

Completing the Accounting Cycle for a Merchandising Corporation

What You'll Learn

1. Journalize closing entries for a merchandising corporation.
2. Post closing entries to the general ledger accounts.
3. Prepare a post-closing trial balance.
4. Describe the steps in the accounting cycle.

Why It's Important

► Like a sole proprietorship, a corporation “cleans the slate” to prepare for the next accounting period.

BEFORE
You

READ

Predict

1. What does the chapter title tell you?
2. What do you already know about this subject from personal experience?
3. What have you learned about this in the earlier chapters?
4. What gaps exist in your knowledge of this subject?

Exploring the *Real World* of Business

CLOSING THE BOOKS

PETsMART

Is your pet like a member of the family? The loyalty that leads to spoiling a cat with a heated cuddle bed or purchasing vitamins for a pet iguana is what contributes to making PETsMART the leader in the retail pet food and supply industry. A strong product mix, combined with pet services like grooming and boarding, have made the company a success. PETsMART's net income has risen to \$68.1 million, more than double the earnings of its nearest competitor.

At the end of a fiscal period, companies like PETsMART prepare closing entries to transfer all temporary account balances to a permanent account. The general ledger is then ready for a new accounting period.

What Do You Think?

What might happen if temporary accounts were not closed before the next accounting period begins?



Working in the Real World

APPLYING YOUR ACCOUNTING KNOWLEDGE

You have almost completed another accounting cycle—this time for a merchandising company. After the financial statements have been prepared, closing entries are made to get the accounting records ready for the next fiscal period. Closing entries for a merchandising business are similar to those you learned about for a service business. There are just more of them.

Personal Connection

1. In your job are there duties that you perform at the end of a night or week that “wipe the slate clean” or “close out” the day’s activities?
2. If you were preparing the closing entries for your workplace, what accounts do you imagine would be involved?

Online Connection

Go to glencoeaccounting.glencoe.com and click on **Student Center**. Click on **Working in the Real World** and select **Chapter 20**.





SECTION 1

BEFORE
You

READ

Main Idea

A corporation's net income (or net loss) is closed to **Retained Earnings**.

Read to Learn...

- how to journalize closing entries for a merchandising corporation. (p. 588)
- how to journalize a net loss. (p. 591)

Journalizing Closing Entries

In Chapter 10 you journalized and posted the closing entries for a sole proprietorship service business. In this chapter you will learn to journalize and post the closing entries for a merchandising corporation. The journalizing procedures are the same.

Steps for Closing the Ledger

How Are Closing Entries for a Corporation Different from Closing Entries for a Sole Proprietorship?

In Chapter 10 you made four entries to close the temporary general ledger accounts of a sole proprietorship:

1. Close the temporary accounts with credit balances to **Income Summary**.
2. Close the temporary accounts with debit balances to **Income Summary**.

		ACCOUNT NAME	TRIAL BALANCE		ADJUSTMENTS		On Your Mark
ACCT.	NO.		DEBIT	CREDIT	DEBIT	CREDIT	
20	310	Income Summary				(a) 3 536 00	Work
21	401	Sales		320 450 00			
22	405	Sales Discounts	73 000				
23	410	Sales Returns and Allowances	2 000 000				
24	501	Purchases	206 700 00				
25	505	Transportation In	4 036 18				
26	510	Purchases Discounts		1 340 00			
27	515	Purchases Returns and Allow.		1 800 00			
28	601	Advertising Expense	2 450 00				
29	605	Bankcard Fees Expense	4 199 27				
30	630	Fed. Corporate Income Tax Exp.	9 840 00			(d) 1 550 00	
31	635	Insurance Expense				(c) 1 250 00	
32	650	Maintenance Expense	3 519 25				
33	655	Miscellaneous Expense	348 28				
34	657	Payroll Tax Expense	3 826 83				
35	660	Rent Expense	14 000 00				
36	665	Salaries Expense	29 374 60				
37	670	Supplies Expense				(b) 3 710 00	
38	680	Utilities Expense	2 364 87				
39			435 798 28	435 798 28	7 526 00	7 526 00	
40		Net Income					
41							

Figure 20–1 Closing Entries Needed for a Corporation

3. Close the balance of **Income Summary** to capital.

4. Close the withdrawals account to capital.

Only the first three closing entries are made to close the temporary accounts for a merchandising business organized as a corporation. Since a corporation does not have a withdrawals account, the fourth closing entry is not needed.

The portion of On Your Mark's work sheet in **Figure 20-1** shows the account balances that are closed. Let's look closely at each closing entry.

1. Close the accounts with balances in the Credit column of the Income Statement section of the work sheet (revenue and contra cost of merchandise accounts) to **Income Summary**. After this closing entry has been journalized and posted, the **Sales**, **Purchases Discounts**, and **Purchases Returns and Allowances** accounts have zero balances.

GENERAL JOURNAL					PAGE <u>23</u>
	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT
1	20--	<i>Closing Entries</i>			
2	Dec. 31	<i>Sales</i>		320 450 00	
3		<i>Purchases Discounts</i>		1 340 00	
4		<i>Purchases Returns and Allow.</i>		1 800 00	
5		<i>Income Summary</i>			323 590 00

Athletic Wear		Sheet		December 31, 20--	
ADJUSTED TRIAL BALANCE		INCOME STATEMENT		BALANCE SHEET	
DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
3 536 00		3 536 00			20
	320 450 00		320 450 00		21
73 000		73 000			22
2 000 000		2 000 000			23
206 700 00		206 700 00			24
4 036 18		4 036 18			25
	1 340 00		1 340 00		26
	1 800 00		1 800 00		27
2 450 000		2 450 000			28
4 199 27		4 199 27			29
9 995 00		9 995 00			30
125 00		125 00			31
3 519 25		3 519 25			32
348 28		348 28			33
3 826 83		3 826 83			34
14 000 000		14 000 000			35
29 374 60		29 374 60			36
3 710 00		3 710 00			37
2 364 87		2 364 87			38
435 953 28	435 953 28	290 915 28	323 590 00	145 038 00	112 363 28
		32 674 72			39
				32 674 72	40
		323 590 00	323 590 00	145 038 00	145 038 00

Income Summary	
Debit	Credit
Adj. 3,536.00	Clos. 323,590.00

Sales	
Debit	Credit
–	+
Clos. 320,450.00	Bal. 320,450.00

Purchases Discounts	
Debit	Credit
–	+
Clos. 1,340.00	Bal. 1,340.00

Purchases Returns and Allowances	
Debit	Credit
–	+
Clos. 1,800.00	Bal. 1,800.00

1 Close temporary accounts with balances in the Income Statement Credit column to Income Summary.

2 Close temporary accounts with balances in the Income Statement Debit column to Income Summary.

3 Close Income Summary to Retained Earnings by the amount of the net income or loss.

Figure 20-1 Closing Entries Needed for a Corporation (continued)

