

Chapter 16: Financial Statements and Closing Entries for a Corporation: Chapter Overview

Financial Statements and Closing Entries for a Corporation: Chapter Objectives

Financial Statements and Closing Entries for a Corporation: Accounting in the Real World: Boeing

Financial Statements and Closing Entries for a Corporation: Key Terms

Financial Statements and Closing Entries for a Corporation: Chapter Objectives

Learning Objectives

After studying Chapter 16, in addition to defining key terms, you will be able to:

- LO1 Prepare an income statement for a merchandising business organized as a corporation.
- LO2 Prepare a statement of stockholders' equity.
- LO3 Prepare a balance sheet for a business organized as a corporation.
- LO4 Prepare closing entries.
- LO5 Prepare a post-closing trial balance.

Financial Statements and Closing Entries for a Corporation: Accounting in the Real World: Boeing

Since 1916, The Boeing Company has been a leader in the aerospace industry. The company's first aircraft was its Model C, a two-man seaplane with a cruising speed of merely 65 miles per hour and a range of 200 miles. Today, Boeing is best known for its 7X7 line of commercial aircraft. The Boeing 737, introduced in 1964, continues to be the dominant aircraft flown by commercial passenger airlines. The latest model carries up to 215 passengers with a cruising speed of 500 miles per hour and a range of 3,200 miles.

Boeing is also a leading defense and space contractor. Boeing manufactures a diverse line of military products, including manned and unmanned combat aircraft, surveillance aircraft, missile defense systems, and satellites. The company is also winding down operations as a contractor for the space shuttle and international space station projects.

Are you short of the \$85 million needed to buy a 737? Boeing can also arrange for a commercial airline to finance its aircraft purchases.

So, is Boeing an aircraft, space exploration, or financial company? The income statement Boeing

prepares in accordance with GAAP provides no answer to that question. Like other large corporations, Boeing's income statement reports a single amount of product sales.

Fortunately, the Securities and Exchange Commission (SEC) requires publicly traded corporations to report more detailed financial information. The document filed with the SEC is known as Form 10-K. Boeing's 10-K contains detailed sales information for each of its products. A table shows that Boeing sells more 737s than all other commercial models combined. A reader can also learn the percent of total company revenue generated from each group of products.

Critical Thinking



1. Identify a company that has extended its product line beyond its original market. Find its 10-K report on its website. How are its sales reported?
2. How else could Boeing report its net sales to provide readers with more detailed information?

Financial Statements and Closing Entries for a Corporation:

Key Terms

- operating revenue
- net sales
- cost of merchandise sold
- gross profit
- operating expenses
- income from operations
- statement of stockholders' equity
- par value
- current liabilities
- long-term liabilities
- supporting schedule

Chapter 16: Financial Statements and Closing Entries for a Corporation: Lesson 16-1: Preparing an Income Statement

Lesson 16-1: Preparing an Income Statement

Uses of Financial Statements

Preparing an Income Statement from a Trial Balance LO1

Operating Revenue Section of an Income Statement for a Merchandising Business

Cost of Merchandise Sold Section of an Income Statement for a Merchandising Business

Completing an Income Statement for a Merchandising Business

End of Lesson Review

- LO1 Prepare an income statement for a merchandising business organized as a corporation.

Uses of Financial Statements

Financial statements provide the primary source of information needed by owners and managers to make decisions on the future activity of a business. All financial information must be reported in order to make sound business decisions. The financial statements should provide information about a business's current financial condition, changes from its previously reported financial condition, and the progress of its operations. [CONCEPT: Adequate Disclosure]

Comparing the financial condition and progress for more than one fiscal period helps owners and managers make sound business decisions. Therefore, financial information must be reported the same way from one fiscal period to the next. [CONCEPT: Consistent Reporting]

ThreeGreen prepares three financial statements to report financial progress and condition. A corporation prepares an income statement and a balance sheet similar to those used by a proprietorship. A corporation also prepares a statement of stockholders' equity.

Preparing an Income Statement from a Trial Balance LO1

The income statement of a merchandising business has four main sections: (1) Operating Revenue, (2) Cost of Merchandise Sold, (3) Operating Expenses, and (4) Other Revenue. Information from an adjusted trial balance is used to prepare the income statement. Amounts in all revenue and expense accounts and Merchandise Inventory are reported on an income statement.

<i>ThreeGreen Products, Inc.</i>			
<i>Adjusted Trial Balance</i>			
<i>December 31, 20--</i>			
ACCOUNT TITLE	DEBIT	CREDIT	
<i>Merchandise Inventory</i>	102 838 00		
<i>Income Summary</i>	5 648 44		
<i>Sales</i>		632 371 75	
<i>Sales Discount</i>	1 648 19		
<i>Sales Returns and Allowances</i>	3 941 57		
<i>Purchases</i>	254 851 26		
<i>Purchases Discount</i>		9 222 14	
<i>Purchases Returns and Allowances</i>		1 495 01	
<i>Advertising Expense</i>	4 680 00		
<i>Credit Card Fee Expense</i>	6 842 20		
<i>Depreciation Expense—Office Equipment</i>	7 485 00		
<i>Depreciation Expense—Store Equipment</i>	9 830 00		
<i>Insurance Expense</i>	8 200 00		
<i>Miscellaneous Expense</i>	3 495 04		
<i>Payroll Taxes Expense</i>	16 697 98		
<i>Rent Expense</i>	8 400 00		
<i>Salary Expense</i>	184 234 95		
<i>Supplies Expense—Office</i>	3 938 17		
<i>Supplies Expense—Store</i>	4 584 61		
<i>Uncollectible Accounts Expense</i>	2 384 10		
<i>Utilities Expense</i>	4 965 42		
<i>Federal Income Tax Expense</i>	23 622 40		
<i>Interest Income</i>		5 570 00	
Totals	842 324 77	842 324 77	



ThreeGreen's income statement, illustrated on the next page, is one of many different styles used by various businesses. This four-column style was chosen because it clearly shows the calculations that are made. This income statement differs from Delgado Web Services' income statement shown in Chapter 7. First, ThreeGreen has more accounts to report on its income statement. Second, the Operating Revenue section is more detailed than the Revenue section on Delgado's income statement. Also, ThreeGreen's income statement includes sections for Cost of Merchandise Sold and Other Revenue.

Operating Revenue Section of an Income Statement for a Merchandising Business

The diagram shows an income statement for ThreeGreen Products, Inc. for the year ended December 31, 20--. The operating revenue section is highlighted in light green. Callouts 1-9 point to specific parts of the statement:

- 1: Heading (ThreeGreen Products, Inc. Income Statement For Year Ended December 31, 20--)
- 2: Operating Revenue Section (the entire green-shaded area)
- 3: Title of Revenue Account (Sales)
- 4: Sales Amount (632,371.75)
- 5: Less Contra Accounts (Less: Sales Discount and Sales Returns and Allowances)
- 6: Contra Account Amounts (1,648.19 and 3,941.57)
- 7: Contra Account Total (5,589.76)
- 8: Net Sales (Net Sales)
- 9: Net Sales Amount (626,781.99)

				% OF NET SALES
Operating Revenue:				
Sales			632 371 75	
Less: Sales Discount	1 648 19			
Sales Returns and Allowances	3 941 57	5 589 76		
Net Sales			626 781 99	100.0

ThreeGreen's normal business activity is the sale of ecologically friendly products. The revenue earned by a business from its normal business operations is called **operating revenue**. The Operating Revenue section of the income statement lists the Sales account and its contra accounts, Sales Discount and Sales Returns and Allowances. The amount of sales, less sales discounts and sales returns and allowances, is called **net sales**.

Preparing the Operating Revenue Section of an Income Statement

1. Write the income statement heading on three lines.
2. Write the name of this section, Operating Revenue:, at the extreme left of the wide column on the first line.
3. Write the title of the revenue account, Sales, on the next line, indented about one centimeter.
4. Write the amount of sales, \$632,371.75, in the third amount column.
5. Write Less: on the next line, indented about one centimeter, followed by Sales Discount and Sales Returns and Allowances on the line after that.
6. Write the amount of the sales discounts, \$1,648.19, and sales returns and allowances, \$3,941.57, in the second amount column.
7. Add sales discounts, \$1,648.19, and sales returns and allowances, \$3,941.57, and write the amount, \$5,589.76, in the third amount column.
8. Write Net Sales on the next line, indented about one centimeter.
9. Subtract the total of the contra accounts, \$5,589.76, from sales, \$632,371.75, to calculate net sales, \$626,781.99. Write that amount in the fourth amount column.

Cost of Merchandise Sold Section of an Income Statement for a Merchandising Business

ThreeGreen Products, Inc.										Vertical Analysis Percentages	
Income Statement											
For Year Ended December 31, 20--											
										% OF NET SALES	
<i>Operating Revenue:</i>											
<i>Sales</i>										632	371.75
<i>Less: Sales Discount</i>										1	648.19
<i>Sales Returns and Allowances</i>										3	941.57
<i>Net Sales</i>										626	781.99
100.0											
<i>Cost of Merchandise Sold:</i>											
<i>Merchandise Inventory, Jan. 1, 20--</i>										108	486.44
<i>Purchases</i>										254	851.26
<i>Less: Purchases Discount</i>										9	22.14
<i>Purchases Returns and Allowances</i>										1	495.01
<i>Net Purchases</i>										252	434.11
<i>Total Cost of Mdse. Avail. for Sale</i>										360	920.55
<i>Less Mdse. Inventory, Dec. 31, 20--</i>										102	838.00
<i>Cost of Merchandise Sold</i>										258	082.55
<i>Gross Profit</i>										368	699.44
											58.8

The original price of all merchandise sold during a fiscal period is called the **cost of merchandise sold**. [CONCEPT: Historical Cost] Cost of merchandise sold is also known as cost of goods sold or cost of sales. The operating revenue remaining after cost of merchandise sold has been deducted is called **gross profit**. Gross profit is often referred to as gross profit on sales. Management uses gross profit as a measure for how effectively the business is performing in its primary functions of buying and selling merchandise. Calculating a ratio between gross profit and net sales enables management to compare its performance to prior fiscal periods.

Most calculated amounts reported on a financial statement have a related description. Net sales and net purchases are two examples. However, the totals of the sales contra accounts, \$5,589.76, and the purchases contra accounts, \$2,417.15, are not described. Instead, the reader of the financial statement is expected to understand the amount by its physical position on the statement. Each amount is immediately to the right of an amount column ruled with a single line.

The single ruled line shown in the illustration below indicates that the column is being totaled. The

amount adjacent to the column is the sum of that column.

