipment	3,000	
Accumulated depreciation – equipment		\$25
Truck	8,000	
Accumulated depreciation – truck		100
Bank loan		6,000
Accounts payable		700
Interest payable		18
Unearned repair revenue		100
Income tax payable		500
Share capital		10,000
Dividends		200
Repair revenue		10,700
Depreciation expense – equipment	25	
Depreciation expense – truck	100	
Rent expense		1,600
Insurance expense		200
Interest expense		18
Salaries expense		3,500
Supplies expense		2,000
Truck operation expense		700
Income tax expense		500
Total debits and credits	\$28,143	\$28,143

THE ACCOUNTING CYCLE

Adjustment: in addition to depreciation of fixed assets, there are four other types of adjustment entries needed:

- **Deferred expenses (Prepaid ~; = _____)**

Assets paid for before their use. When they are used, this asset's value is reduced and an expense is recognized. Some examples include supplies, insurance, and depreciation.

- **Deferred revenues (unearned ~; = _____)**

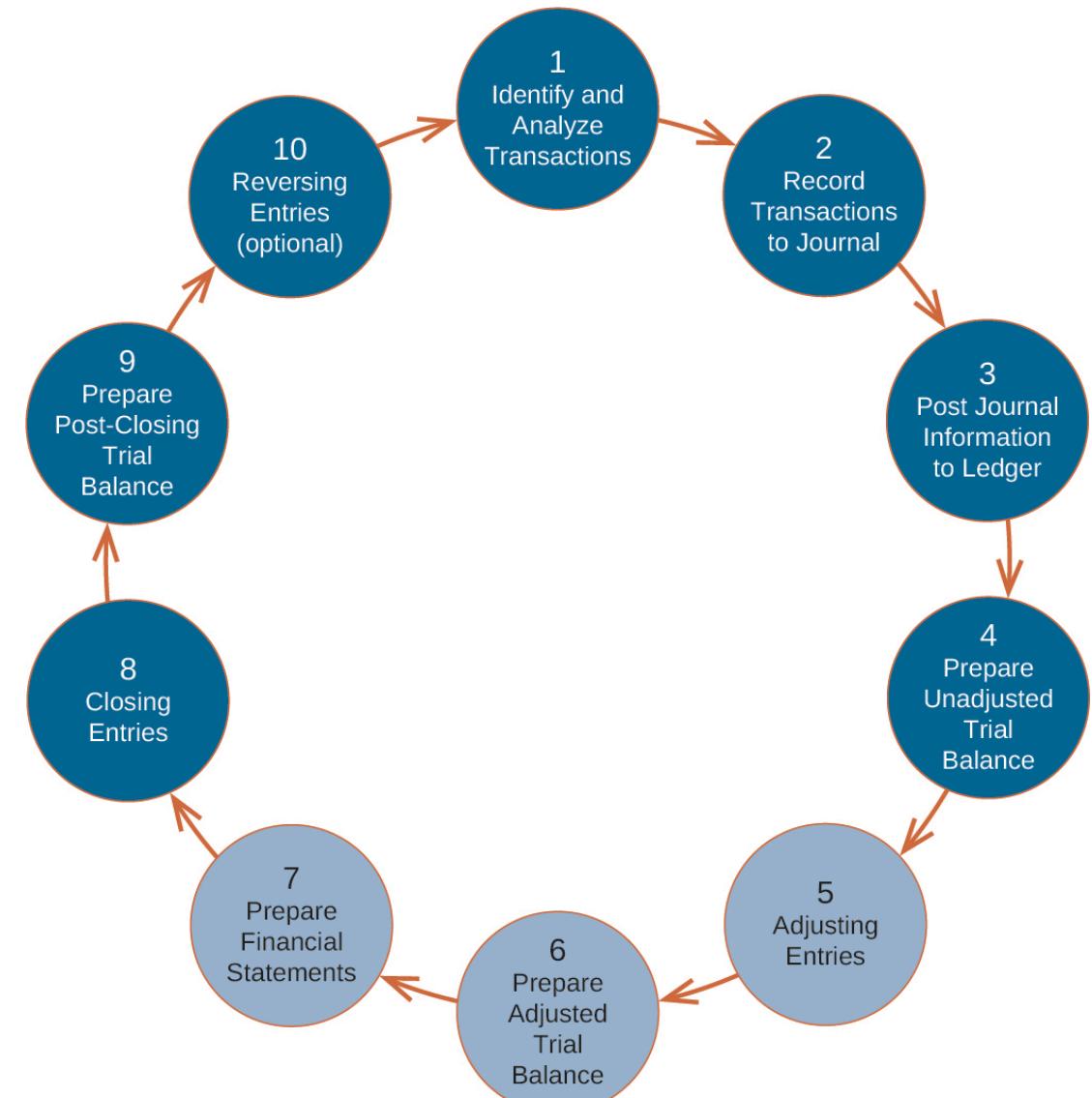
Customer advanced payments for product or services yet to be provided. When the company provides the product or service, revenue is then recognized.