Income Summary	
Debit	Credit
Adj. 3,536.00	Clos. 323,590.00
Clos. 287,379.28	

Purchases	
Debit	Credit
+ 206,700.00	—
Bal. 206,700.00	Clos. 206,700.00

Bankcard Fees Expense	
Debit	Credit
+ 4,199.27	—
Bal. 4,199.27	Clos. 4,199.27

Maintenance Expense	
Debit	Credit
+ 3,519.25	—
Bal. 3,519.25	Clos. 3,519.25

Rent Expense	
Debit	Credit
+ 14,000.00	—
Bal. 14,000.00	Clos. 14,000.00

Utilities Expense	
Debit	Credit
+ 2,364.87	—
Bal. 2,364.87	Clos. 2,364.87

Sales Discounts	
Debit	Credit
+ 730.00	—
Bal. 730.00	Clos. 730.00

Transportation In	
Debit	Credit
+ 4,036.18	—
Bal. 4,036.18	Clos. 4,036.18

Federal Corporate Income Tax Expense	
Debit	Credit
+ 9,995.00	—
Bal. 9,995.00	Clos. 9,995.00

Miscellaneous Expense	
Debit	Credit
+ 348.28	—
Bal. 348.28	Clos. 348.28

Salaries Expense	
Debit	Credit
+ 29,374.60	—
Bal. 29,374.60	Clos. 29,374.60

Sales Returns and Allowances	
Debit	Credit
+ 2,000.00	—
Bal. 2,000.00	Clos. 2,000.00

Advertising Expense	
Debit	Credit
+ 2,450.00	—
Bal. 2,450.00	Clos. 2,450.00

Insurance Expense	
Debit	Credit
+ 125.00	—
Bal. 125.00	Clos. 125.00

Payroll Tax Expense	
Debit	Credit
+ 3,826.83	—
Bal. 3,826.83	Clos. 3,826.83

Supplies Expense	
Debit	Credit
+ 3,710.00	—
Bal. 3,710.00	Clos. 3,710.00

- Close the accounts with balances in the Debit column of the Income Statement section of the work sheet (contra revenue, cost of merchandise, and expense accounts) to **Income Summary**. After this closing entry has been journalized and posted, the contra revenue, cost of merchandise, and expense accounts have zero balances.

Income Summary now has a credit balance of \$32,674.72.

\$ 323,590.00	closing credit
— 3,536.00	adjustment debit
— 287,379.28	closing debit
<u>\$ 32,674.72</u>	credit balance

- Close **Income Summary** to **Retained Earnings**.

Income Summary		Retained Earnings	
Debit	Credit	Debit	Credit
Adj. 3,536.00	Clos. 323,590.00		
Clos. 287,379.28			
Clos. 32,674.72			
		Bal. 19,771.19	
		Clos. 32,674.72	
		<u>Bal. 52,445.91</u>	

After the entry to close **Income Summary** to **Retained Earnings** has been journalized and posted, **Income Summary** has a zero balance. The balance of **Retained Earnings** is increased to \$52,445.91.

GENERAL JOURNAL				PAGE <u>23</u>	
	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT
6	Dec. 31	Income Summary		287 379 28	6
7		Sales Discounts			730 00 7
8		Sales Returns and Allow.			2000 00 8
9		Purchases			206700 00 9
10		Transportation In			4036 18 10
11		Advertising Expense			2450 00 11
12		Bankcard Fees Expense			4199 27 12
13		Fed. Corp. Inc. Tax Expense			9995 00 13
14		Insurance Expense			125 00 14
15		Maintenance Expense			3519 25 15
16		Miscellaneous Expense			348 28 16
17		Payroll Tax Expense			3826 83 17
18		Rent Expense			14000 00 18
19		Salaries Expense			29374 60 19
20		Supplies Expense			3710 00 20
21		Utilities Expense			2364 87 21
22	Dec. 31	Income Summary		32674 72	22
23		Retained Earnings			32674 72 23
24					24

Closing Entry to Transfer a Net Loss

How Do You Close a Net Loss to Retained Earnings?

Sometimes businesses incur net losses. Suppose that after posting the first two entries closing the temporary accounts, the **Income Summary** account is as shown. Before it is closed, **Income Summary** has a debit balance of \$5,000.00:

$$\begin{array}{r}
 \$ 3,612.00 \text{ adjustment debit} \\
 + 65,178.00 \text{ closing debit} \\
 - 63,790.00 \text{ closing credit} \\
 \hline
 \$ 5,000.00 \text{ debit balance}
 \end{array}$$

Income Summary	
Debit	Credit
Adj. 3,612.00	Clos. 63,790.00
Clos. 65,178.00	

To close **Income Summary**, credit it for \$5,000 and debit **Retained Earnings** for \$5,000. The net loss amount *decreases* the earnings the business retains. This closing entry is recorded in the general journal as follows:

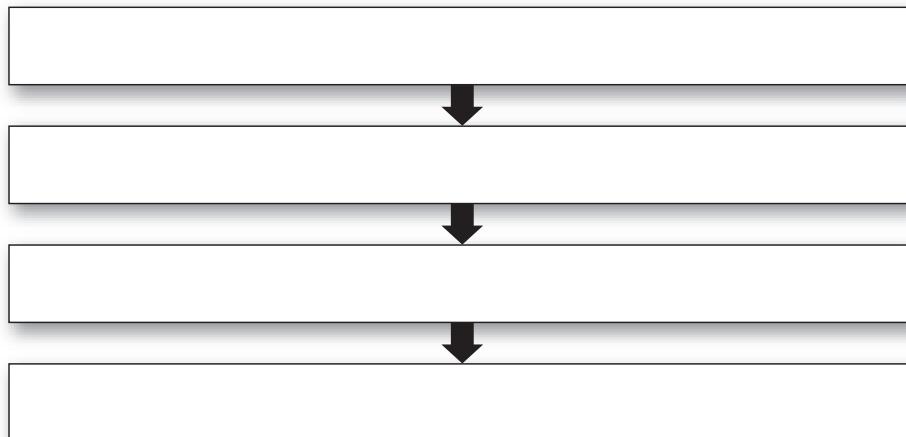
GENERAL JOURNAL				PAGE <u>23</u>	
	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT
1		Closing Entries			1
22	Dec. 31	Retained Earnings		5000 00	22
23		Income Summary			5000 00 23
24					24

As You READ
In Your Own Words

Closing In your own words, explain the concept of closing the ledger.

Reinforce the Main Idea

Using a diagram like this one, describe the step-by-step process for journalizing a merchandising corporation's closing entries. Add or remove answer boxes as needed.