ThreeGreen Products, Inc.													
Income Statement													
For Year Ended December 31, 20--													
												% OF NET SALES	
<i>Operating Revenue:</i>													
<i>Sales</i>													
<i>Less: Sales Discount</i>													
<i>Sales Returns and Allowances</i>													
<i>Net Sales</i>													

Total of adjacent column

Preparing the Cost of Merchandise Sold Section of an Income Statement

1. Write the name of this section, Cost of Merchandise Sold:, at the extreme left of the wide column.
2. Write the beginning inventory.
 - a. Indent about one centimeter on the next line and write Merchandise Inventory, Jan. 1, 20--.
 - b. Write the beginning merchandise inventory balance, \$108,486.44, in the third amount column. The amount of beginning inventory is the January 1 balance of the Merchandise Inventory general ledger account.
3. Prepare the Purchases subsection.
 - a. Indent about one centimeter on the next line and write Purchases. Enter the purchases amount, \$254,851.26, in the second amount column.
 - b. Write Less: on the next line, indented about one centimeter, followed by Purchases Discount and Purchases Returns and Allowances aligned below it. It is permissible to abbreviate long titles when necessary.
 - c. Write the amount of the purchases discounts, \$922.14, and purchases returns and allowances, \$1,495.01, in the first amount column.
 - d. Add purchases discounts, \$922.14, and purchases returns and allowances, \$1,495.01, and write the amount, \$2,417.15, in the second amount column.
 - e. Write Net Purchases on the next line, indented about one centimeter.
 - f. Subtract the total of the contra accounts, \$2,417.15, from Purchases, \$254,851.26, to calculate net purchases, \$252,434.11. Write that amount in the third amount column.
4. Calculate the total cost of merchandise available for sale.
 - a. Indent about one centimeter on the next line, and write Total Cost of Merchandise Available

for Sale.

- b. Add the beginning merchandise inventory, \$108,486.44, and net purchases, \$252,434.11, to calculate the total cost of merchandise available for sale, \$360,920.55. Write that amount in the third amount column.
5. Write the amount of the ending inventory found in the adjusted trial balance.
 - a. Indent about one centimeter on the next line, and write Less Merchandise Inventory, Dec. 31, 20--.
 - b. Write the ending merchandise inventory, \$102,838.00, found in the adjusted trial balance, in the third amount column.
6. Calculate the cost of merchandise sold.
 - a. Indent about one centimeter on the next line, and write Cost of Merchandise Sold.
 - b. Subtract the ending merchandise inventory, \$102,838.00, from the total cost of merchandise available for sale, \$360,920.55, to calculate the cost of merchandise sold, \$258,082.55. Write that amount in the fourth amount column.
7. Calculate the gross profit.
 1. Write Gross Profit on the next line at the extreme left of the wide column.
 2. Write the gross profit, \$368,699.44, in the fourth amount column. (Total operating revenue, \$626,781.99, less cost of merchandise sold, \$258,082.55, equals gross profit, \$368,699.44.)
8. Prepare a vertical analysis.
 - a. Divide each amount in the fourth amount column by the amount of net sales. Round each percentage to the nearest 0.1%.
 - b. Write the percentage in the % of Net Sales column.

Other titles for an income statement include a statement of earnings, profit and loss statement, statement of operations, and statement of income.

Completing an Income Statement for a Merchandising Business

ThreeGreen Products, Inc. Income Statement For Year Ended December 31, 20--				
Gross Profit			368 699 44	58.8
Operating Expenses:				
Advertising Expense	4 680 00			
Credit Card Fee Expense	6 842 20			
Depreciation Expense—Office Equipment	7 485 00			
Depreciation Expense—Store Equipment	9 830 00			
Insurance Expense	8 200 00			
Miscellaneous Expense	3 495 04			
Payroll Taxes Expense	16 697 98			
Rent Expense	8 400 00			
Salary Expense	184 234 95			
Supplies Expense—Office	3 938 17			
Supplies Expense—Store	4 584 61			
Uncollectible Accounts Expense	2 384 10			
Utilities Expense	4 965 42			
Total Operating Expenses		265 737 47	42.4	
Income from Operations		102 961 97	16.4	
Other Revenue:				
Interest Income		5 570 00	0.1	
Net Income before Federal Income Tax		103 518 97	16.5	
Less Federal Income Tax Expense		23 622 40	3.8	
Net Income after Federal Income Tax		79 896 57	12.7	

The expenses incurred by a business in its normal operations are called **operating expenses**. The operating revenue remaining after the cost of merchandise sold and operating expenses have been deducted is called **income from operations**. Income from operations is also referred to as operating income. Businesses often earn income unrelated to their normal business

operations. One example is interest earned on invested or loaned funds. On the income statement, Interest Income is presented after Income from Operations in a section labeled Other Revenue.

Completing an Income Statement

1. Prepare the Operating Expenses section.
 - a. Write the name of this section, Operating Expenses:, at the extreme left of the wide column.
 - b. On the next line, indented about one centimeter, list the expense account titles, one per line, in the order in which they appear on the trial balance.
 - c. Write the amount of each expense account balance in the third amount column.
 - d. Indent about one centimeter, and write Total Operating Expenses on the next line in the wide column below the last expense account title.
 - e. Total the individual expense amounts and write the total, \$265,737.47, in the fourth amount column on the total line.
2. Calculate the income from operations.
 - a. Write Income from Operations on the next line at the extreme left of the wide column.
 - b. Write the amount, \$102,961.97, in the fourth amount column. (Gross profit, \$368,699.44, less total operating expenses, \$265,737.47, equals income from

operations, \$102,961.97.)

3. Prepare the Other Revenue section.
 - a. Write the name of this section, Other Revenue:, at the extreme left of the wide column.
 - b. Indent about one centimeter, and write Interest Income on the next line in the wide column. Write the amount, \$557.00, on the same line in the fourth amount column.
4. Calculate the net income before federal income tax.
 - a. Write Net Income before Federal Income Tax on the next line at the extreme left of the wide column.
 - b. Write the amount, \$103,518.97, in the fourth amount column. (Income from operations, \$102,961.97, plus other revenue, \$557.00, equals net income before federal income tax, \$103,518.97.)
5. Write Less Federal Income Tax Expense on the next line at the extreme left of the wide column. Write the amount, \$23,622.40, on the same line in the fourth amount column.
6. Calculate net income after federal income tax.
 - a. Write Net Income after Federal Income Tax on the next line at the extreme left of the wide column.
 - b. Write the amount, \$79,896.57, in the fourth amount column. (Net income before federal income tax, \$103,518.97, less federal income tax expense, \$23,622.40, equals net income after federal income tax, \$79,896.57.)
7. Rule double lines across the four amount columns to show that the income statement is complete.
8. Prepare a vertical analysis.
 - a. Divide each amount in the fourth amount column by the amount of net sales. Round each percentage to the nearest 0.1%.
 - b. Write the percentage in the % of Net Sales column.

End of Lesson Review

LO1 Prepare an income statement for a merchandising business organized as a corporation.

Terms Review

- operating revenue
- net sales
- cost of merchandise sold
- operations
- gross profit
- operating expenses
- income from

Audit Your Understanding

1. What is the major difference between the income statements for merchandising businesses and service businesses?
2. How is the cost of merchandise sold calculated?
3. Why is interest income presented in a section other than Operating Revenue?

Work Together 16-1

Preparing an income statement for a merchandising business

The adjusted trial balance for Superior Corporation for the year ended December 31 of the current year is given in the Working Papers. The beginning merchandise inventory amount is \$86,789.15. Your instructor will guide you through the following examples.

- Prepare an income statement.
- Prepare a vertical analysis of each amount in the fourth amount column. Round calculations to the nearest 0.1%. Save your work to complete Work Together 16-2.

On Your Own 16-1

Preparing an income statement for a merchandising business

Eastern Imports' adjusted trial balance for the year ended December 31 of the current year is given in the Working Papers. The beginning merchandise inventory amount is \$128,110.24. Work this problem independently.

1. Prepare an income statement.
2. Prepare a vertical analysis of each amount in the fourth amount column. Round calculations to the nearest 0.1%. Save your work to complete On Your Own 16-2.

Chapter 16: Financial Statements and Closing Entries for a Corporation: Ethics in Action: Don't Bite the Hand That Feeds You

Ethics in Action: Don't Bite the Hand That Feeds You

Instructions

Many grocery and department stores package their damaged, returned, and overstocked nonperishable items for sale to salvage stores. The items are packed into large crates and sold by the crate at a substantial discount over retail price. The salvage stores do not even know what items are in the crates until the crates are delivered and opened.

Patti Dexter has worked in the floral department of Harvest Grocery Store for several years. In her spare time, she has been helping her parents open a salvage store within one mile of Harvest Grocery Store. Patti intends to keep her current job and help her parents only on crate delivery day.

Instructions

Determine whether it is ethical for Patti to work for both Harvest Grocery Store and her parents' salvage store. Use The Kroger Co. Policy on Business Ethics as a guide.

Chapter 16: Financial Statements and Closing Entries for a Corporation: Think Like an Accountant: Managing a Stock Portfolio

Think Like an Accountant: Managing a Stock Portfolio

Lakeland Marina operates six marinas on Lake Martin. Located in a northern climate, the company earns more than 70% of its annual revenues during three summer months. The money earned during these months is needed to operate the marinas during the cold winter months when sales plummet.

Daniel Ellis, CPA, is the chief financial officer of the company. He is responsible for investing excess cash until it is needed to pay operating expenses during the winter months. The company's board of directors has a policy that restricts how Daniel can invest the cash. Daniel is limited to buying the stock of companies listed in the S&P 500. The S&P 500 is a collection of large American companies. He constantly monitors the market prices of stocks in the portfolio to evaluate his investment decisions.

The company maintains investment accounts with five local financial advisors. Each financial advisor is affiliated with a national investment firm. Daniel likes having access to the variety of investment research that each advisor's firm offers. Spreading the investments around is also good business. Each of the financial advisors has a boat docked at one of the marinas.

Unfortunately, using five financial advisors means that Daniel receives five investment reports. He needs one place where he can monitor the value of the entire stock portfolio.

Open the Spreadsheet TLA_CH16



Complete the worksheet to determine the current value of the investments. Answer the following questions:

1. Identify the stocks having the highest positive percentage change, as denoted by the green arrow in the % Change column.
2. Which stock has the highest total value?
3. What ratio using two items of information from the schedule could provide Daniel with useful information about the performance of each stock?

Chapter 16: Financial Statements and Closing Entries for a Corporation: Forensic Accounting: The Demise of Arthur Andersen

Forensic Accounting: The Demise of Arthur Andersen

Activity

Instructions

For nearly a century, the name Arthur Andersen stood for quality accounting services. Arthur Andersen's clients included many of the world's best-known companies: FedEx, Merck, Sara Lee, Walgreens, and Delta Air Lines. One of the "Big Five" accounting firms, Arthur Andersen employed over 85,000 employees worldwide. The number of staff and clients attending classes at its suburban Chicago training center made the firm the largest corporate user of O'Hare Airport.

In a stunning turn of events in 2002, the Big Five became the "Big Four." In 2001, energy company Enron announced that its financial statements were inflated by a massive accounting fraud. Of course, Enron's stockholders wanted to know why its auditor, Arthur Andersen, failed to detect the fraud. The investigations and lawsuits that followed delved into the actions of both Enron executives and Arthur Andersen employees.