- **Accrued revenues**

Revenues earned in a period but have yet to be recorded and no money has been collected. Accrued revenues are updated at the end of the period to recognize revenue and money owed to the company.

- **Accrued expenses**

Accrued expenses are incurred in a period but have yet to be recorded and no money has been paid. Accrued expenses are updated to reflect the expense and the company's liability.



Adjusted Trial Balance at the End of a Reporting Period		Account Balance	
	Account	Debit	Credit
Cash		\$ 3,700	
Accounts receivable		2,400	
Prepaid insurance		2,200	
Equipment		3,000	
Accumulated depreciation – equipment			\$ 25
Truck		8,000	
Accumulated depreciation – truck			100
Accounts payable			700
Unearned revenue			100
Interest payable			19
Income tax payable			500
Notes payable			6,000
Common stock			10,000
Dividends		200	
Repair revenue			10,700
Depreciation expense – equipment		25	
Depreciation expense – truck		100	
Rent expense		1,600	
Insurance expense		200	
Interest expense		19	
Salaries expense		3,500	
Supplies expense		2,000	
Truck operation expense		700	
Income tax expense		500	
Total debits and credits		<u>\$28,144</u>	<u>\$28,144</u>

<u>Account</u>	<u>Debit</u>	<u>Credit</u>
Cash	\$ 3,700	
Accounts receivable	2,400	
Prepaid insurance	2,200	
Equipment	3,000	
Accum. dep. – equipment		\$ 25
Truck	8,000	
Accum. dep. – truck		100
Accounts payable		700
Unearned revenue		100
Interest payable		19
Income tax payable		500
Notes payable		6,000
Common stock		10,000
Dividends	200	
Repair revenue		10,700
Dep. expense – equipment	25	
Dep. expense – truck	100	
Rent expense	1,600	
Insurance expense	200	
Interest expense	19	
Salaries expense	3,500	
Supplies expense	2,000	
Truck operation expense	700	
Income tax expense	500	
	\$28,144	\$28,144

Big Dog Carworks Corp.

For the Month Ended January 31, 2015

Revenues	
Repair revenue	\$10,700
Expenses	
Salaries expense	\$ 3,500
Supplies expense	2,000
Rent expense	1,600
Truck operation expense	700
Insurance expense	200
Dep. expense – truck	100
Dep. expense – equipment	25
Interest expense	19
Income tax expense	500
	<hr/>
Total expenses	8,644
Net income	\$2,056

<u>Account</u>	<u>Debit</u>	<u>Credit</u>
Cash	\$ 3,700	
Accounts receivable	2,400	
Prepaid insurance	2,200	
Equipment	3,000	
Accum. dep. – equipment		\$ 25
Truck	8,000	
Accum. dep. – truck		100
Accounts payable		700
Unearned revenue		100
Interest payable		19
Income tax payable		500
Notes payable		6,000
Common stock		10,000
Dividends	200	
Repair revenue		10,700
Dep. expense – equipment	25	
Dep. expense – truck	100	
Rent expense	1,600	
Insurance expense	200	
Interest expense	19	
Salaries expense	3,500	
Supplies expense	2,000	
Truck operation expense	700	
Income tax expense	500	
	\$28,144	\$28,144

Common Stock and Dividends are transferred to the Statement of Stockholders' Equity. Dividends is part of Retained Earnings because it is a distribution of Net Income.

Big Dog Carworks Corp. Income Statement For the Month Ended January 31, 2015	
1	
Revenues	
Repair revenue	\$10,700
Expenses	
Salaries expense	\$ 3,500
Supplies expense	2,000
Rent expense	1,600
Truck operation expense	700
Insurance expense	200
Dep. expense – truck	100
Dep. expense – equipment	25
Interest expense	19
Income tax expense	500
Total expenses	
	8,644
Net income	\$2,056

Big Dog Carworks Corp.
Statement of Stockholders' Equity
For the Month Ended January 31, 2015

Net Income is transferred to the Statement of Stockholders' Equity as part of Retained Earnings.