Journalizing a Merchandising Corporation's Closing Entries**Do the Math**

The closing debit entry to the **Income Summary** account was \$263,000, and the closing credit entry was \$300,000. If the **Income Summary** account had a \$42,000 credit balance after these entries, was the inventory adjustment a debit or credit? What was the amount?

**Problem 20-1 Identifying Accounts Affected by Closing Entries**

The following account names appear in the chart of accounts of Larkin's Department Store.

Accounts Receivable	Purchases
Bankcard Fees Expense	Purchases Discounts
Capital Stock	Purchases Returns and Allowances
Cash in Bank	Retained Earnings
Equipment	Sales
Fed. Corp. Income Tax Expense	Sales Discounts
Fed. Corp. Income Tax Payable	Sales Returns and Allowances
Income Summary	Sales Tax Payable
Insurance Expense	Supplies
Merchandise Inventory	Supplies Expense
Miscellaneous Expense	Transportation In
Prepaid Insurance	Utilities Expense

Instructions Use the form in your working papers to answer the following questions about each account. Assume that all accounts have normal balances.

1. Is the account affected by a closing entry?
2. During closing, is the account debited or credited?
3. During closing, is **Income Summary** debited or credited?



SECTION 2

Posting Closing Entries

Closing entries recorded in the general journal are posted to the general ledger.

Closing the General Ledger

How Do You Close a Merchandising Corporation's General Ledger?

Figure 20–2 shows the portion of On Your Mark's general ledger affected by the closing process after the closing entries have been posted. Write the term *Closing Entry* (abbreviated *Clos. Ent.* here) for each posting in the Description column of the general ledger account.

ACCOUNT		<i>Retained Earnings</i>		ACCOUNT NO.		305	
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
20--							
Dec. 1	Balance	✓					19 771 19
31	Clos. Ent.	G23		32 674 72			52 445 91

ACCOUNT		Income Summary		ACCOUNT NO.		310	
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
20--							
Dec. 31	Adj. Ent.	G22	3 5 3 6 00			3 5 3 6 00	
	31	Clos. Ent.	G23		3 2 3 5 9 0 0 0		3 2 0 0 5 4 0 0
	31	Clos. Ent.	G23	2 8 7 3 7 9 2 8			3 2 6 7 4 7 2
	31	Clos. Ent.	G23	3 2 6 7 4 7 2			—

ACCOUNT <u>Sales</u>				ACCOUNT NO. <u>401</u>			
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
20--							
Dec. 1	Balance	✓					300 0 0 0 0 0
	31	S12		10 7 5 0 0 0			310 7 5 0 0 0
	31	CR13		9 7 0 0 0 0			320 4 5 0 0 0
	31	Clos. Ent.	G23	320 4 5 0 0 0			—

BEFORE You

READ

Main Idea

After posting the closing entries, prepare a post-closing trial balance.

Read to Learn...

- how to post the closing entries for a merchandising corporation. (p. 593)
- how to prepare a post-closing trial balance for a merchandising corporation. (p. 597)
- about a review of the accounting cycle for a merchandising business. (p. 598)

As You READ

Instant Recall

Posting to the General Ledger Begin with the date, and continue posting by moving from the left to the right. Remember to enter the account number in the Posting Reference column of the general journal.

Figure 20–2 Partial General Ledger at the End of the Fiscal Period

ACCOUNT *Sales Discounts*ACCOUNT NO. 405

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					700 00	
31	CR13		30 00				730 00	
31	Clos. Ent.	G23			730 00	—		

ACCOUNT *Sales Returns and Allowances*ACCOUNT NO. 410

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					1850 00	
4	G20		150 00				2000 00	
31	Clos. Ent.	G23			2000 00	—		

ACCOUNT *Purchases*ACCOUNT NO. 501

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					1900 00 00	
19	CP14		1300 00				1913 00 00	
31	P12		1540 00				2067 00 00	
31	Clos. Ent.	G23			2067 00	—		

ACCOUNT *Transportation In*ACCOUNT NO. 505

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					3761 18	
24	CP14		275 00				4036 18	
31	Clos. Ent.	G23			4036 18	—		

ACCOUNT *Purchases Discounts*ACCOUNT NO. 510

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					1200 00	
31	CP14				140 00		1340 00	
31	Clos. Ent.	G23	1340 00					

Figure 20–2 Partial General Ledger at the End of the Fiscal Period (continued)

ACCOUNT Purchases Returns and Allowances ACCOUNT NO. 515

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					1 6 0 0 0 0	
16		G21		2 0 0 0 0			1 8 0 0 0 0	
31	Clos. Ent.	G23	1 8 0 0 0 0				—	

ACCOUNT Advertising Expense ACCOUNT NO. 601

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					2 4 5 0 0 0	
31	Clos. Ent.	G23		2 4 5 0 0 0			—	

ACCOUNT Bankcard Fees Expense ACCOUNT NO. 605

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					4 1 2 4 2 7	
31		CP14	7 5 0 0				4 1 9 9 2 7	
31	Clos. Ent.	G23		4 1 9 9 2 7			—	

ACCOUNT Federal Corporate Income Tax Expense ACCOUNT NO. 630

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 1	Balance	✓					9 8 4 0 0 0	
31	Adj. Ent.	G22	1 5 5 0 0				9 9 9 5 0 0	
31	Clos. Ent.	G23		9 9 9 5 0 0			—	

ACCOUNT Insurance Expense ACCOUNT NO. 635

DATE	DESCRIPTION	POST. REF.	DEBIT		CREDIT		BALANCE	
			DEBIT	CREDIT	DEBIT	CREDIT	DEBIT	CREDIT
20--								
Dec. 31	Adj. Ent.	G22	1 2 5 0 0				1 2 5 0 0	
31	Clos. Ent.	G23		1 2 5 0 0			—	

Figure 20–2 Partial General Ledger at the End of the Fiscal Period (continued)

ACCOUNT <u>Miscellaneous Expense</u>				ACCOUNT NO. <u>655</u>			
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		CREDIT
					DEBIT	CREDIT	
20--							
Dec. 1	Balance	✓					3 2 8 28
	31	CP14	20 00				3 4 8 28
	31	Clos. Ent.	G23		3 4 8 28	—	

ACCOUNT <u>Payroll Tax Expense</u>				ACCOUNT NO. <u>657</u>			
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		CREDIT
					DEBIT	CREDIT	
20--							
Dec. 1	Balance	✓				3 8 2 6 83	
31	Clos. Ent.	G23		3 8 2 6 83	—		