Arthur Andersen was no stranger to lawsuits. Investors often sue auditors when a corporation fails or announces an accounting fraud. But the Enron failure was different. Investigators learned that Arthur Andersen employees had shredded documents related to the firm's Enron audit. Arthur Andersen was convicted of obstruction of justice. Due to the conviction, the firm was banned from auditing any financial statements submitted to the Securities and Exchange Commission. The loss of its publicly



traded corporate clients effectively killed the firm.

At the time, the Enron bankruptcy was the largest in U.S. history. Enron would only hold that dubious honor for a month. Telecommunications giant WorldCom, another Arthur Andersen client, filed for bankruptcy in July 2002.

Enron and WorldCom share a common story. Each company was heralded for its innovative, dynamic business model. Each company's financial statements reported increasing earnings. In reality, those financial statements were hiding the fact that earnings were declining. Each accounting fraud was a failed attempt by executives to protect their reputations and maintain inflated stock prices. In each case, Arthur Andersen failed to detect the frauds.

Activity

Cress Valley Electronics, with one store located in Nashville, has submitted its financial statements to your bank. Its owner, Donald Morris, is seeking a loan to expand his business.

Instructions



Open the spreadsheet FA_CH16 and complete the steps on the Instructions tab.

Chapter 16: Financial Statements and Closing Entries for a Corporation: Lesson 16-2: Preparing a Statement of Stockholders' Equity

Lesson 16-2: Preparing a Statement of Stockholders' Equity

Stockholders' Equity Information LO2

Capital Stock Section of the Statement of Stockholders' Equity

Retained Earnings Section of the Statement of Stockholders' Equity

End of Lesson Review

- LO2 Prepare a statement of stockholders' equity.

Stockholders' Equity Information LO2

ThreeGreen Products, Inc.												
Income Statement												
For Year Ended December 31, 20--												
Net Income before Federal Income Tax												103 518 97
Less Federal Income Tax Expense												23 622 40
Net Income after Federal Income Tax												<u>79 896 57</u>

ACCOUNT <i>Capital Stock</i>										ACCOUNT NO. 3110			
DATE	ITEM	POST. REF.	DEBIT	CREDIT	BALANCE								
					DEBIT		CREDIT						
Jan. 1	Balance	✓						70 000 00					
May 14		CR5		5 000 00				75 000 00					

ThreeGreen Products, Inc.												
Adjusted Trial Balance												
December 31, 20--												
ACCOUNT TITLE					DEBIT				CREDIT			
<i>Capital Stock</i>									75 000 00			
<i>Retained Earnings</i>									65 218 84			
<i>Dividends</i>					15 000 00							

A financial statement that shows changes in a corporation's ownership for a fiscal period is called a [statement of stockholders' equity](#). The information to prepare a statement of stockholders' equity is obtained from several sources. The current year's income statement summarizes the change in retained earnings from the operation of the business. The general ledger provides the beginning balance and activity in the Capital Stock account. The current year's adjusted trial balance provides the current balances of other capital accounts.

Capital Stock Section of the Statement of Stockholders' Equity

The diagram shows a financial statement for ThreeGreen Products, Inc. The heading (1) is "ThreeGreen Products, Inc. Statement of Stockholders' Equity For Year Ended December 31, 20--". The table (2) is titled "Capital Stock: \$10.00 Par Value". It has three rows: "January 1, 20--, 7,000 Shares Issued" with a value of 70,000.00; "Issued during Current Year, 500 Shares" with a value of 5,000.00; and "Balance, December 31, 20--, 7,500 Shares Issued" with a value of 75,000.00. Callout 3 points to the beginning balance, callout 4 to the current year issuance, and callout 5 to the total ending balance.

ThreeGreen Products, Inc.	
Statement of Stockholders' Equity	
For Year Ended December 31, 20--	
Capital Stock:	
\$10.00 Par Value	
January 1, 20--, 7,000 Shares Issued	70 0 0 0 00
Issued during Current Year, 500 Shares	5 0 0 0 00
Balance, December 31, 20--, 7,500 Shares Issued	75 0 0 0 00

A statement of stockholders' equity contains two major sections: (1) Capital Stock and (2) Retained Earnings. The amount of capital stock issued as of the beginning of the year is the beginning balance of the Capital Stock general ledger account. Any additional stock transactions during the fiscal year are recorded in the same account. Thus, the amounts in the Capital Stock section of the statement of stockholders' equity are obtained from Capital Stock.

Each share of stock issued by a corporation has a monetary value. A value assigned to a share of stock and printed on the stock certificate is called **par value**. When issuing shares of stock, a corporation can assign any par value allowed by laws in the state in which it incorporates.

Preparing the Capital Stock Section of a Statement of Stockholders' Equity

1. Write the heading: company name, ThreeGreen Products, Inc.; statement name, Statement of Stockholders' Equity; and fiscal period, For Year Ended December 31, 20--.
2. Write the heading, Capital Stock:. On the next line, write the par value of the stock, \$10.00 Par Value, indented about one centimeter.
3. On the next line, write January 1, 20--, the number of shares, 7,000, and Shares Issued. In the second amount column enter \$70,000.00, the dollar amount of stock issued as of the beginning of the year.
4. On the next line, write Issued during Current Year, 500 Shares, the number of shares issued. In the second amount column, write the dollar amount of stock issued during the year, \$5,000.00.
5. On the next line, write Balance, December 31, 20--, 7,500 Shares Issued, the current amount of

shares outstanding. Calculate the total dollar amount of stock issued as of the end of the year by adding the dollar amount of beginning stock, \$70,000.00, and the dollar amount of shares issued during the year, \$5,000.00. Write the total amount, \$75,000.00, in the third amount column.

Retained Earnings Section of the Statement of Stockholders' Equity

1 Retained Earnings Section

3 Net Income after Federal Income Tax

2 Beginning Balance

4 Dividends Declared

5 Increase in Retained Earnings

6 Ending Balance

7 Total Stockholders' Equity

ThreeGreen Products, Inc.			
Statement of Stockholders' Equity			
For Year Ended December 31, 20--			
Capital Stock:			
\$10.00 Par Value			
January 1, 20--, 7,000 Shares Issued		70 0 0 0 00	
Issued during Current Year, 500 Shares		5 0 0 0 00	
Balance, December 31, 20--, 7,500 Shares Issued			75 0 0 0 00
Retained Earnings:			
Balance, January 1, 20--		65 2 1 8 84	
Net Income after Federal Income Tax for 20--	79 8 9 6 57		
Less Dividends Declared during 20--	15 0 0 0 00		
Net Increase during 20--		64 8 9 6 57	
Balance, December 31, 20--			130 1 1 5 41
Total Stockholders' Equity, December 31, 20--			205 1 1 5 41

Net income increases a corporation's total capital. Some income may be retained by a corporation for business expansion. Some income may be distributed as dividends to provide stockholders with a return on their investments. During the year, ThreeGreen's board of directors declared \$15,000.00 in dividends.

The Retained Earnings section of the Statement of Stockholders' Equity is prepared using amounts on the adjusted trial balance and the income statement. The beginning balance of Retained Earnings and the amount of dividends declared are obtained from the adjusted trial balance. The net income after federal income taxes is obtained from the income statement.

It is not uncommon for a business to have a net loss during its early years of existence. The losses would result in a debit balance in Retained Earnings. This amount would be reported as an accumulated deficit on the statement of retained earnings.

Preparing the Retained Earnings Section of a Statement of Stockholders' Equity

1. Write the heading, Retained Earnings:.
2. Write the beginning balance of Retained Earnings, \$65,218.84, from the adjusted trial balance, indented about one centimeter.
3. Write the net income after federal income tax, \$79,896.57, from the income statement.
4. Write the amount of dividends, \$15,000.00, from the adjusted trial balance.
5. Subtract dividends, \$15,000.00, from net income after federal income tax, \$79,896.57, to calculate the increase in retained earnings, \$64,896.57. Write that amount in the second amount column.
6. Add the beginning balance of retained earnings, \$65,218.84, and the increase in retained earnings, \$64,896.57, to calculate the ending balance of retained earnings, \$130,115.41. Write that amount in the third amount column.
7. Add the ending amounts of capital stock, \$75,000.00, and retained earnings, \$130,115.41, to calculate the total amount of stockholders' equity, \$205,115.41. Write that amount in the third amount column.

End of Lesson Review

- LO2 Prepare a statement of stockholders' equity.

Terms Review

- statement of stockholders' equity
- par value

Audit Your Understanding

1. What financial information does a statement of stockholders' equity report?
2. What are the two major sections of a statement of stockholders' equity?
3. Where is the information found to prepare the Capital Stock section of a statement of stockholders' equity?
4. Where is the beginning balance of retained earnings found?
5. When issuing shares of stock, what par value can a corporation assign to each share?
6. Where is net income after federal income taxes found?

Work Together 16-2

Preparing a statement of stockholders' equity

Use the trial balance and income statement for Superior Corporation from Work Together 16-1. A form for the statement of stockholders' equity is given in the Working Papers. Your instructor will guide you through the following example.

Prepare a statement of stockholders' equity for the current year. As of January 1, Superior Corporation had issued 8,000 shares of capital stock with a par value of \$10.00 per share. During the fiscal year, the corporation issued 250 additional shares of capital stock. Save your work to complete Work Together 16-3.

On Your Own 16-2

Preparing a statement of stockholders' equity

Use the trial balance and income statement for Eastern Imports from On Your Own 16-1. A form for the statement of stockholders' equity is given in the Working Papers. Work this problem independently.

Prepare a statement of stockholders' equity for the current year. As of January 1, Eastern Imports had issued 124,000 shares of capital stock with a par value of \$1.00 per share. During the fiscal year, the corporation issued 12,000 additional shares of stock. Save your work to complete On Your Own 16-3.

Chapter 16: Financial Statements and Closing Entries for a Corporation: Lesson 16-3: Preparing a Balance Sheet

Lesson 16-3: Preparing a Balance Sheet

- LO3 Prepare a balance sheet for a business organized as a corporation.

Balance Sheet Information on a Trial Balance LO3

ThreeGreen Products, Inc.				
Adjusted Trial Balance				
December 31, 20--				
ACCOUNT TITLE	DEBIT		CREDIT	
Cash	54	194	34	
Petty Cash		2	50	00
Accounts Receivable	20	381	81	
Allowance for Uncollectible Accounts				2509
Merchandise Inventory	102	838	00	
Supplies—Office		6	10	00
Supplies—Store		4	65	00
Prepaid Insurance		2	80	00
Notes Receivable		6	20	00
Interest Receivable			9	30
Office Equipment	24	895	18	
Accumulated Depreciation—Office Equipment				13674
Store Equipment	59	148	11	
Accumulated Depreciation—Store Equipment				18325
Accounts Payable				16489
Sales Tax Payable				3574
Employee Income Tax Payable				950
Social Security Tax Payable				2023
Medicare Tax Payable				473
Health Insurance Premiums Payable				460
Retirement Benefits Payable				465
Unemployment Tax Payable—Federal				297
Unemployment Tax Payable—State				147
Federal Income Tax Payable				362
Dividends Payable				375

A corporation's balance sheet reports assets, liabilities, and stockholders' equity on a specific date. [CONCEPT: Accounting Period Cycle] Some management decisions can best be made after owners have analyzed the balance sheet. For example, balance sheet information would help management to decide whether the corporation should incur additional liabilities to acquire additional plant assets.

