

Name: _____

Lesson 8-1: Recording Closing Entries

Objectives: LO1: Journalize and post closing entries for a service business organized as a proprietorship.

A. Need for Permanent and Temporary Accounts

- Permanent accounts: Accounts used to accumulate information until it is transferred to the owner's capital account
 - AKA? nominal accounts
 - The ending account balance of permanent accounts for one fiscal period are the beginning account balances for the next fiscal period.
- Temporary accounts: Accounts used to accumulate information until it is transferred to the owner's capital account
 - AKA? nominal accounts
 - Which four accounts/account types are temporary?
 1. Revenue
 2. Expenses
 3. Drawing
 4. Income Summary
 - ***Remember, these are all "subdivisions" of Owner's Equity (except Income Summary)**
 - Temporary accounts show change in owner's capital account for a single fiscal period.
 - At the end of the fiscal period, temporary accounts are zeroed out and transferred to the capital account.
 - Temporary accounts began a new fiscal period with what balance? \$0.00

B. Need for Closing Temporary Accounts

- Closing entries: Journal entries used to prepare temporary accounts for a new fiscal period
- Remember, temporary account balances must be at ZERO to start a new fiscal period.
 - Because of this, we must CLOSE the accounts (transfer the balances to Owner's Equity)
- To close a temporary account, an amount equal is recorded in the account on the side opposite of the balance.
 - Example. If an account has a DEBIT of \$3500, what would we do to ZERO it out? CREDIT \$350
- Just like GRADES are recorded, and started as a clean slate every semester, so are TEMPORARY ACOCUNTS.

C. Need for Income Summary Account

Income Summary	
Debit	Credit
Total expenses	Revenue (greater than expenses) (Credit balance is the net income.)

Income Summary	
Debit	Credit
Total expenses (greater than revenue) (Debit balance is the net loss.)	Revenue

- Whenever a temporary account is closed, the closing entry must have equal debits and credits.
- A temporary account named Income Summary is used to summarize the closing entries for revenue and expense accounts.
- Why is the Income Summary account unique? Has no “normal” balance – can be debit or credit balance
- If Revenue is greater than Expenses, the Income Summary account will have a Credit balance.
- If Expenses are greater than Revenue, the Income Summary account will have a Debit balance.
- What are the four closing entries?
 1. _____
 2. _____
 3. _____
 4. _____
- We get the information for our closing entries from the Work Sheet (BS and IS columns)

D. Closing Entry for an Income Statement Account with a Credit Balance

The diagram illustrates the process of closing the Income Statement. It shows three main components: the Income Statement, the General Journal, and the Income Summary account.

- Income Statement:** A table with columns for 'S' (Sales) and 'E' (Expenses). The 'Sales' row shows a value of 5,820.00. The 'Expenses' row shows a value of 0.00. The total is 5,820.00.
- General Journal:** A table with columns for 'DATE', 'ACCOUNT TITLE', 'DOC. NO.', 'POST. REF.', 'DEBIT', and 'CREDIT'. The 'Closing Entries' section shows the following entries:

DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT
31	Sales			5,820.00	
	Income Summary				5,820.00
- Income Summary:** A table with columns for 'DATE', 'ACCOUNT TITLE', 'DOC. NO.', 'POST. REF.', 'DEBIT', and 'CREDIT'. The 'Income Summary' row shows a value of 5,820.00.

Arrows indicate the flow of data: from the 'Sales' row in the Income Statement to the 'Sales' row in the General Journal, and from the 'Income Summary' row in the General Journal to the 'Income Summary' row in the Income Summary account. The 'Closing Entries' section in the General Journal is labeled 'Closing Entries'.

Sales			
Closing	5,820.00	bal.	5,820.00
		(New Bal.	0.00)

Income Summary	
	Closing (revenue) 5,820.00

- Which account on the Income Statement has a Credit balance? **Sales**
- What account do we use to CLOSE our temporary accounts? **Income Summary**

- List the four steps of completing the closing entry for Sales:
 1. Write heading "Closing Entries" in the middle of the next blank line
 2. Write the date (last day of fiscal period)
 3. Write Sales and Debit the account balance
 4. Write Income Summary and Credit the account balance of Sales

E. Closing Entry for Income Statement Accounts with a Debit Balance

ACCOUNT TITLE		INCOME STATEMENT	
		DEBIT	CREDIT
13 Advertising Expense		397.00	
14 Cash Short and Over		1.00	
15 Communications Expense		80.00	
16 Equipment Rental Expense		1,455.00	
17 Insurance Expense		150.00	
18 Miscellaneous Expense		45.00	
19 Supplies Expense		530.00	

(Credit to close)