ACCOUNT <u>Rent Expense</u>				ACCOUNT NO. <u>660</u>			
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		CREDIT
					DEBIT	CREDIT	
20--							
Dec. 1	Balance	✓				12 0 0 0 00	
	31	CP14	2 0 0 0 00			14 0 0 0 00	
	31	Clos. Ent.	G23	14 0 0 0 00		—	

Figure 20-2 Partial General Ledger at the End of the Fiscal Period (continued)



ACCOUNT <i>Supplies Expense</i>				ACCOUNT NO. <i>670</i>			
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		CREDIT
			DEBIT	CREDIT	DEBIT	DEBIT	
20--							
Dec. 31	Adj. Ent.	G22	3 7 1 0 00		3 7 1 0 00		
	31 Clos. Ent.	G23		3 7 1 0 00		—	

ACCOUNT <i>Utilities Expense</i>				ACCOUNT NO. <i>680</i>			
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		CREDIT
			DEBIT	CREDIT	DEBIT	DEBIT	
20--							
Dec. 1	Balance ✓					2 3 6 4 87	
	31 Clos. Ent.	G23		2 3 6 4 87		—	

Figure 20–2 Partial General Ledger at the End of the Fiscal Period (continued)

Preparing a Post-Closing Trial Balance

How Do You Prepare a Post-Closing Trial Balance?

A post-closing trial balance is prepared at the end of the accounting period to prove that the general ledger accounts are in balance after all adjusting and closing entries have been posted. Figure 20–3 shows the post-closing trial balance for On Your Mark.

On Your Mark Athletic Wear		
Post-Closing Trial Balance		
December 31, 20--		
<i>Cash in Bank</i>	15 1 7 9 00	
<i>Accounts Receivable</i>	10 4 0 4 00	
<i>Merchandise Inventory</i>	81 3 8 5 00	
<i>Supplies</i>	1 8 3 9 00	
<i>Prepaid Insurance</i>	1 3 7 5 00	
<i>Delivery Equipment</i>	19 8 3 1 00	
<i>Office Equipment</i>	9 8 2 5 00	
<i>Store Equipment</i>	5 2 0 0 00	
<i>Accounts Payable</i>		13 8 5 0 00
<i>Fed. Corp. Income Tax Payable</i>		1 5 5 00
<i>Employees' Fed. Income Tax Payable</i>		6 4 0 00
<i>Employees' State Income Tax Payable</i>		8 0 00
<i>Social Security Tax Payable</i>		2 4 8 00
<i>Medicare Tax Payable</i>		5 8 00
<i>Fed. Unemployment Tax Payable</i>		1 8 36
<i>State Unemployment Tax Payable</i>		1 1 4 73
<i>Sales Tax Payable</i>		2 4 2 8 00
<i>Capital Stock</i>		75 0 0 0 00
<i>Retained Earnings</i>		52 4 4 5 91
Totals	145 0 3 8 00	145 0 3 8 00

As You READ

Key Point

Post-Closing Trial Balance

Balance The post-closing trial balance and the balance sheet list the same account balances.

Connect to... HISTORY

After the stock market crash in 1929 and the Great Depression that followed, Congress created the Securities and Exchange Commission (SEC) in 1934 to protect investors.

Figure 20–3 Post-Closing Trial Balance

Compare and Contrast

Corporation and Sole Proprietorship How is closing the general ledger for these forms of businesses similar? How is it different?

Completing the Accounting Cycle for a Merchandising Business

What Is the Accounting Cycle for a Merchandising Business?

You have completed the study of the accounting cycle for a merchandising business organized as a corporation, which consists of the following steps:

1. Collect and verify source documents.
2. Analyze each business transaction.
3. Journalize each transaction.
4. Post to the general and subsidiary ledgers.
5. Prepare a trial balance.
6. Complete a work sheet.
7. Prepare the financial statements—income statement, statement of retained earnings, and balance sheet. Publicly held corporations also prepare a statement of cash flows.
8. Journalize and post the adjusting entries.
9. Journalize and post the closing entries.
10. Prepare a post-closing trial balance.

The accounting cycle for a service and a manufacturing business follows the same steps. Also, regardless of how a business is organized—sole proprietorship, partnership, or corporation—the basic steps of the accounting cycle are the same. **Figure 20–4** illustrates the accounting cycle.

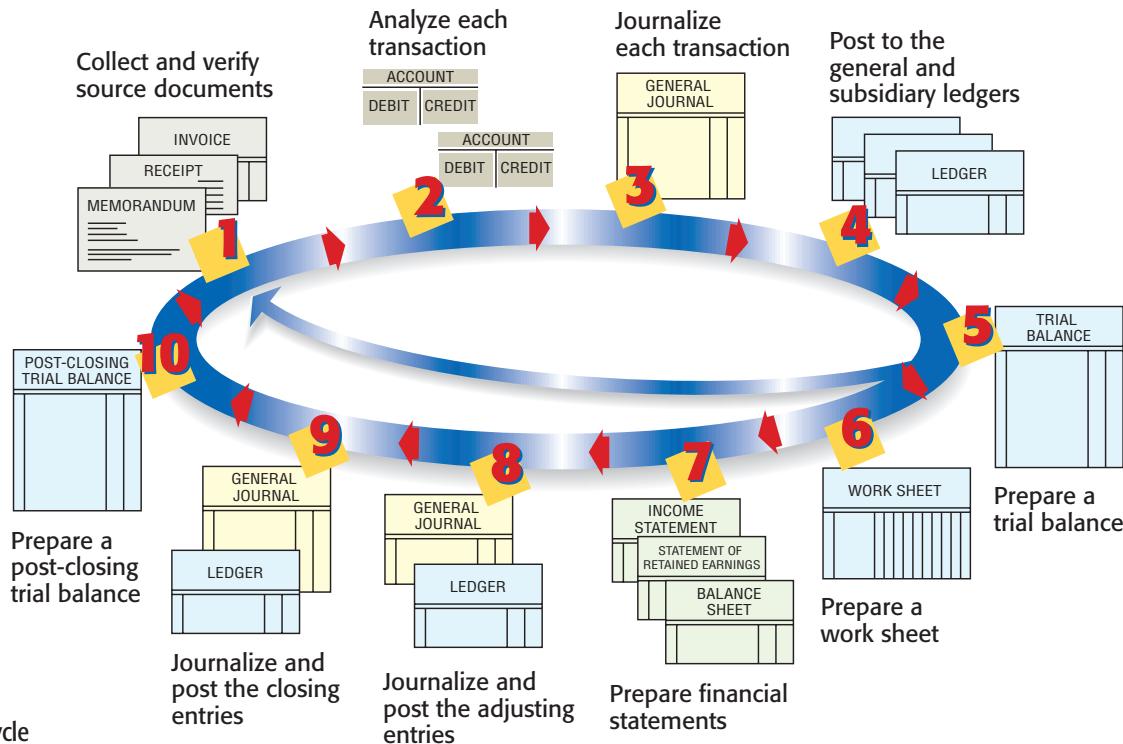
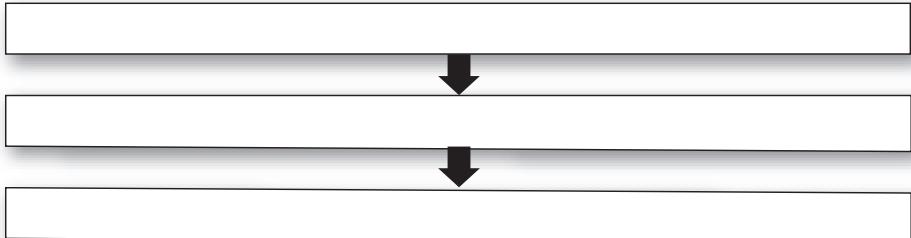