The information used to prepare a balance sheet is obtained from two sources: (1) the trial balance and (2) the statement of stockholders' equity.

Current Assets Section of a Balance Sheet

ThreeGreen Products, Inc.	
Balance Sheet	
December 31, 20--	
Assets	
Current Assets:	
Cash	54 1 9 4 34
Petty Cash	2 5 0 0 0
Accounts Receivable	20 3 8 1 81
Less Allowance for Uncollectible Accounts	2 5 0 9 25
Merchandise Inventory	102 8 3 8 0 0
Supplies—Office	6 1 0 0 0
Supplies—Store	4 6 5 0 0
Prepaid Insurance	2 8 0 0 0 0
Notes Receivable	6 2 0 0 0 0
Interest Receivable	9 3 0 0
Total Current Assets	185 3 2 2 90

ThreeGreen classifies its assets as current assets and plant assets. A business owning both current and plant assets usually lists them under separate headings on a balance sheet. Some of ThreeGreen's asset accounts have related contra accounts that reduce the related account on the balance sheet. The difference between an asset's account balance and its related contra account balance is known as book value. An asset's book value is reported on a balance sheet by listing three amounts: (1) the balance of the asset account, (2) the balance of the asset's contra account, and (3) the book value.

Preparing the Current Assets Section of a Balance Sheet

1. Write the balance sheet heading on three lines.
2. Begin preparing the Assets section of the balance sheet. Use information from the adjusted trial balance.
 - a. Write the section title, Assets, on the first line in the middle of the wide column.
 - b. Write the section title, Current Assets:, on the next line at the extreme left of the wide column.
 - c. Beginning on the next line, indented about one centimeter, write Cash and Petty Cash in the order in which they appear on the adjusted trial balance.
 - d. Write the balance of each asset account in the second column.
3. Calculate the book value of accounts receivable.
 - a. Write Accounts Receivable on the next line, indented about one centimeter.
 - b. Write the total amount of accounts receivable, \$20,381.81, in the first amount column.
 - c. Write Less Allowance for Uncollectible Accounts on the next line, indented about two centimeters.
 - d. Write the amount of the allowance for uncollectible accounts, \$2,509.25, in the first amount column.
 - e. Subtract the allowance for uncollectible accounts, \$2,509.25, from the total amount of accounts receivable, \$20,381.81, to calculate the book value of accounts receivable, \$17,872.56. Write that amount in the second amount column on the same line.
4. Write the remaining current asset account titles and amounts.
5. Calculate total current assets.
 - a. Write Total Current Assets on the next line, indented about one centimeter.
 - b. Add the amounts in the second amount column and write the total, \$185,322.90, in the third amount column.

Plant Assets Section of a Balance Sheet

ThreeGreen Products, Inc.									
Balance Sheet									
December 31, 20--									
Plant Assets Section ①									
Total Current Assets									185 3 2 2 90
Plant Assets:									
Office Equipment	24 8 9 5 18								
Less Accumulated Depreciation—Office Equipment	13 6 7 4 00	11 2 2 1 18							
Store Equipment	59 1 4 8 11								
Less Accumulated Depreciation—Store Equipment	18 3 2 5 00	40 8 2 3 11							
Total Plant Assets								52 0 4 4 29	
Total Assets								237 3 6 7 19	

② Book Value of Office Equipment

③ Book Value of Store Equipment

④ Total Plant Assets

⑤ Total Assets

Preparing the Plant Assets Section of a Balance Sheet

1. Write the heading, Plant Assets:, on the next line at the extreme left of the wide column.
2. Calculate the book value of office equipment using information from the adjusted trial balance.
 - a. Write Office Equipment on the next line, indented about one centimeter.
 - b. Write the total amount of office equipment, \$24,895.18, in the first amount column.
 - c. Write Less Accumulated Depreciation—Office Equipment on the next line, indented about two centimeters.
 - d. Write the amount of the accumulated depreciation—office equipment, \$13,674.00, in the first amount column.
 - e. Subtract the accumulated depreciation—office equipment, \$13,674.00, from the total amount of office equipment, \$24,895.18, to calculate the book value of office equipment, \$11,221.18. Write that amount in the second amount column on the same line.
3. Use the same procedure to calculate the book value of store equipment.
4. Calculate total plant assets.
 - a. Write Total Plant Assets on the next line, indented about one centimeter.
 - b. Add the amounts in the second amount column and write the total, \$52,044.29, in the third amount column.
5. Calculate total assets.
 - a. Write Total Assets on the next line at the extreme left of the wide column.
 - b. Add the totals of current assets, \$185,322.90, and plant assets, \$52,044.29, and write the amount, \$237,367.19, on the same line in the third amount column.

Liabilities Section of a Balance Sheet

ThreeGreen Products, Inc.										
Balance Sheet										
December 31, 20--										
<i>Total Assets</i>							237	367	19	
Liabilities										
<i>Current Liabilities:</i>										
<i>Accounts Payable</i>						16	489	10		
<i>Sales Tax Payable</i>						3	574	64		
<i>Employee Income Tax Payable—Federal</i>						9	500	00		
<i>Social Security Tax Payable</i>						2	023	06		
<i>Medicare Tax Payable</i>						4	731	14		
<i>Health Insurance Premiums Payable</i>						4	600	00		
<i>Retirement Benefits Payable</i>						4	650	00		
<i>Unemployment Tax Payable—Federal</i>						2	970	02		
<i>Unemployment Tax Payable—State</i>						1	474	2		
<i>Federal Income Tax Payable</i>						3	622	40		
<i>Dividends Payable</i>						3	750	00		
<i>Total Liabilities</i>							32	251	78	

① Liabilities Section
② Account Title and Amount of Each Current Liability
③ Total Liabilities

Liabilities are classified according to the length of time until they are due. Liabilities due within a short time, usually within a year, are called **current liabilities**. Liabilities owed for more than a year are called **long-term liabilities**. One example of a long-term liability would be a mortgage loan. On December 31 of the current year, ThreeGreen does not have any long-term liabilities.

To prepare the Liabilities section of the balance sheet, use information from the adjusted trial balance.

A company having both current liabilities and long-term liabilities would include headings and totals for each category. The process is similar to preparing the Assets section of a balance sheet.

Preparing the Liabilities Section of a Balance Sheet

1. Write the section title, Liabilities, on the next line in the middle of the wide column.
2. Write the title, Current Liabilities:, on the next line at the extreme left of the wide column.
 - a. Beginning on the next line, indented about one centimeter, write the liability account titles in the order in which they appear on the adjusted trial balance.
 - b. Write the balance of each liability account in the second amount column.
3. Calculate total liabilities.
 - a. Write Total Liabilities on the next line below the last liability account title at the extreme

left of the wide column.

- b. Write the amount of the total liabilities, \$32,251.78, on the same line in the third amount column.

Stockholders' Equity Section of a Balance Sheet

ThreeGreen Products, Inc. Balance Sheet December 31, 20--	
Total Assets	237 3 6 7 19
Total Liabilities	32 2 5 1 78
Stockholders' Equity	
Capital Stock	75 0 0 0 00
Retained Earnings	130 1 1 5 41
Total Stockholders' Equity	205 1 1 5 41
Total Liabilities and Stockholders' Equity	237 3 6 7 19

Annotations:

- 1 Stockholders' Equity Section
- 2 Capital Stock
- 3 Retained Earnings
- 4 Total Stockholders' Equity
- 5 Total Liabilities and Stockholders' Equity
- 6 Double Rule

A major difference between the balance sheets of a corporation and a proprietorship is the Owners' Equity section. The Owners' Equity section of ThreeGreen's balance sheet is labeled Stockholders' Equity. Some corporations use the same label, Owners' Equity, as proprietorships. Either label is acceptable.

The Stockholders' Equity section contains the total amounts of capital stock and retained earnings. These amounts are calculated and reported on the statement of stockholders' equity.

ThreeGreen's completed balance sheet is shown on the following page.

Preparing the Stockholders' Equity Section of a Balance Sheet

1. Write the heading, Stockholders' Equity, on the next line, centered in the wide column.
2. Write Capital Stock on the next line. Write the amount of capital stock, \$75,000.00, calculated on the statement of stockholders' equity, in the second amount column.
3. Write Retained Earnings on the next line. Write the amount of retained earnings, \$130,115.41, calculated on the statement of stockholders' equity, in the second amount column.
4. Add the amount of capital stock, \$75,000.00, and retained earnings, \$130,115.41, to calculate the

total of stockholders' equity, \$205,115.41. Enter that amount in the third amount column.

5. Add the amount of total liabilities, \$32,251.78, and total stockholders' equity, \$205,115.41, to calculate the total of liabilities and stockholders' equity, \$237,367.19. Enter that amount in the third amount column. Verify the accuracy by comparing the total amount of assets and the total amount of liabilities and stockholders' equity. These two amounts must be the same.
6. Draw double rules across the three columns at the end of the Assets section and the Stockholders' Equity section to show that assets equal liabilities plus owners' equity.

Completed Balance Sheet

<i>ThreeGreen Products, Inc.</i>			
<i>Balance Sheet</i>			
<i>December 31, 20--</i>			
<i>Assets</i>			
<i>Current Assets:</i>			
<i>Cash</i>			54 194 34
<i>Petty Cash</i>			25 000
<i>Accounts Receivable</i>	20 381 81		
<i> Less Allowance for Uncollectible Accounts</i>	25 092 5	17 872 56	
<i>Merchandise Inventory</i>		102 838 00	
<i>Supplies—Office</i>		6 100 0	
<i>Supplies—Store</i>		4 650 0	
<i>Prepaid Insurance</i>		2 800 0	
<i>Notes Receivable</i>		6 200 0	
<i>Interest Receivable</i>		93 0	
<i>Total Current Assets</i>			185 322 90
<i>Plant Assets:</i>			
<i>Office Equipment</i>	24 895 18		
<i> Less Accumulated Depreciation—Office Equipment</i>	13 674 00	11 221 18	
<i>Store Equipment</i>	59 148 11		
<i> Less Accumulated Depreciation—Store Equipment</i>	18 325 00	40 823 11	
<i>Total Plant Assets</i>			52 044 29
<i>Total Assets</i>			237 367 19
<i>Liabilities</i>			
<i>Current Liabilities:</i>			
<i>Accounts Payable</i>		16 489 10	
<i>Sales Tax Payable</i>		3 574 64	
<i>Employee Income Tax Payable</i>		9 500 0	
<i>Social Security Tax Payable</i>		2 023 06	
<i>Medicare Tax Payable</i>		4 731 4	
<i>Health Insurance Premiums Payable</i>		4 600 0	
<i>Retirement Benefits Payable</i>		4 650 0	
<i>Unemployment Tax Payable—Federal</i>		2 970 2	
<i>Unemployment Tax Payable—State</i>		1 474 2	
<i>Federal Income Tax Payable</i>		3 622 40	
<i>Dividends Payable</i>		3 750 0	
<i>Total Liabilities</i>			32 251 78
<i>Stockholders' Equity</i>			
<i>Capital Stock</i>		75 000 0	
<i>Retained Earnings</i>		130 115 41	
<i>Total Stockholders' Equity</i>			205 115 41
<i>Total Liabilities and Stockholders' Equity</i>			237 367 19

Total assets must equal the total of liabilities and stockholders' equity. If these totals are not equal, identify the errors before preparing adjusting and closing entries.