	Common	Retained	Total
	stock	earnings	equity
	\$ -0-	\$ -0-	\$ -0-
Balance at beginning of period	\$ -0-	\$ -0-	\$ -0-
Stock issued			
Dividends			
Net income			
Balance at end of period			

These accounts are used to prepare _____

Big Dog Carworks Corp.
Trial Balance
At January 31, 2015

Account	Debit	Credit
Cash	\$ 3,700	
Accounts receivable	2,400	
Prepaid insurance	2,200	
Equipment	3,000	
Accum. dep. – equipment		\$ 25
Truck	8,000	
Accum. dep. – truck		100
Accounts payable		700
Unearned revenue		100
Interest payable		19
Income tax payable		500
Notes payable		6,000
Common stock		10,000
Dividends	200	
Repair revenue		10,700
Dep. expense – equipment	25	
Dep. expense – truck	100	
Rent expense	1,600	
Insurance expense	200	
Interest expense	19	
Salaries expense	3,500	
Supplies expense	2,000	
Truck operation expense	700	
Income tax expense	500	
	\$28,144	\$28,144

Big Dog Carworks Corp.

At January 31, 2015

<i>Assets</i>	
Cash	\$ 3,700
Accounts receivable	2,400
Prepaid insurance	2,200
Equipment	\$3,000
Less: Accum. dep.	25
Truck	\$8,000
Less: Accum. dep.	100
Total assets	\$19,175
<i>Liabilities</i>	
Accounts payable	\$ 700
Unearned revenue	100
Interest payable	19
Income tax payable	500
Notes payable	6,000
Total liabilities	\$7,319
<i>Equity</i>	
Common stock	
Retained earnings	
Total equity	11,856
Total liabilities and equity	\$19,175

The Common Stock and Retained Earnings balances are transferred to the balance sheet from the statement of stockholders' equity.

Adjusted Trial Balance at the End of a Reporting Period		Account Balance	
Account		Debit	Credit
Cash		\$ 3,700	
Accounts receivable		2,400	
Prepaid insurance		2,200	
Equipment		3,000	
Accumulated depreciation – equipment			\$ 25
Truck		8,000	
Accumulated depreciation – truck			100
Accounts payable			700
Unearned revenue			100
Interest payable			19
Income tax payable			500
Notes payable			6,000
Common stock			10,000
Dividends		200	
Repair revenue			10,700
Depreciation expense – equipment		25	
Depreciation expense – truck		100	
Rent expense		1,600	
Insurance expense		200	
Interest expense		19	
Salaries expense		3,500	
Supplies expense		2,000	
Truck operation expense		700	
Income tax expense		500	
Total debits and credits		<u>\$28,144</u>	<u>\$28,144</u>

Adjusted Trial Balance at the End of a Reporting Period

Account	Account Balance	
	Debit	Credit
Cash	\$ 3,700	
Accounts receivable	2,400	
Prepaid insurance	2,200	
Equipment	3,000	
Accumulated depreciation – equipment		\$ 25
Truck	8,000	
Accumulated depreciation – truck		100
Accounts payable		700
Unearned revenue		100
Interest payable		19
Income tax payable		500
Notes payable		6,000
Common stock		10,000
Dividends	200	
Repair revenue		10,700
Depreciation expense – equipment	25	
Depreciation expense – truck	100	
Rent expense	1,600	
Insurance expense	200	
Interest expense	19	
Salaries expense	3,500	
Supplies expense	2,000	
Truck operation expense	700	
Income tax expense	500	
Total debits and credits	<u>\$28,144</u>	<u>\$28,144</u>

Asset accounts, liability accounts, and the _____ are used to prepare the balance sheet.

3

Common stock, dividends, and the _____ are used to prepare the statement of stockholders' equity.

2

Revenue and expense accounts are used to prepare the _____.