Figure 20–4
The Accounting Cycle

The accounting system used, whether manual or computerized, does not affect the steps in the accounting cycle. In a computerized accounting system, however, the computer performs many of the routine procedures such as posting.

Reinforce the Main Idea

Using a diagram like this one, describe the step-by-step process for posting a merchandising corporation's closing entries. Add or remove answer boxes as needed.

Posting a Merchandising Corporation's Closing Entries**Do the Math**

Totals on the post-closing trial balance were assets, \$156,000, and liabilities, \$75,000. If the ending balance of **Retained Earnings** was \$45,000, what was the capital stock account's ending balance?

**Problem 20–2 Analyzing a Source Document**

Instructions Review the source document and prepare the journal entry to record this transaction in your working papers. Your Backpack Inc. uses a cash payments journal to record disbursements.

**Problem 20–3 Organizing the Steps in the Accounting Cycle**

Instructions List the following steps of the accounting cycle in their proper order. Use the form provided in your working papers or a separate sheet of paper.

- Analyzing business transactions
- Collecting and verifying source documents
- Completing the work sheet
- Journalizing business transactions
- Journalizing and posting adjusting entries

- Journalizing and posting closing entries
- Posting journal entries to ledgers
- Preparing financial statements
- Preparing a post-closing trial balance
- Preparing a trial balance

Key Concepts

1. The information for journalizing closing entries comes from the Income Statement section of the work sheet. Only three steps are necessary to close the temporary accounts of a corporate merchandising business.

a. Close all temporary accounts with credit balances to **Income Summary**.

GENERAL JOURNAL					PAGE <u>XX</u>
	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT
1	20--	<i>Closing Entries</i>			
2	<i>Date</i>	<i>Sales</i>		<i>xx xxx xx</i>	
3		<i>Purchases Discounts</i>		<i>xx xxx xx</i>	
4		<i>Purchases Returns and Allow.</i>		<i>xx xxx xx</i>	
5		<i>Income Summary</i>			<i>xx xxx xx</i>
6					

b. Close all temporary accounts with debit balances to **Income Summary**.

GENERAL JOURNAL					PAGE <u>XX</u>
	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT
6	<i>Date</i>	<i>Income Summary</i>		<i>xx x x x xx</i>	
7		<i>Sales Discounts</i>			<i>x x x xx</i>
8		<i>Sales Returns and Allow.</i>			<i>x x x xx</i>
9		<i>Purchases</i>			<i>x x x xx</i>
10		<i>Transportation In</i>			<i>x x x xx</i>
11		<i>Expense Account</i>			<i>x x x xx</i>
12		<i>Expense Account</i>			<i>x x x xx</i>
13		<i>Expense Account</i>			<i>x x x xx</i>
14					

c. Close the balance of **Income Summary** to the **Retained Earnings** account.

GENERAL JOURNAL					PAGE <u>XX</u>
	DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT
1		<i>Closing Entries</i>			
22	<i>Date</i>	<i>Income Summary</i>		<i>x x x x xx</i>	
23		<i>Retained Earnings</i>			<i>x x x x xx</i>
24					

2. After you have recorded closing entries in the general journal, post them to the general ledger. Write *Closing Entry* in the Description column of the general ledger account. Refer to **Figure 20–2** on pages 593–597 to review a partial general ledger at the end of the accounting period.

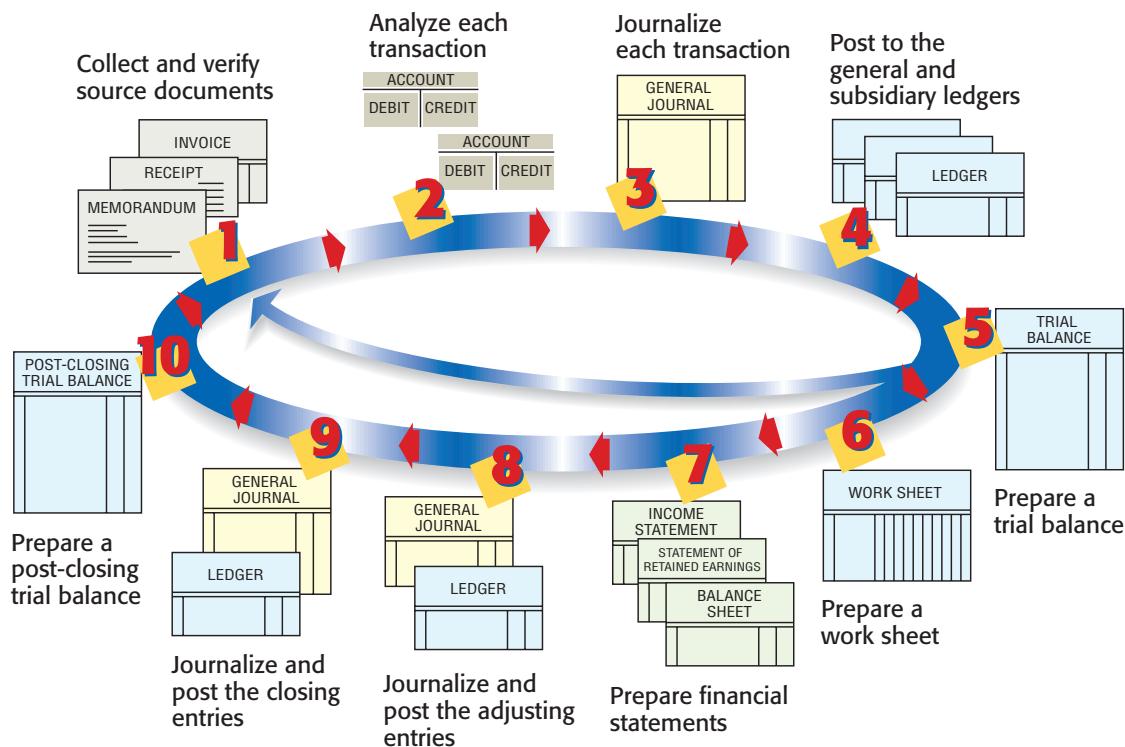
3. A post-closing trial balance is prepared at the end of the accounting period to prove that the general ledger accounts are in balance, that is, their debits equal their credits. The following is an example of a post-closing trial balance.