Supporting Schedules for a Balance Sheet

A report prepared to give details about an item on a principal financial statement is called a **supporting schedule**. A supporting schedule is sometimes referred to as a supplementary report or an exhibit.

ThreeGreen prepares two supporting schedules to accompany the balance sheet. The supporting schedules are a schedule of accounts payable and a schedule of accounts receivable. A balance sheet shows only the accounts payable total amount. The account balance for each vendor is not shown. When detailed information is needed, a supporting schedule of accounts payable is prepared, showing the balance for each vendor. A balance sheet also shows only the accounts receivable total amount. When information about the account balance for each customer is needed, a supporting schedule of accounts receivable is prepared. ThreeGreen's supporting schedules on December 31 are similar to the supporting schedules for November 30 shown in Chapters 9 and 10.

End of Lesson Review

- LO3 Prepare a balance sheet for a business organized as a corporation.

Terms Review

- current liabilities
- long-term liabilities
- supporting schedule

Audit Your Understanding

1. How does ThreeGreen classify its assets?
2. What three items are listed on the balance sheet for an account having a related contra asset account?
3. What is an example of a long-term liability?
4. Where are the amounts obtained for the Stockholders' Equity section of the balance sheet?
5. What are two supporting schedules that might accompany a balance sheet?

Work Together 16-3

Preparing a balance sheet for a corporation

Use Superior Corporation's trial balance and statement of stockholders' equity from Work Together 16-2. A form for the balance sheet is given in the Working Papers. Your instructor will guide you through the following example.

Prepare a balance sheet for the current year. Save your work to complete Work Together 16-4.

On Your Own 16-3

Preparing a balance sheet for a corporation

Use Eastern Imports' trial balance and statement of stockholders' equity from On Your Own 16-2. A form for the balance sheet is given in the Working Papers. Work this problem independently.

Prepare a balance sheet for the current year. Save your work to complete On Your Own 16-4.

Chapter 16: Financial Statements and Closing Entries for a Corporation: Why Accounting?: Museum Curators Do Accounting Too

Why Accounting?: Museum Curators Do Accounting Too

Critical Thinking

If you have ever been to a museum of history, you probably realize that the museum artifacts and the way they are displayed tell a story. Have you ever thought about the person who created the display? A curator is a person in charge of collecting, preserving, displaying, and documenting museum objects.

In a small museum, the curator is often the only paid employee. The curator determines what objects to collect and how to safeguard them, as well as what research will be done. He or she plans the display of each object and decides what documentation will be used to tell its story. The same collection of objects can tell very different stories depending on how the curator interprets the historical data and chooses to display them.



As the only paid employee, the curator sometimes must also handle the finances and accounting for the museum. That can be a challenging task for a person who may not have any training in accounting. Also, the curator will likely have more interest in the preservation and communication of history than in the museum's finances.

Critical Thinking



Contact the curator of a museum either in person or via e-mail. Ask the curator if he or she had an accounting course. Also, ask the curator how knowledge of accounting would make him or her more effective in his or her job. Report your findings to the class.

Chapter 16: Financial Statements and Closing Entries for a Corporation: Lesson 16-4: Recording Closing Entries for Income Statement Accounts

Lesson 16-4: Recording Closing Entries for Income Statement Accounts

- LO4 Prepare closing entries.

Closing Entries LO4

Closing entries for a corporation are made from information in the adjusted trial balance. Closing entries for revenue and expense accounts are similar to those for proprietorships. A corporation's closing entries to close net income and temporary equity accounts are also similar to those for a proprietorship. However, these closing entries affect different accounts. A corporation records four closing entries:

1. A closing entry for income statement accounts with credit balances (revenue and contra-cost accounts).
2. A closing entry for income statement accounts with debit balances (cost, contra revenue, and expense accounts).
3. A closing entry to record net income or net loss in the Retained Earnings account and close the Income Summary account.
4. A closing entry for the Dividends account.

The Income Summary Account

At the end of a fiscal period, the temporary accounts are closed to prepare the general ledger for the next fiscal period. [CONCEPT: Matching Expenses with Revenue] To close a temporary account, an amount equal to its balance is recorded on the side opposite the balance. Amounts needed for the closing entries are obtained from the adjusted trial balance and from the statement of stockholders' equity. Closing entries are recorded in the general journal.

Chapter 8 discusses the difference between permanent accounts and temporary accounts.

Permanent accounts, also referred to as real accounts, include the asset and liability accounts as well as the owners' capital accounts. The ending account balances of permanent accounts for one fiscal period are the beginning account balances for the next fiscal period. Temporary accounts, also referred to as nominal accounts, include the revenue, cost, expense, and dividend accounts.

Another temporary account is used to summarize the closing entries for revenue, cost, and expenses. The account is titled Income Summary because it is used to summarize information about net income. Income Summary is used only at the end of a fiscal period to help prepare other accounts for a new fiscal period.

The Income Summary account is unique because it does not have a normal balance side. The balance of this account is determined by the amounts posted to the account at the end of a fiscal period. When revenue is greater than total expenses, resulting in a net income, the Income Summary account has a credit balance, as shown in the T account.

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



A corporation is not required to pay a dividend to its shareholders. Thus, some corporations only prepare three closing entries.

Closing Entry for Accounts with Credit Balances

ThreeGreen Products, Inc.		
Adjusted Trial Balance		
December 31, 20--		
ACCOUNT TITLE	DEBIT	CREDIT
Sales		632 371 75
Sales Discount	1 648 19	
Sales Returns and Allowances	3 941 57	
Purchases	254 851 26	
Purchases Discount		9 222 14
Purchases Returns and Allowances		1 495 01
Interest Income		5 570 00
Totals	842 324 77	842 324 77

GENERAL JOURNAL							PAGE 16
DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT		
	<i>Closing Entries</i>						
Dec. 31	Sales			632 371 75		1	
	Purchases Discount			9 222 14		2	
	Purchases Returns and Allowances			1 495 01		3	
	Interest Income			5 570 00		4	
	Income Summary				635 345 90	5	

ThreeGreen's adjusted trial balance has four income statement accounts with credit balances. One account, Sales, is a revenue account. Two accounts, Purchases Discount and Purchases Returns and Allowances, are contra cost accounts. The fourth account is an Other Revenue account. Each account has a normal credit balance that must be reduced to zero to prepare the account for the next fiscal period. [CONCEPT: Matching Expenses with Revenue]

To reduce each balance to zero, each account is debited for the amount of the balance. The impact of the closing entry on Sales is shown in the account. Income Summary is credited for \$635,345.90, the total of the four debits in closing entry.

Sales		T	
Closing	632,371.75	Bal.	632,371.75
		(New Bal.)	0.00
			this
Income Summary			
Adj. (mdse. inv.)	5,648.44	Closing	635,345.90
			(credit accounts)

The balance in Income Summary will be adjusted by other closing entries.

Closing Income Statement Accounts with Credit Balances

1. Write the heading, Closing Entries, in the middle of the general journal's Account Title column on a new page. This heading explains all of the closing entries that follow. Therefore, indicating a source document is unnecessary. The first closing entry is recorded on the first four lines below the heading.
2. Write the date, Dec. 31, 20--, in the Date column.
3. Write the account title of each revenue and contra cost account in the Account Title column. Write the balance of each revenue and contra cost account in the Debit column.
4. Write the title of the account credited, Income Summary, in the Account Title column, indented about one centimeter. Write the amount, \$635,345.90, in the Credit column.

Closing Entry for Income Statement Accounts with Debit Balances

DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT
	<i>Income Summary</i>			564844	
	<i>Sales</i>				63237175
	<i>Sales Discount</i>			164819	
	<i>Sales Returns and Allowances</i>			394157	
	<i>Purchases</i>			25485126	
	<i>Purchases Discount</i>				92214
	<i>Purchases Returns and Allowances</i>				149501
	<i>Advertising Expense</i>			468000	
	<i>Credit Card Fee Expense</i>			684220	
	<i>Utilities Expense</i>			496542	
	<i>Federal Income Tax Expense</i>			2362240	

GENERAL JOURNAL						PAGE 16
DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT	
31	<i>Income Summary</i>			54980089		
	<i>Sales Discount</i>				164819	
	<i>Sales Returns and Allowances</i>				394157	
	<i>Purchases</i>				25485126	
	<i>Advertising Expense</i>				468000	
	<i>Credit Card Fee Expense</i>				684220	
	<i>Depreciation Expense—Office Equipment</i>				748500	
	<i>Depreciation Expense—Store Equipment</i>				983000	
	<i>Insurance Expense</i>				820000	
	<i>Miscellaneous Expense</i>				349504	
	<i>Payroll Taxes Expense</i>				1669798	
	<i>Rent Expense</i>				840000	
	<i>Salary Expense</i>				18423495	
	<i>Supplies Expense—Office</i>				393817	
	<i>Supplies Expense—Store</i>				458461	
	<i>Uncollectible Accounts Expense</i>				238410	
	<i>Utilities Expense</i>				496542	
	<i>Federal Income Tax Expense</i>				2362240	

ThreeGreen's adjusted trial balance has many income statement accounts with debit balances—contra revenue accounts, Purchases, and the expense accounts. These debit balances must be reduced to zero to prepare the accounts for the next fiscal period. [CONCEPT: Matching Expenses

with Revenue] To reduce the balances to zero, the accounts are credited for the amount of their balances. Income Summary is debited for the total amount.

Closing Income Statement Accounts with Debit Balances

1. Write the date, 31, in the Date column.
2. Write the title of the account debited, Income Summary, in the Account Title column. The debit to Income Summary is not entered in the amount column until all contra revenue, cost, and expense balances have been journalized and the total amount calculated.
3. Write the account title of each contra revenue, cost, and expense account in the Account Title column, each indented about one centimeter. Write the balance of each account in the Credit column.
4. Add the credit amounts for this entry. Write the total of the credited accounts, \$549,800.89, in the Debit column on the same line as the account title Income Summary.

Summary of Closing Entry for Income Statement Accounts with Debit Balances

The second closing entry reduces the balance of the contra revenue, Purchases, and expense accounts to a zero balance. The effect of the closing entry on Purchases is shown in the T account.

After recording this closing entry, Income Summary has three amounts:

Purchases			
Bal.	254,851.26	Closing	254,851.26
<i>(New Bal.</i>	<i>0.00)</i>		

- A debit of \$5,648.44, the amount of the merchandise inventory adjustment.
- A credit of \$635,345.90, the amount of the entry to close the revenue and contra cost accounts.
- A debit of \$549,800.89, the amount of the entry to close the contra revenue, cost, and expense accounts.