Date	Income Summary	Debit Amount
31	Income Summary	2,658.00
	Advertising Expense	397.00
	Cash Short and Over	1.00
	Communications Expense	80.00
	Equipment Rental Expense	1,455.00
	Insurance Expense	150.00
	Miscellaneous Expense	45.00
	Supplies Expense	530.00

Credit

Income Summary		Equipment Rental Expense	
Closing (expenses)	2,658.00	Closing (revenue)	5,820.00
		(New Bal.)	3,162.00
		(New Bal.)	0.00
		Closing	1,455.00

Advertising Expense		Insurance Expense	
Bal.	397.00	Bal.	150.00
(New Bal.)	0.00	(New Bal.)	0.00
Closing	397.00	Closing	150.00

Cash Short and Over		Miscellaneous Expense	
Bal.	1.00	Bal.	45.00
(New Bal.)	0.00	(New Bal.)	0.00
Closing	1.00	Closing	45.00

Communications Expense		Supplies Expense	
Bal.	80.00	Bal.	530.00
(New Bal.)	0.00	(New Bal.)	0.00
Closing	80.00	Closing	530.00

- We use the same steps as above to close the Debit Balance (expense) accounts, EXCEPT we **DEBIT/CREDIT** (circle one) Income Summary instead.
- After we close the Credit (Sales) accounts and debit (Expense) Accounts, we are left with our NET LOSS/INCOME in the INCOME SUMMARY account...this is the difference between the **Revenue** and **Expense** accounts.

F. Closing Entry to Record Net Income/Loss and Close Income Summary Account

ACCOUNT TITLE		INCOME STATEMENT	
		DEBIT	CREDIT
20		2 6 5 8 00	5 8 2 0 00
21	Net Income	3 1 6 2 00	
22		5 8 2 0 00	5 8 2 0 00

GENERAL JOURNAL						PAGE 3	
DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT		
31	Income Summary			3 1 6 2 00			
	Michael Delgado, Capital				3 1 6 2 00		

Income Summary			
Closing (expenses)	2,658.00	Closing (revenue)	5,820.00
Closing	3,162.00	(New Bal.)	0.00

Michael Delgado, Capital	
Bal.	2,000.00
Closing (net inc.)	3,162.00
(New Bal.)	5,162.00

- If the company has Net Income, Income Summary is _____ to close it and the capital account is _____ to increase it.
- If the company has a Net Loss, Income Summary is _____ to close it and the capital account is _____ to decrease it. (HINT: OPPOSITE OF ABOVE)

G. Closing Entry for the Owner's Drawing Account

ACCOUNT TITLE		BALANCE SHEET	
		DEBIT	CREDIT
9	Michael Delgado, Capital		2 0 0 0 00
10	Michael Delgado, Drawing	1 1 5 0 00	

GENERAL JOURNAL						PAGE 3	
DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT		
31	Michael Delgado, Capital			1 1 5 0 00			
	Michael Delgado, Drawing				1 1 5 0 00		

Michael Delgado, Capital			
Closing (drawing)	1,150.00	Bal.	2,000.00
		Net Income	3,162.00
		(New Bal.)	4,012.00

Michael Delgado, Drawing	
Bal.	1,150.00
(New Bal.)	0.00
Closing	1,150.00

- Remember, withdrawals **reduce** the amount of the owner's equity.
- Since the Drawing account is neither an expense nor revenue, we do not use Income Summary to close it. Instead, we close it **directly to the capital account**.

Check yourself!

1. What do the ending balances of permanent accounts for one fiscal period represent at the beginning of the next fiscal period?

Beginning balances

2. What do the balances of temporary accounts show?

Changes in the owner's capital account for a single fiscal period

3. List the four closing entries.

1. An entry to close income statement accounts with credit balances.
2. An entry to close income statement accounts with debit balances.
3. An entry to record net income or net loss and close the Income Summary account.
4. An entry to close the owner's drawing account

Lesson 8-2: Preparing a Post-Closing Trial Balance

Objectives: L03: Prepare a post-closing trial balance.

A. General Ledger Accounts After Closing Entries are Posted

- How do we signify that an account has a zero balance in the general ledger? Line through both debit and credit balance columns
- WHY do we do this?