On Your Mark Athletic Wear Post-Closing Trial Balance December 31, 20--		
Cash in Bank	15 179 00	
Accounts Receivable	10 404 00	
Merchandise Inventory	81 385 00	
Supplies	1 839 00	
Prepaid Insurance	1 375 00	
Delivery Equipment	19 831 00	
Office Equipment	9 825 00	
Store Equipment	5 200 00	
Accounts Payable		13 850 00
Fed. Corp. Income Tax Payable		1 550 00
Employees' Fed. Income Tax Payable		6 400 00
Employees' State Income Tax Payable		80 00
Social Security Tax Payable		2 480 00
Medicare Tax Payable		58 00
Fed. Unemployment Tax Payable		18 36
State Unemployment Tax Payable		1 147 3
Sales Tax Payable		2 428 00
Capital Stock		75 000 00
Retained Earnings		52 445 91
Totals	145 038 00	145 038 00

4. The basic accounting cycle is the same whether

- the business is a service provider or merchandiser
- the business is organized as a sole proprietorship, corporation, or partnership
- the business uses a manual or computerized accounting system

The following illustrates the complete accounting cycle.



AFTER
YOU

READ

Check Your Understanding

1. **Journalizing the Closing Entries**
 - a. Which account(s) are used to close temporary accounts with debit and credit balances?
 - b. How are temporary accounts with debit balances closed?
2. **Posting the Closing Entries**
 - a. What is written in the Description column of the general ledger account as the closing entries are posted?
 - b. What is entered in the Posting Reference column of the general ledger account?
3. **Post-Closing Trial Balance**
 - a. What is the purpose of preparing a post-closing trial balance?
 - b. Does the **Income Summary** account appear on the post-closing trial balance? Why or why not?
4. **Accounting Cycle**
 - a. Name the 10 steps in the accounting cycle.
 - b. Which tasks in the accounting cycle are performed automatically in a computerized accounting system?

Apply Key Terms

The following key terms were introduced in Chapter 10. Let's review the terms as they relate to a merchandising corporation such as PETsMART. What differences exist between the closing entries for a sole proprietorship and the closing entries for a merchandising corporation? Use the following terms in your explanation.

closing entries
permanent accounts

temporary accounts



Closing the Fiscal Year

Making the Transition from a Manual to a Computerized System

Task	Manual Methods	Computerized Methods
Closing a fiscal year	<ul style="list-style-type: none"> Journalize the entries to close the revenue, expense, Income Summary, and Withdrawals accounts. Post the closing entries. 	<ul style="list-style-type: none"> Closing the fiscal year is performed only if you want to clear income and expense accounts at the end of the fiscal year. If you have selected the closing option, the software journalizes closing entries.
Preparing a post-closing trial balance	<ul style="list-style-type: none"> After the closing entries have been posted to the ledger, prepare a trial balance to verify the equality of debits and credits. All expense and revenue accounts should have zero balances. 	<ul style="list-style-type: none"> A post-closing trial balance can be printed to verify that all revenue and expense accounts have been closed.



Peachtree® Q & A

Peachtree Question	Answer
What tasks should I perform before closing a fiscal year?	<ol style="list-style-type: none"> Post and print all journal entries and reports before you close the fiscal year. Back up all files before closing. Closing the fiscal year cannot be reversed.
How do I close the fiscal year?	<ol style="list-style-type: none"> From the Tasks menu, select System. Choose Year-End Wizard. You will be prompted if any procedures need to be completed before the system continues the closing process.



QuickBooks Q & A

QuickBooks Question	Answer
What tasks should I perform before closing a fiscal year?	<ol style="list-style-type: none"> Post and print all journal entries and reports before you close the fiscal year. Back up the company file before closing.
How do I close the fiscal year?	<ol style="list-style-type: none"> From the Company menu, select Set Up Users. Click Closing Date. Enter the date on which you want to close your books and enter a password.

For detailed instructions, see your Glencoe Accounting Chapter Study Guides and Working Papers.

Complete problems using:

Manual Glencoe
Working Papers OR Peachtree Complete
Accounting Software OR QuickBooks
Templates OR Spreadsheet
Templates**Peachtree®****SMART GUIDE****Step-by-Step Instructions:****Problem 20-4**

1. Select the problem set for Sunset Surfwear (Prob. 20-4).
2. Rename the company and set the system date.
3. Choose **System** from the **Tasks** menu and then select **Year-End Wizard** to close the fiscal year.
4. Print a post-closing trial balance.
5. Complete the Analyze activity.
6. End the session.

TIP: Choose the General Ledger Trial Balance report whenever you are instructed to print a Post-Closing Trial Balance.

Problem 20-4 Journalizing Closing Entries

The following amounts appeared in the Income Statement section of Sunset Surfwear's work sheet.

Instructions In your working papers, record the closing entries for the year ended December 31. Start with general journal page 13.

ACCT. NO.	ACCOUNT NAME	INCOME STATEMENT	
		DEBIT	CREDIT
13 310	Income Summary		7 000 000
14 401	Sales		90 000 000
15 405	Sales Discounts	1 000 000	
16 410	Sales Returns and Allowances	2 400 000	
17 501	Purchases	25 000 000	
18 505	Transportation In	3 000 000	
19 510	Purchases Discounts		50 000
20 515	Purchases Returns and Allowances		1 500 000
21 625	Federal Corporate Income Tax Exp.	5 532 000	
22 635	Insurance Expense	300 000	
23 650	Miscellaneous Expense	6 000 000	
24 655	Rent Expense	12 000 000	
25 665	Supplies Expense	45 000	
26 675	Utilities Expense	14 000 000	
27		69 682 000	99 000 000
28	Net Income	29 318 000	
29		99 000 000	99 000 000
30			

Analyze

Identify the effect of the closing entries on the Retained Earnings account.

Problem 20-5 Journalizing and Posting Closing Entries

The following account balances appeared in the Income Statement section of the work sheet of Shutterbug Cameras.

Instructions

1. Journalize the closing entries for the year ended December 31. Start with page 14 of a general journal (in your working papers).
2. Post the closing entries to the general ledger accounts, which are included in your working papers.