Income Summary			
Adj. (mdse. inv.)	5,648.44	Closing (credit accounts)	635,345.90
Closing (debit accounts)	549,800.89	<i>(New Bal.</i>	<i>79,896.57)</i>

The credit balance of Income Summary, \$79,896.57, is equal to the net income after federal income tax amount shown on

the income statement. However, Income Summary is not closed as part of this closing entry. Instead,

the account is closed with the third closing entry when net income is recorded.

Closing Entry to Record Net Income

GENERAL JOURNAL							PAGE 16
DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT		
25	31	<i>Income Summary</i>		79 896 57		25	
26		<i>Retained Earnings</i>			79 896 57	26	
27						27	

Debit Income Summary

Credit Retained Earnings

After closing entries for the income statement accounts are posted, Income Summary has a credit balance of \$79,896.57. This credit balance equals the net income reported on the statement of stockholders' equity and income statement.

A corporation's net income should be recorded in the Retained Earnings account at the end of the fiscal year. After the closing entry is posted, Income Summary has a zero balance.

Income Summary			
Adj. (mdse. inv.)	5,648.44	Closing (credit accounts)	635,345.90
Closing (debit accounts)	549,800.89		
Closing (Retained Earnings)	79,896.57	(New Bal.)	0.00

Retained Earnings	
Bal.	65,218.84
Closing (Income Summary)	79,896.57
(New Bal.)	145,115.41

The new balance in Retained Earnings, \$145,115.41, does not yet equal the amount reported on the statement of stockholders' equity. A fourth closing entry is required to adjust Retained Earnings to the correct amount.

Closing Entry for Dividends

GENERAL JOURNAL							PAGE 16
DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT		
27	31	<i>Retained Earnings</i>		15 000 00		27	
28		<i>Dividends</i>			15 000 00	28	
29						29	

Debit Retained Earnings

Credit Dividends

Because dividends decrease the earnings retained by a corporation, the Dividends account is closed to Retained Earnings. After the closing entry is posted, Dividends has a zero balance. The amount of the Dividends account, \$15,000.00, has reduced the balance of Retained Earnings. The new balance in Retained Earnings, \$130,115.41, now equals the amount reported on the statement of stockholders' equity. Therefore, the Retained Earnings account is up to date.

Retained Earnings	
Closing (Dividends)	15,000.00
Bal.	65,218.84
Closing (Income Summary)	79,896.57
(New Bal.)	130,115.41

Dividends	
Bal.	15,000.00
(New Bal.)	0.00
Closing (Retained Earnings)	15,000.00

Completed Closing Entries for a Corporation Recorded in a Journal

GENERAL JOURNAL		PAGE 16			
DATE	ACCOUNT TITLE	DOC. NO.	POST. REF.	DEBIT	CREDIT
	<i>Closing Entries</i>				
Dec. 31	Sales			632 371 75	
	Purchases Discount			9 22 14	
	Purchases Returns and Allowances			1 49 5 01	
	Interest Income			5 57 00	
	Income Summary				635 345 90
31	Income Summary			549 800 89	
	Sales Discount				1 64 8 19
	Sales Returns and Allowances				3 94 1 57
	Purchases				254 851 26
	Advertising Expense				4 68 0 00
	Credit Card Fee Expense				6 84 2 20
	Depreciation Expense—Office Equipment				7 48 5 00
	Depreciation Expense—Store Equipment				9 83 0 00
	Insurance Expense				8 20 0 00
	Miscellaneous Expense				3 49 5 04
	Payroll Taxes Expense				16 69 7 98
	Rent Expense				8 40 0 00
	Salary Expense				184 234 95
	Supplies Expense—Office				3 93 8 17
	Supplies Expense—Store				4 58 4 61
	Uncollectible Accounts Expense				2 38 4 10
	Utilities Expense				4 96 5 42
	Federal Income Tax Expense				23 62 2 40
31	Income Summary			79 896 57	
	Retained Earnings				79 896 57
31	Retained Earnings			15 000 00	
	Dividends				15 000 00

After all closing entries have been recorded, ThreeGreen's general journal appears as shown above. The next step is to post these closing entries to the general ledger.

It is not uncommon for a business to have hundreds, even thousands, of accounts. Preparing a closing entry by entering each account balance would be a monumental task subject to human error. Computerized accounting systems provide a single command that prepares and posts the entries.

End of Lesson Review

- LO4 Prepare closing entries.

Audit Your Understanding

1. Where is the information obtained to journalize closing entries for revenue, cost, and expenses?
2. What is the name of the temporary account used to summarize the closing entries for revenue, cost, and expenses?

Work Together 16-4

Journalizing closing entries

Use Superior Corporation's trial balance and financial statements from Work Together 16-3. A general journal is given in the Working Papers. Your instructor will guide you through the following example.

Record the following closing entries on page 19 of the general journal.

- a. Close the income statement accounts with credit balances.
- b. Close the income statement accounts with debit balances.
- c. Close the Income Summary account.
- d. Close the Dividends account.

On Your Own 16-4

Journalizing closing entries

Use Eastern Imports' trial balance and financial statements from On Your Own 16-3. A general journal is given in the Working Papers. Work this problem independently.

Record the following closing entries on page 25 of the general journal.

- a. Close the income statement accounts with credit balances.
- b. Close the income statement accounts with debit balances.
- c. Close the Income Summary account.
- d. Close the Dividends account.

Chapter 16: Financial Statements and Closing Entries for a Corporation: Global Awareness: Major Changes in China's Accounting Standards

Global Awareness: Major Changes in China's Accounting Standards

Critical Thinking

When the People's Republic of China (PRC) was formed in 1949, all the businesses in China came under state ownership. This meant that companies were owned and controlled by the government. All accounting standards were determined by the government. The accounting system and financial statements focused on accounting for state-owned assets. There was no measure of profit or loss and no accounting for the debts of an organization.

Since 1979, new laws have been passed that allow foreign investors to invest in Chinese businesses. As a result of demands by these foreign investors, Chinese accounting standards began to change. The standards moved Chinese accounting away from just measuring and recording assets to a focus on profit and loss.

These new standards paved the way for a major change to occur in Chinese accounting standards in 2006. The Ministry of Finance announced new rules called Accounting Standards for Business Enterprises (or ASBEs). With only a few exceptions, the ASBEs follow the International Financial Reporting Standards (IFRS).

This move to ASBEs has resulted in great savings for Chinese corporations. At one point in time, a Chinese company that sold shares of stock in the United States had to prepare three sets of financial statements—one following the original standards established by the PRC, one following IFRS, and one following U.S. GAAP. Since 2008, the U.S. Securities and Exchange Commission (SEC) has allowed foreign companies selling shares of stock in the United States to submit financial statements prepared following IFRS. Today, Chinese businesses selling shares of stock in the United States only have to prepare one set of financial statements, using the new ASBEs.

Critical Thinking



3. Use the Internet to research China's ASBEs and IFRS. (IFRS were discussed in the Global Awareness feature in Chapter 10.)
4. List one area in which the ASBEs differ from IFRS.

Chapter 16: Financial Statements and Closing Entries for a Corporation: Lesson 16-5: Preparing a Post-Closing Trial Balance

Lesson 16-5: Preparing a Post-Closing Trial Balance

- LO5 Prepare a post-closing trial balance.

General Ledger after Closing Entries are Posted

ACCOUNT Merchandise Inventory				ACCOUNT NO. 1140			
DATE	ITEM	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
Dec. 31	Balance	✓			108 4 8 6 44		
31		G15		5 6 4 8 44	102 8 3 8 00		

ACCOUNT Retained Earnings				ACCOUNT NO. 3130			
DATE	ITEM	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
Dec. 1	Balance	✓			65 2 1 8 84		
31		G16		79 8 9 6 57	145 1 1 5 41		
31		G16	15 0 0 0 00		130 1 1 5 41		

ACCOUNT Dividends				ACCOUNT NO. 3140			
DATE	ITEM	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
Dec. 31	Balance	✓			15 0 0 0 00		
31		G16		15 0 0 0 00			

ACCOUNT Income Summary				ACCOUNT NO. 3150			
DATE	ITEM	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
Dec. 31		G15	5 6 4 8 44		5 6 4 8 44		
31		G16		635 3 4 5 90	629 6 9 7 46		
31		G16	549 8 0 0 89		79 8 9 6 57		
31		G16	79 8 9 6 57				

ACCOUNT Sales				ACCOUNT NO. 4110			
DATE	ITEM	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
Dec. 31	Balance	✓			632 3 7 1 75		
31		G16	632 3 7 1 75				

Closing entries do not change asset and liability accounts such as Merchandise Inventory. Revenue,

cost, and expense accounts, such as Sales, have zero balances.

Three closing entries affect Income Summary: the \$635,345.90 credit closes the credit accounts; the \$549,800.89 debit closes expense accounts; the \$79,896.57 debit, ThreeGreen's net income after federal income tax, is closed to Retained Earnings leaving Income Summary with a zero balance. The \$15,000.00 balance in Dividends is also closed to Retained Earnings leaving Dividends with a zero balance. The ledger is now ready for the next fiscal period.

Post-Closing Trial Balance LO5

ThreeGreen Products, Inc. Post-Closing Trial Balance December 31, 20--				
ACCOUNT TITLE	DEBIT	CREDIT		
Cash	54 194 34			
Petty Cash	2 500 00			
Accounts Receivable	20 381 81			
Allowance for Uncollectible Accounts		2 509 25		
Merchandise Inventory	102 838 00			
Supplies—Office	6 100 00			
Supplies—Store	4 650 00			
Prepaid Insurance	2 800 00			
Notes Receivable	6 200 00			
Interest Receivable	9 300 00			
Office Equipment	24 895 18			
Accumulated Depreciation—Office Equipment		13 674 00		
Store Equipment	59 148 11			
Accumulated Depreciation—Store Equipment		18 325 00		
Accounts Payable		16 489 10		
Sales Tax Payable		3 574 64		
Employee Income Tax Payable—Federal		9 500 00		
Social Security Tax Payable		2 023 06		
Medicare Tax Payable		4 731 14		
Health Insurance Premiums Payable		4 600 00		
Retirement Benefits Payable		4 650 00		
Unemployment Tax Payable—Federal		2 977 02		
Unemployment Tax Payable—State		1 477 42		
Federal Income Tax Payable		3 622 40		
Dividends Payable		3 750 00		
Capital Stock		75 000 00		
Retained Earnings		130 115 41		
Totals	271 875 44	271 875 44		

A post-closing trial balance is prepared to prove the equality of debits and credits in the general ledger. Account balances on the post-closing trial balance agree with the balances on the balance sheet shown on page 491.