1



THE ACCOUNTING CYCLE

5.1 Describe and Prepare Closing Entries for a Business

- Closing entries: Closing entries prepare a company for the next period and zero out balance in temporary accounts.
- Purpose of closing entries: Closing entries are necessary because they help a company review income accumulation during a period, and verify data figures found on the adjusted trial balance.
- Permanent accounts: Permanent accounts do not close and are accounts that transfer balances to the next period. They include balance sheet accounts, such as assets, liabilities, and stockholder's equity
- Temporary accounts: Temporary accounts are closed at the end of each accounting period and include income statement, dividends, and income summary accounts.
- Income Summary: The Income Summary account is an intermediary between revenues and expenses, and the Retained Earnings account. It stores all the closing information for revenues and expenses, resulting in a “summary” of income or loss for the period.
- Recording closing entries: There are four closing entries; closing revenues to income summary, closing expenses to income summary, closing income summary to retained earnings, and close dividends to retained earnings.
- Posting closing entries: Once all closing entries are complete, the information is transferred to the general ledger T-accounts. Balances in temporary accounts will show a zero balance.

The Accounting Cycle:

Step 8. Closing Entries

Closing entry 1: DR CR

Closing entry 2: DR CR

Closing entry 3: DR CR

Closing entry 4: DR CR

PRINTING PLUS Adjusted Trial Balance For the Month Ended January 31, 2019		
Account Title	Debit	Credit
Cash	\$24,800	
Accounts Receivable	1,200	
Interest Receivable	140	
Supplies	400	
Equipment	3,500	
Accumulated Depreciation: Equipment		\$ 75
Accounts Payable		500
Salaries Payable		1,500
Unearned Revenue		3,400
Common Stock		20,000
Dividends	100	
Interest Revenue		140
Service Revenue		10,100
Supplies Expense	100	
Depreciation Expense: Equipment	75	
Salaries Expense	5,100	
Utility Expense	300	
Total	\$35,715	\$35,715

The Accounting Cycle:

Step 8. Closing Entries

PRINTING PLUS

Adjusted Trial Balance

For the Month Ended January 31, 2019

Account Title	Debit	Credit
Cash	\$24,800	
Accounts Receivable	1,200	
Interest Receivable	140	
Supplies	400	
Equipment	3,500	
Accumulated Depreciation: Equipment		\$ 75
Accounts Payable		500
Salaries Payable		1,500
Unearned Revenue		3,400
Common Stock		20,000
Dividends	100	
Interest Revenue		140
Service Revenue		10,100
Supplies Expense	100	
Depreciation Expense: Equipment	75	
Salaries Expense	5,100	
Utility Expense	300	
Total	<u><u>\$35,715</u></u>	<u><u>\$35,715</u></u>

Steps 9 – Prepare Post-Closing Trial Balance

PRINTING PLUS Adjusted Trial Balance For the Month Ended January 31, 2019		
Account Title	Debit	Credit
Cash	\$24,800	
Accounts Receivable	1,200	
Interest Receivable	140	
Supplies	400	
Equipment	3,500	
Accumulated Depreciation: Equipment		\$ 75
Accounts Payable		500
Salaries Payable		1,500
Unearned Revenue		3,400
Common Stock		20,000
Dividends	100	
Interest Revenue		140
Service Revenue		10,100
Supplies Expense	100	
Depreciation Expense: Equipment	75	
Salaries Expense	5,100	
Utility Expense	300	
Total	<u>\$35,715</u>	<u>\$35,715</u>

PRINTING PLUS Post-Closing Trial Balance January 31, 2019		
Account	Debit	Credit
Cash	\$24,800	
Accounts Receivable	1,200	
Interest Receivable	140	
Supplies	400	
Equipment	3,500	
Accumulated Depreciation: Equipment		\$ 75
Accounts Payable		500
Salaries Payable		1,500
Unearned Revenue		3,400
Common Stock		20,000
Retained Earnings		4,565
Total	<u>\$30,040</u>	<u>\$30,040</u>

SUMMARY

- The adjusted trial balance is used to prepare financial statements.
- Income Statement is first prepared
 - The income statement shows the net income or loss as a result of revenue and expense activities occurring in a period.
- Net income (or loss) from the income statement is used to prepare the RE part of the Statement of Owners' Equity.
 - The statement of retained earnings shows the effects of net income (loss) and dividends on the earnings the company maintains.
- Once the equity accounts are updated, together with the ledger balances of assets and liabilities from the adjusted trial balance, the Balance Sheet is prepared.
 - The balance sheet visually represents the accounting equation, showing that assets balance with liabilities and equity.



**Thank you!
Questions?**