ACCT. NO.	ACCOUNT NAME	INCOME STATEMENT	
		DEBIT	CREDIT
20	310 Income Summary	4 000 000	
21	401 Sales		150 000 000
22	410 Sales Returns and Allowances	5 000 000	
23	501 Purchases	90 000 000	
24	505 Transportation In	5 000 000	
25	510 Purchases Discounts		1 000 000
26	515 Purchases Returns and Allowances		1 500 000
27	620 Federal Corporate Income Tax Exp.	4 700 000	
28	645 Miscellaneous Expense	300 000	
29	650 Rent Expense	6 000 000	
30	660 Supplies Expense	1 630 000	
31	670 Utilities Expense	3 000 000	
32		119 630 000	152 500 000
33	Net Income	32 870 000	
34		152 500 000	152 500 000
35			

Analyze

Describe what would happen if the accountant for Shutterbug Cameras made a mistake and did not close the Transportation In account.

Problem 20-6 Identifying Accounts for Closing Entries

A partial list of the accounts used by Cycle Tech Bicycles appears on page 606. All of the accounts have nonzero balances.

Peachtree®

SMART GUIDE

Step-by-Step Instructions:

Problem 20-5

1. Select the problem set for Shutterbug Cameras (Prob. 20-5).
2. Rename the company and set the system date.
3. Close the fiscal year.
4. Print a post-closing trial balance.
5. Complete the Analyze activity.
6. End the session.

QuickBooks

PROBLEM GUIDE

Step-by-Step Instructions:

Problem 20-5

1. Restore the Problem 20-5.QBB file.
2. Enter the closing entries.
3. Print a post-closing trial balance.
4. Complete the Analyze activity.
5. Back up your work.

CONTINUE 

Peachtree®

SMART GUIDE

Step-by-Step Instructions:
Problem 20-6

1. Select the problem set for Cycle Tech Bicycles (Prob. 20-6).
2. Rename the company and set the system date.
3. Print a Chart of Accounts report.
4. List the accounts that will be debited and those that will be credited when closed.
5. Complete the Analyze activity.
6. End the session.

General Ledger

- 101 Cash in Bank
- 650 Miscellaneous Expense
- 125 Merchandise Inventory
- 665 Supplies Expense
- 215 Sales Tax Payable
- 505 Transportation In
- 305 Retained Earnings
- 401 Sales
- 405 Sales Discounts
- 310 Income Summary
- 501 Purchases
- 515 Purchases Returns and Allowances
- 601 Advertising Expense
- 625 Federal Corporate Income Tax Expense
- 657 Rent Expense
- 135 Prepaid Insurance

Instructions In your working papers, list all account numbers and names for accounts that will be debited when closed. Next, list all account numbers and names for accounts that will be credited when closed.

Analyze

Examine your list. Determine whether it contains all of the accounts. If it does not, explain why.

SPREADSHEET
SMART GUIDEStep-by-Step Instructions:
Problem 20-7

1. Select the spreadsheet template for Problem 20-7.
2. Enter your name and the date in the spaces provided on the template.
3. Complete the spreadsheet using the instructions in your working papers.
4. Print the spreadsheet and proof your work.
5. Complete the Analyze activity.
6. Save your work and exit the spreadsheet

Problem 20-7 Completing End-of-Period Activities

The general ledger accounts for River's Edge Canoe & Kayak as of December 31, the end of the period, appear in the working papers.

Instructions In your working papers:

1. Prepare a trial balance on a ten-column work sheet.
2. Complete the work sheet. Use the following adjustment information.

Merchandise inventory, December 31	\$20,000
Supplies inventory, December 31	900
Unexpired insurance, December 31	1,800
Total federal corporate income taxes for the year	2,965

3. Prepare an income statement from the work sheet information.
4. Prepare a statement of retained earnings.
5. Prepare a balance sheet.
6. Journalize and post the adjusting entries. Begin on general journal page 14.
7. Journalize and post the closing entries.
8. Prepare a post-closing trial balance.

Analyze

Conclude whether the company made a profit for the year.



Problem 20-8 Preparing Adjusting and Closing Entries

In the middle of the end-of-period activities, the accountant for Buzz Newsstand was called away because of an illness in the family. Before leaving, the accountant prepared the work sheet and the financial statements. However, the business manager can locate only the trial balance shown here (before adjustments) and the income statement shown on page 608.

Instructions In your working papers:

1. Journalize the adjusting and closing entries on page 16 of the general journal.
2. Using the information provided, prepare a post-closing trial balance.

Buzz Newsstand					
Trial Balance, Before Adjustments					
December 31, 20--					
101	Cash in Bank	12	0 3 5 00		
115	Accounts Receivable	6	1 0 6 00		
130	Merchandise Inventory	64	8 0 0 00		
135	Supplies	3	9 1 6 00		
140	Prepaid Insurance	5	4 0 0 00		
145	Delivery Truck	46	1 0 6 00		
201	Accounts Payable			4	6 9 0 00
204	Fed. Corp. Income Tax Pay.			—	
215	Sales Tax Payable			4	1 6 00
301	Capital Stock			40	0 0 0 00
305	Retained Earnings			24	6 0 3 00
310	Income Summary				
401	Sales			299	1 5 6 00
410	Sales Returns and Allowances	9	5 0 0 00		
501	Purchases	168	6 2 4 00		
505	Transportation In	8	2 3 6 00		
510	Purchases Discounts			2	9 5 0 00
515	Purchases Returns and Allowances			2	1 0 8 00
601	Advertising Expense	4	0 0 0 00		
625	Fed. Corp. Income Tax Expense	12	5 0 0 00		
635	Insurance Expense	—	—		
650	Miscellaneous Expense	1	6 0 0 00		
660	Salaries Expense	26	9 0 0 00		
665	Supplies Expense	—	—		
675	Utilities Expense	4	2 0 0 00		
	Totals	373	9 2 3 00	373	9 2 3 00

Peachtree®

SMART GUIDE

Step-by-Step Instructions:

Problem 20-8

1. Select the problem set for Buzz Newsstand (Prob. 20-8).
2. Rename the company and set the system date.
3. Print a Working Trial Balance to help you prepare the adjustments.
4. Record the adjustments using the **General Journal Entry** option.
5. Print a General Journal report and proof your work.
6. Complete the Analyze activity.
7. Close the fiscal year.
8. Print a post-closing trial balance.
9. End the session.

TIP: Peachtree automatically updates the general ledger accounts when you close the fiscal year.

QuickBooks

PROBLEM GUIDE

Step-by-Step Instructions:

Problem 20-8

1. Restore the Problem 20-8.QBB file.
2. Print a Trial Balance.
3. Record the adjustments.
4. Print a Journal report.
5. Complete the Analyze activity.
6. Enter the closing entries.
7. Print a post-closing trial balance.
8. Back up your work.