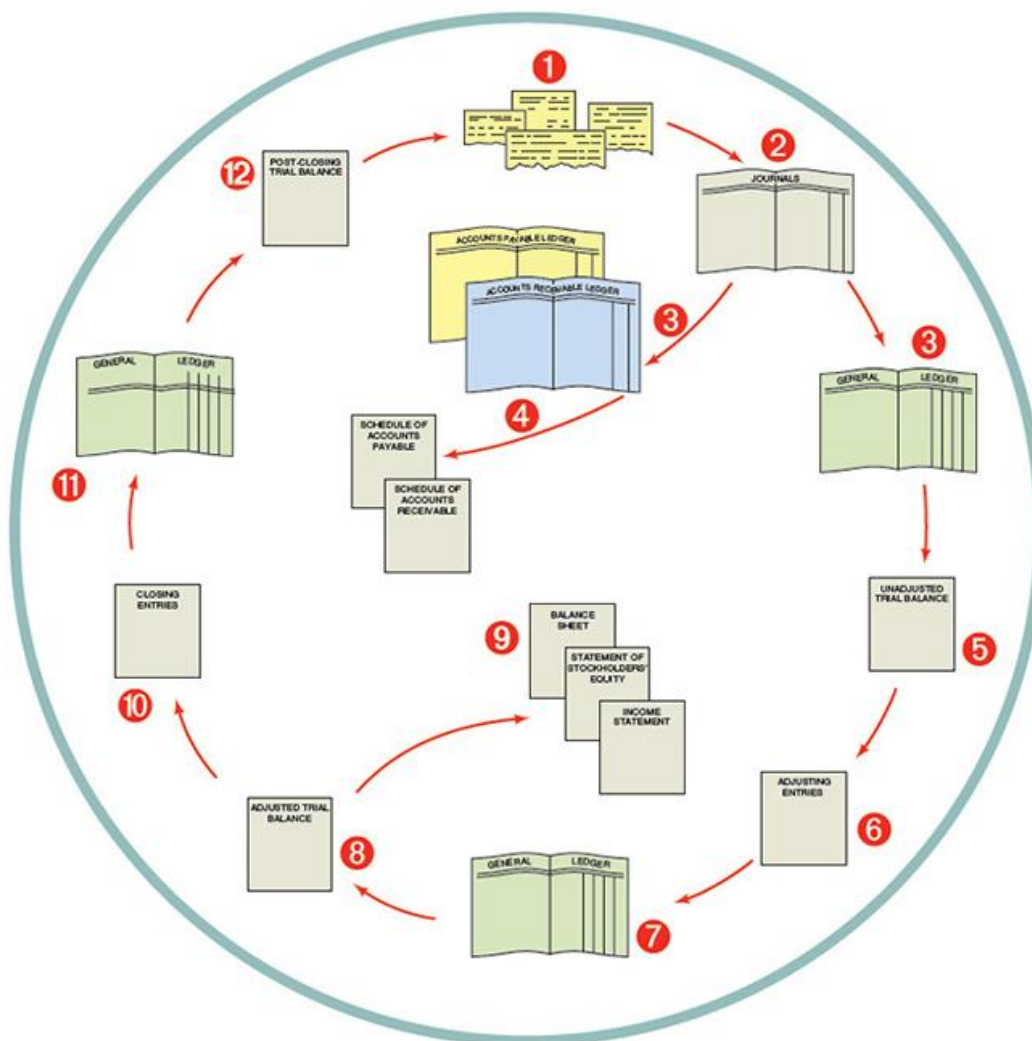
Recording adjusting and closing entries can be a time-consuming process for large, multinational companies. After financial statements are prepared, an audit still must still be performed. More

adjustments may result from the audit. For this reason, the SEC allows publicly held companies up to three months to submit their financial statements.

Preparing a Post-Closing Trial Balance

1. Write the post-closing trial balance heading on three lines.
2. List all general ledger accounts that have balances in the Account Title column.
3. Write the balance of each asset account in the Debit column. Write the balance of each contra asset, liability, and capital account in the Credit column.
4. Write the word Totals on the next line below the last account title.
5. Total the columns and write the totals, \$271,875.44, on the Totals line.
6. Verify that the column totals equal. Rule double lines below both column totals.

Accounting Cycle for a Merchandising Business Organized as a Corporation



Service and merchandising businesses use a similar accounting cycle. The accounting cycles are also similar for a proprietorship and a corporation. Variations occur when subsidiary ledgers are used. Variations also occur in preparing financial statements.

Using the Accounting Cycle for a Merchandising Business

1. Source documents are checked for accuracy, and transactions are analyzed into debit and credit parts.
2. Transactions, from information on source documents, are recorded in journals.
3. Journal entries are posted to the accounts payable ledger, the accounts receivable ledger, and the general ledger.
4. Schedules of accounts payable and accounts receivable are prepared from the subsidiary ledgers.
5. An unadjusted trial balance is prepared from the general ledger.
6. Adjusting entries are journalized.
7. Adjusting entries are posted to the general ledger.
8. An adjusted trial balance is prepared from the general ledger.
9. Financial statements are prepared from the adjusted trial balance.
10. Closing entries are journalized.
11. Closing entries are posted to the general ledger.
12. A post-closing trial balance is prepared from the general ledger.

End of Lesson Review

- LO5 Prepare a post-closing trial balance.

Audit Your Understanding

1. Which accounts and balances are listed on a post-closing trial balance? In what order are they listed?
2. What is the purpose of preparing a post-closing trial balance?
3. What two steps in the accounting cycle occur after adjusting entries are posted to the general ledger?

Work Together 16-5

Preparing a post-closing trial balance

Plumbing Central's December 31 account balances for the current year are shown below. The balances include the adjusting and closing entries. Your instructor will guide you through the following example.

Account	Balance
Cash	\$ 12,810.20
Petty Cash	350.00
Accounts Receivable	18,398.80
Allowance for Uncollectible Accounts	1,200.00
Merchandise Inventory	140,980.00
Supplies—Store	2,268.00
Prepaid Insurance	1,980.00
Accounts Payable	11,676.50
Sales Tax Payable	1,584.00
Capital Stock	50,000.00
Retained Earnings	112,326.50

Prepare a post-closing trial balance on the form provided in the Working Papers.

On Your Own 16-5

Preparing a post-closing trial balance

Foreign Auto Supply's December 31 account balances for the current year are shown below. The balances include the adjusting and closing entries. Work this problem independently.

Account	Balance
Cash	\$ 13,485.00
Merchandise Inventory	121,152.00
Supplies—Office	741.00
Notes Receivable	3,560.00
Equipment	35,487.00
Accumulated Depreciation—Equipment	12,450.00
Accounts Payable	23,154.00
Sales Tax Payable	1,548.00
Federal Income Tax Payable	2,489.00
Dividends Payable	5,000.00
Capital Stock	75,000.00
Retained Earnings	54,784.00

Prepare a post-closing trial balance on the form provided in the Working Papers.

Chapter 16: Financial Statements and Closing Entries for a Corporation: End of Chapter Review

End of Chapter Review

Using the System Manager to Navigate a Computerized Accounting System

Computerized accounting systems are typically composed of from five to several dozen modules. The modules are individual applications that perform unique functions. Modules tend to mirror the specific functions performed in an accounting department: general ledger, accounts receivable, accounts payable, payroll, etc. These individual applications are linked together by another module—a controlling program often called the system manager. The system manager acts as a portal to each of the modules and provides utilities that are shared by each of them. For example, banking functions need to be accessed by both Accounts Payable and Accounts Receivable modules, and banking transactions affect General Ledger accounts. So the banking utility works best as part of the system manager. Likewise, reports are used in virtually all modules, so the Reports utility usually resides within the system manager as well.

Most small-business accounting systems contain the six modules illustrated below, although there are variations. One software consultant counted over 90 different modules available for computerized accounting systems. The larger and more complex a business is, the more modules it is likely to need. Many accounting systems allow businesses to add modules as they grow. These added modules, or applications, are also accessed by the user through the system manager. A few examples of these additional modules would be Human Resource Management, Customer Service, Web Business Tools, and Point-of-Sale.



1 The General Ledger module contains all general ledger accounts. Accounts are created, edited, or deactivated by selecting Chart of Accounts.

- A trial balance can be viewed or printed at any time.
- Some common reports are made available to the user directly from the modules. They may be listed under the module heading, as illustrated above. The user has selected the income statement. The reports listed here could also be accessed from the module's main menu. A larger number of reports, especially custom reports, are accessed by clicking on the Reports button. Examples might include an income statement with a vertical analysis and a statement of stockholders' equity.

2 The Accounts Receivable module is primarily designed to manage a business's customer accounts. Cash receipts are linked to the banking utility and the general ledger accounts.

- Some computerized accounting systems provide separate modules for sales orders. Some, like the one illustrated here, include basic sales entry functions in the Accounts Receivable module.
- Businesses that sell in several states and municipalities will encounter sales tax rates that vary from state to state, from county to county, and from city to city. The wider a business's operating area, the more likely it is to need a sales tax management utility. It can be included in a

module, as it is here, or it can be a module on its own.

3 The Accounts Payable module is primarily designed to manage a business's vendor accounts. The cash payments function is linked to the banking utility and the general ledger accounts.

- Purchase orders can be a part of the Accounts Payable module, as shown here, or a separate module.
- Managing sales tax as part of the purchasing process is less complex than it is for sales. These taxes are paid to vendors. However, some purchases may be tax-exempt. States generally require businesses to file reports of their tax-exempt purchases. This utility helps to manage that obligation.

4 Recall that computerized accounting systems use perpetual inventory systems (Chapter 9, Lesson 9-2). The Inventory module is designed to track the receipt and sale of inventory items and to maintain a record of the cost of each item. When a sale is recorded in the Accounts Receivable module, items sold are automatically deducted from the inventory on hand. The cost of the items is automatically recorded in the Cost of Merchandise Sold account. You will learn more about inventory in Chapter 20.

5 The Payroll module is designed to manage a business's employee records and to enable the business to accurately and efficiently compensate its employees. Many small businesses contract with payroll service providers to handle their payroll. In that case, this module would not be in active use.

6 Plant assets, commonly called fixed assets, are managed through the Plant Assets module. Depreciation and property taxes are managed in this module as well. You will learn more about plant assets in Chapter 19.

7 Some large business organizations operate multiple companies. Most computerized accounting systems allow businesses to handle the accounting for more than one business. When there is more than one company, the company for which transactions are to be entered is selected by clicking on the Company button.

8 As with most application software, the publisher of the application periodically releases updates. The Update button accesses those releases. The Tutorials button allows the user to learn how to use the features of the system. The software publisher usually provides these tutorials as part of the software.

Financial Statements and Closing Entries for a Corporation: Chapter Summary

Financial statements are prepared using information from three sources: (1) end-of-fiscal-period account balances from the adjusted trial balance, (2) selected beginning account balances from general ledger accounts, and (3) amounts calculated on another financial statement.