So there is no question that we forgot to enter data

ACCOUNT <i>Income Summary</i>										ACCOUNT NO. 330									
DATE		ITEM	POST. REF.	DEBIT				CREDIT				BALANCE							
												DEBIT				CREDIT			
Jan.	31		G3					5	8	2	0	0	0	0		5	8	2	0
	31		G3	2	6	5	8	0	0							3	1	6	2
	31		G3	3	1	6	2	0	0										
ACCOUNT <i>Sales</i>										ACCOUNT NO. 410									
DATE		ITEM	POST. REF.	DEBIT				CREDIT				BALANCE							
												DEBIT				CREDIT			
Jan.	10		G1					1	1	0	0	0	0			1	1	0	0
	12		G1					5	0	0	0					1	6	0	0
	16		G1					4	0	0	0					2	0	0	0
	18		G1					5	3	5	0					2	5	3	5
	24		G2					1	3	2	0					3	8	5	5
	29		G2					1	2	8	0					5	1	3	5
	31		G2					6	8	5	0					5	8	2	0
	31		G3	5	8	2	0	0	0										
ACCOUNT <i>Advertising Expense</i>										ACCOUNT NO. 510									
DATE		ITEM	POST. REF.	DEBIT				CREDIT				BALANCE							
												DEBIT				CREDIT			
Jan.	17		G1	3	8	3	0	0				3	8	3	0				
	31		G2	1	4	0	0					3	9	7	0				
	31		G3					3	9	7	0								

B. Post-Closing Trial Balance

1 Heading

2 Account Titles

3 Account Balances

4 Single Rule

5 Compare Totals

6 Totals

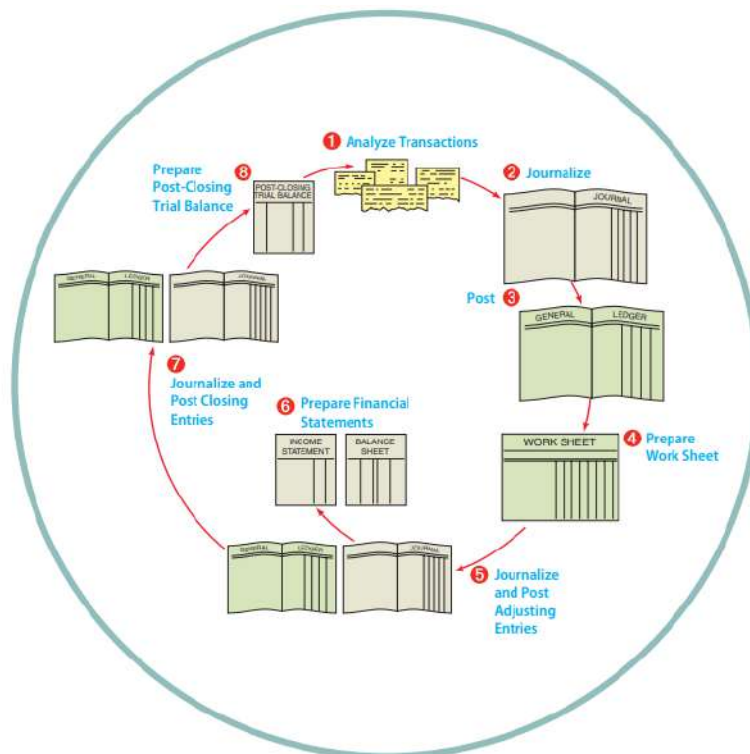
7 Record Totals

8 Double Rule

ACCOUNT TITLE	DEBIT	CREDIT
Cash	2 5 9 7 00	
Petty Cash	1 0 0 00	
Accounts Receivable—Main Street Services	3 0 0 00	
Accounts Receivable—Valley Landscaping	4 0 0 00	
Supplies	9 0 0 00	
Prepaid Insurance	7 5 0 00	
Accounts Payable—Canyon Office Supplies		1 2 0 00
Accounts Payable—Mountain Graphic Arts		1 0 5 00
Michael Delgado, Capital		4 0 1 2 00
Totals	4 2 3 7 00	4 2 3 7 00

- Post-closing trial balance: A trial balance prepared after the closing entries are posted
- What do we use the Post-Closing Trial Balance to verify? debits = credits after closing temporary accounts
- Only general ledger accounts with balances are included on the post-closing trial balance. We do not list temporary accounts, as they have been closed and have zero balances.
- Where do you single rule on the post-closing trial balance? Single rule below the capital account
- This is another way we check that **Assets = Liabilities + Owner's Equity**

C. Accounting Cycle for a Service Business



- Accounting cycle: The series of accounting activities included in recording financial information for a fiscal period

Check yourself!

1. Why are lines drawn in both the Balance Debit and Balance credit columns when an account has a zero balance?

To assure a reader that a balance has not been omitted

2. Which accounts go on the post-closing trial balance?

Only those with balances (permanent accounts)

3. Why are temporary accounts omitted from a post-closing trial balance?

Because they are closed and have zero balances

4. What are the steps in the accounting cycle?

- | | |
|--------------------------|---|
| 1. Analyze transactions. | 5. Journalize and post adjusting entries. |
| 2. Journalize. | 6. Prepare financial statements. |
| 3. Post. | 7. Journalize and post closing entries. |
| 4. Prepare work sheet. | 8. Prepare post-closing trial balance. |