CONTINUE

Buzz Newsstand		
Income Statement		
For the Year Ended December 31, 20--		
<i>Revenue:</i>		
Sales	299 156 00	
Less: Sales Ret. and Allow.	<u>9 500 00</u>	
Net Sales	289 656 00	
<i>Cost of Merch. Sold:</i>		
Merch. Inv., Jan 1, 20--	64 800 00	
Purchases	168 624 00	
Plus: Transportation In	<u>8 236 00</u>	
Cost of Del. Merch.	176 860 00	
Less: Purch. Discounts	2 950 00	
Purch. Ret. and Allow.	<u>2 108 00</u>	5 058 00
Net Purchases	171 802 00	
Cost of Merch. Avail.	236 602 00	
Merch. Inv., Dec. 31, 20--	<u>60 400 00</u>	
Cost of Merch. Sold	176 202 00	
Gross Profit on Sales		113 454 00
<i>Operating Expenses:</i>		
Advertising Expense	4 000 00	
Insurance Expense	1 800 00	
Miscellaneous Expense	1 600 00	
Salaries Expense	26 900 00	
Supplies Expense	2 744 00	
Utilities Expense	4 200 00	
Total Oper. Expenses		41 244 00
Operating Income		72 210 00
Less: Fed. Inc. Tax Exp.		14 913 00
Net Income		<u>57 297 00</u>

Analyze Determine the impact of adjusting entries on net income.

Practice your test-taking skills! The questions on this page are reprinted with permission from national organizations:

- Future Business Leaders of America
- Business Professionals of America

Use a separate sheet of paper to record your answers.



Future Business Leaders of America

MULTIPLE CHOICE

1. Closing entries for a corporation are made from information in a work sheet's
 - a. Trial Balance columns.
 - b. Adjustments columns.
 - c. Income Statement columns.
 - d. Balance Sheet columns.
 - e. none of these answers
2. The procedure for transferring information from a journal to ledger accounts is called
 - a. journalizing.
 - b. adjusting.
 - c. file maintenance.
 - d. posting.
 - e. none of these answers
3. Proving the accuracy of the adjusting and closing entries is best defined as
 - a. preparing a post-closing trial balance.
 - b. preparing the statements.
 - c. closing the temporary accounts.
 - d. adjusting the ledger accounts.
 - e. none of these answers
4. To close the Income Summary account of a corporation with a net loss, the balance is closed into the
 - a. Retained Earnings account with a debit.
 - b. Retained Earnings account with a credit.
 - c. account which caused the net loss with a debit.
 - d. none of the above



Business Professionals of America

MULTIPLE CHOICE

5. Which of the following accounts is closed at the end of a fiscal period?
 - a. Membership Fees Income
 - b. Accounts Receivable
 - c. Delivery Equipment
 - d. Retained Earnings

Need More Help?

Go to glencoeaccounting.glencoe.com and click on Student Center. Click on Winning Competitive Events and select Chapter 20.

- Practice Questions and Test-Taking Tips
- Concept Capsules and Terminology



CRITICAL
Thinking**CASE**
STUDY**Matter of**
ETHICS**Completing the Accounting Cycle**

1. What is the source of information for journalizing the closing entries?
2. How are temporary accounts with credit balances closed?
3. Describe the journal entry to record a net loss.
4. Analyze the closing of the **Income Summary** and **Retained Earnings** accounts when the business has net income and when it has a net loss.
5. Create a memory device to help you remember all the closing entries for a corporation.
6. Justify the use of only three closing entries for a corporation although a sole proprietorship uses four.

Merchandising Business: Department Store

You work in the accounting department for Pearl's, a trendy department store. The accounting manager asked you to review the work of an accounting intern who completed the closing process. Some temporary accounts in the post-closing trial balance still have balances.

INSTRUCTIONS

1. Explain how to tell which accounts should have zero balances after closing.
2. Explain how to determine which accounts have and have not been closed.
3. Suggest ways to explain to the intern why temporary accounts have zero balances after closing.
4. List human-relations skills you might use in your explanation to the intern.

Handling Sales Returns

Most retail stores give employees specific instructions on how to process a sales return. For example, a cash refund can only be given if cash was paid. Imagine that you work for a large sporting goods store like The Sports Authority. Your friend, Martin, comes in to return a sweatshirt he purchased recently. You know he purchased the sweatshirt on sale, but he wants you to give him a full refund.

ETHICAL DECISION MAKING

1. What are the ethical issues?	4. How do the alternatives affect the parties?
2. What are the alternatives?	5. What would you do?
3. Who are the affected parties?	

Explaining Results

As you are completing the closing entries for the fourth quarter, you realize that your company, Dynamic Sound, has a net loss. You know that management is not aware that the fourth quarter financial statements are so bleak. Select a partner from your class and role-play an explanation of how the **Income Summary** and **Retained Earnings** accounts are affected by the loss. In your explanation, model customer service principles of accuracy, thoroughness, and respect.



Maintaining and Troubleshooting Technologies

In the accounting department of KidsWear Inc., you process the closing entries. This morning the printer will not print the ledgers or journals.

INSTRUCTIONS

List the steps you need to take to troubleshoot this problem. For each step indicate whom to call if the problem is not resolved.



Number Conventions

Many countries use decimal points instead of commas to separate thousands and use a comma instead of a decimal point as a decimal marker. For example the number 45,255.08 becomes 45.255,08.

INSTRUCTIONS Convert these numbers: (1) 121,309,411.98 (2) 74,520.229



Your Stocks

Your future savings may include stock. Your stock investment becomes an asset for you and part of stockholders' equity for the company.

PERSONAL FINANCE ACTIVITY Choose a company to investigate as an investment. List how you could find the stock's current price.

PERSONAL FINANCE ONLINE Go to glencoeaccounting.glencoe.com and click on Student Center. Click on Making It Personal and select Chapter 20.



Calculating Return on Stockholders' Equity

One measure of a corporation's profitability is the return on stockholders' equity. It shows how much the business earned for each dollar invested by stockholders.

$$\frac{\text{Net Income}}{\text{Average Stockholders' Equity}} = \frac{\$20,990}{\$200,832} = 0.1045 \text{ or } 10.45\%$$

Average stockholders' equity = (beginning stockholders' equity + ending stockholders' equity) \div 2.

INSTRUCTIONS

Use PETsMART's financial statements in Appendix F to complete the following.

1. Calculate the return on stockholders' equity for the year ending February 1, 2004.
2. Explain why you think this calculation is important to potential buyers of a company's stock.



Closing the Books

How do business activities affect net income or net loss? Visit glencoeaccounting.glencoe.com and click on Student Center. Click on WebQuest and select Unit 4 to continue your Internet project.