The income statement of a merchandising business has four main sections: (1) Operating Revenue, (2) Cost of Merchandise Sold, (3) Operating Expenses, and (4) Other Revenue. The Operating Revenue section uses sales less its contra accounts to calculate net sales. The Cost of Merchandise Sold section uses the amounts of merchandise inventory, purchases, and purchases contra accounts to calculate the cost of merchandise sold. The cost of merchandise sold is subtracted from net sales to calculate the gross profit. The total of all operating expense accounts, subtracted from gross profit, equals income from operations. The Other Revenue section contains any revenue account not directly related to the normal operating activities of the business. Federal income tax expense is then deducted to yield net income after federal income tax.

The statement of stockholders' equity reports the changes in equity accounts. The statement contains two sections: (1) Capital Stock and (2) Retained Earnings. Each section begins with the beginning balance and reports changes during the fiscal period.

The balance sheet reports the asset and liability accounts on the adjusted trial balance. Assets are classified as current assets and plant assets. The book value of any account having a contra asset account is presented. Stockholders' equity amounts are obtained from the statement of stockholders' equity.

Temporary accounts are closed after financial statements are prepared. Four entries are recorded: (1) income statement accounts with credit balances, (2) income statement accounts with debit balances, (3) net income to retained earnings, and (4) dividends to retained earnings. After the closing entries are posted, a post-closing trial balance is prepared. The post-closing trial balance is prepared to ensure that the general ledger is prepared for the next fiscal period.

Financial Statements and Closing Entries for a Corporation: Explore Accounting

Alternative Fiscal Years

Many small companies use a fiscal year that is the same as the calendar year, January 1 to December 31. However, there may be several reasons why a different fiscal period would be beneficial. If the calendar year-end comes in the middle of a high sales period, a fiscal year ending at this time can be more difficult. All employees are extremely busy with sales and shipping. Because of this activity, accurately identifying sales, inventory, and accounts receivable is more difficult. If the calendar year-end comes just before the high sales period begins, an analysis of the company's financial condition will not be as favorable. The company may have borrowed money to buy a high level of inventory, so the company has higher debt and high inventory levels. Therefore, some companies choose to use a natural business year as the fiscal year, as discussed in Chapter 6.

Baker's Dozen, Inc., is a corporation that makes and sells decorative cakes, cookies, and candies. Approximately 90% of its sales are made between November 1 and February 15 because of the three holidays of Thanksgiving, Christmas, and Valentine's Day. The company spends six months—May to November—preparing for its heavy sales period. The company has selected April 1 to March 31 as its fiscal year. By March 31, inventory is low, most accounts receivable have been collected, and the company has not yet replaced inventory to begin preparing for the next season. Thus, this is an ideal time to end the fiscal year. Inventory is easier to count, the level of accounts receivable is lower, and more employees are available to help with the closing activities.

Instructions

What other types of companies may find it beneficial to use a fiscal year different from the calendar year? What would be the ideal fiscal period for these companies? You may wish to find a local business that has a fiscal period different from the calendar year. If so, determine the reasons for selecting the fiscal period it now uses.

Financial Statements and Closing Entries for a Corporation: Apply Your Understanding: Application Problem

INSTRUCTIONS: Download problem instructions for Excel, QuickBooks, and Peachtree from the textbook companion website at www.C21accounting.com.

16-1 Application Problem: Preparing an Income Statement for a Merchandising Business LO1

A form for completing this problem and an adjusted trial balance for Top-Light Corporation for the

year ended December 31 of the current year are given in the Working Papers. The beginning balance of Merchandise Inventory is \$90,260.72. Save your work to complete Problem 16-2.

Instructions:

1. Prepare an income statement.
2. Prepare a vertical analysis of each amount in the fourth amount column. Round percentage calculations to the nearest 0.1%.

16-2 Application Problem: Preparing a Statement of Stockholders' Equity LO2

A form for completing this problem is given in the Working Papers. Use the income statement and trial balance from Problem 16-1. Save your work to complete Problem 16-3.

Instructions:

Prepare a statement of stockholders' equity for Top-Light Corporation for the fiscal year ended on December 31 of the current year. Use the following additional information.

Capital stock outstanding on January 1	2,000 shares
Capital stock issued during the year	300 shares
Capital stock par value	\$25.00
Retained earnings, January 1	\$50,403.31

16-3 Application Problem: Preparing a Balance Sheet for a Corporation LO3

A form for completing this problem is given in the Working Papers. Use the trial balance and financial statements from Problem 16-2. Save your work to complete Problem 16-4.

Instructions:

Prepare a balance sheet for the current year.

16-4 Application Problem: Journalizing Closing Entries LO4

Use Top-Light Corporation's trial balance and financial statements from Problems 16-1 and 16-2. A general journal is given in the Working Papers.

Instructions:

Record the following closing entries on page 21 of the general journal.

- a. Close the income statement accounts with credit balances.
- b. Close the income statement accounts with debit balances.
- c. Close the Income Summary account.
- d. Close the Dividends account.



1. Journalize and post closing entries to the general journal.
2. Make the selections to print the balance sheet and income statement.
3. Make the selections to print the general journal and the post-closing trial balance.



1. Journalize and post adjusting entries to the journal.
2. Make the selections to print the balance sheet and the profit and loss statement.
3. Make the selections to print the journal and the post-closing trial balance.



1. Key the account balances in the trial balance section of the worksheet.
2. Use the required formulas to calculate the totals of the Trial Balance columns.
3. Key the closing entries in the Adjustments columns.
4. Create the appropriate formulas to extend amounts to the income statement and balance sheet.



1. Go to www.cengage.com/login
2. Click on AA Online to access.
3. Go to the online assignment and follow the instructions.

16-5 Application Problem: Preparing a Post-Closing Trial Balance LO5



1. Go to www.cengage.com/login
2. Click on AA Online to access.
3. Go to the online assignment and follow the instructions.

MidSouth Electric's balance sheet accounts with December 31 balances for the current year, after adjusting and closing entries have been posted, are shown below.

Account	Balance
Cash	\$ 23,524.22
Petty Cash	250.00
Accounts Receivable	23,643.44
Allowance for Uncollectible Accounts	3,980.00

Merchandise Inventory	156,262.33
Supplies	352.00
Notes Receivable	6,490.00
Interest Receivable	\$ 32.45
Accounts Payable	11,676.50
Sales Tax Payable	1,584.00
Federal Income Tax Payable	3,790.00
Dividends Payable	4,000.00
Capital Stock	72,000.00
Retained Earnings	113,523.94

Instructions:

Prepare a post-closing trial balance on the form provided in the Working Papers.

Financial Statements and Closing Entries for a Corporation: Apply Your Understanding: Mastery Problem

16-M Mastery Problem: Preparing Financial Statements and Closing Entries LO1, 2, 3, 4

The adjusted trial balance for Paulson Corporation for the year ended December 31 of the current year and forms for completing this problem are given in the Working Papers. The beginning balance of Merchandise Inventory is \$112,825.90.

Instructions:

1. Prepare an income statement.
2. Prepare a vertical analysis of each amount in the fourth amount column. Round percentage calculations to the nearest 0.1%.
3. Prepare a statement of stockholders' equity. The company had 4,500 shares of \$10.00 par value stock outstanding on January 1. The company issued an additional 500 shares during the year.
4. Prepare a balance sheet for the current year.
5. Journalize the closing entries on page 19 of the general journal.



1. Journalize and post closing entries to the general journal.
2. Make the selections to print the balance sheet and income statement.
3. Make the selections to print the general journal and the post-closing trial balance.



1. Journalize and post adjusting entries to the journal.
2. Make the selections to print the balance sheet and the profit and loss statement.
3. Make the selections to print the general journal and the post-closing trial balance.



1. Key the account balances in the trial balance section of the worksheet.
 2. Use the required formulas to calculate the totals of the Trial Balance columns.
 3. Key the closing entries in the Adjustments columns.
 4. Create the appropriate formulas to extend amounts to the income statement and balance sheet.
- Financial Statements and Closing Entries for a Corporation: Apply Your Understanding: Challenge Problem

16-C Challenge Problem: Preparing an Income Statement LO1

Selected sections of the adjusted trial balance for KLT Corporation are presented in the Working Papers. The corporation's chart of accounts contains several sales accounts. KLT Corporation also has an account for interest expense. A form for completing this problem is also given in the Working Papers. The beginning balance of Merchandise Inventory is \$66,964.96.

Instructions:

1. Prepare the income statement for KLT Corporation.
2. Prepare a vertical analysis of the income statement.

Financial Statements and Closing Entries for a Corporation: 21st Century Skills

Should You Buy Stock?

Theme: Financial, Economic, Business, and Entrepreneurial Literacy

Skills: Creativity and Innovation, Critical Thinking and Problem Solving, Communication and

Collaboration, ICT Literacy

A share of stock is a unit of ownership in a corporation. Stock may be purchased by individuals, investment companies, pension funds, institutions, banks, and other companies. Publicly traded stocks are bought and sold on stock exchanges throughout the world. Ownership of a corporation's stock entitles the owner to distributions of earnings if dividends are declared. Many investors, however, buy stock with the expectation that it will increase in value and the stock can be sold for a profit.

Stock ownership entitles the owner to vote at stockholders' meetings proportional to the number of shares owned. Important issues regarding the corporation may be decided at these meetings including the election of the members of the board of directors. Sometimes an individual or group of stockholders will attempt to gain a majority of a company's stock in order to elect their choice of directors and thus take control of the company.

Investors might determine which stocks they will purchase based on political or social issues. For example, an investor might buy stocks only of companies that have environmental policies. Another investor might buy stocks only of companies that have family-friendly policies allowing for a balance in work and family life for their employees.

Application

1. Assume that as a stockholder you are responsible for selecting the membership of the board of directors for a new social network company. Identify 9–11 individuals (by name or title) whom you would like to serve on the board of directors. Explain why each individual would be a valuable contributor.
2. Compose a letter to one of these individuals asking them to serve on the board of directors for your company. Using persuasion, explain why their involvement would be beneficial to everyone.
3. Many investors are unsure of the right time to buy or sell stock. Using websites like www.finance.yahoo.com, research dollar cost averaging, a common investment strategy. Write a financial advice column explaining to new investors the meaning of this concept and how it can be implemented.

Financial Statements and Closing Entries for a Corporation: Analyzing Nike's Financial Statements

Nike has two classes of common stock—Class A and Class B. The majority of Class A stock is

owned by Philip H. Knight, cofounder and chairman of the board of directors. This class of stock has different voting rights than Class B stock. For example, the Class A stockholders can elect three-fourths of the members of the board of directors. This right allows the Class A stockholders to have more control over the individuals who govern the corporation. Class B shares are publicly traded under the symbol NKE. Quarterly dividends are paid to both classes of stock.

Class A stockholders also have the right to convert their shares, one for one, into Class B shares. This right allows Class A stockholders to sell their shares on the stock market.

Instructions

Use the Consolidated Statements of Shareholders' Equity on pages B-8 and B-9 of Appendix B to answer the following questions.

1. How many shares of Class A and Class B shares are outstanding as of May 31, 2011?

2. How many Class A shares were converted into Class B shares in fiscal year 2011?

What change in the dollar amounts of the stockholders' equity accounts results from Class A stock being issued to employees?