THE WORKSHEET and CLOSING ENTRIES

I. **Review of Key Concepts and Terms:**

A. The purpose of the worksheet

1. To **show that the accounts of the business are in balance (debits = credits) and to provide, in one location, a systematic and comprehensive reconciliation of the accounts from trial balance to financial statements**. The worksheet starts with pre-closing trial balance amounts adding adjusting, closing and reversing entries and produces a post closing trial balance from which the adjusted account balances are placed in the appropriate financial statements (i.e. balance sheet accounts are positioned on the balance sheet and income statement accounts on the income statement).
2. The worksheet is *not a formal accounting record* such as the journal or the ledger, rather it is a tool used to assist the accountant in the preparation of the Balance Sheet and Income Statement. **The primary benefit of the worksheet lies in its ability to demonstrate that the accounts are in balance at the end of the period, through the adjusting process.** By demonstrating that the accounts are in balance from the pre-closing trial balance through the adjusting and closing process to the post closing trial balance the worksheet greatly reduces the probability of errors in the financial statements.

B. Closing Entries

1. Closing entries are those entries made at the end of the accounting period to close the nominal (income statement) accounts. Because the income statement measures income for a specific period, income statement accounts must start each measurement period with a zero balance. During the accounting period revenues and expenses are recorded in these accounts, and at the end of the period we can deduct the expenses incurred during the period from the revenues earned in order to determine the net income of the period. We call these expense and revenue accounts **nominal** or **temporary** because they have balances only during the accounting period and must be eliminated (reduced to zero balance) at the end of the period so that the next measurement period starts with zero balances. This process insures that only the revenues and expenses of a specific period are used to compute the net income of that period.

C. The Closing Process Demonstrated

1. Consider the following facts for Shane and Co., CPA's:

Revenues....................................	$	500,000
Administrative expenses.....................		120,000
Rent		80,000
Miscellaneous expenses......................		25,000

Step 1. Close the revenue accounts to the expense and revenue summary.

Revenues....................................	500,000	
Expense and Revenue Summary............		500,000

Step 2. Close the expense accounts to the expense and revenue summary.

Expense and revenue summary..........	225,000	
Administrative expenses................		120,000
Rent		80,000
Miscellaneous expense..................		25,000

Step 3. Close the expense and revenue summary (income summary) to the statement of retained earnings (or the balance sheet if no statement of retained earnings is to be produced).

Expense and revenue summary...........	275,000	
Retained Earnings.............................		275,000

Account	Debit	Credit
Revenues	a)500,000	500,000
		-0-
Admin. Exp.	120,000	b)120,000
		-0-
Rent Exp.	80,000	b) 80,000
		-0-
Misc. Exp	25,000	b) 25,000
		-0-
Expense and Revenue Summary	b) 120,000	a) 500,000
	b) 80,000	
	b) 25,000	
		275,000 Bal
	c) 275,000	
		-0-
	Net Loss	Net Income
Retained Earnings		c) 275,000

Note: Dr side is net loss/Cr side in NI →

Note: the expense and revenue summary account is used only to close the nominal accounts at the end of the accounting period. If revenues exceed expenses, the account will have a credit balance representing net income. Alternatively, if expenses exceed revenues, the account will have a debit balance and the debit balance in the account will represent net loss.

D. The Post-Closing Trial Balance

1. The purpose of the Post-closing trial balance is to prove that the accounts remain in balance after the adjusting and closing process. In addition, no nominal (income statement) accounts should appear in the post-closing trial balance because they should have been closed (have zero balance).

E. The Accounting Process Reviewed

1. Steps occurring continuously during the period:
   a. Transactions analyzed and **recorded in the journal**
   b. Transactions are **posted to the ledger**
2. Steps occurring during interim or year-end reporting:
   a. **Pre-closing** trial balance is prepared
   b. **adjusting entries** are prepared to bring the accounts up to date. Note that adjusting and closing entries made for interim reporting purposes are normally not "booked" i.e. they are not recorded in the ledger. The booking of adjusting and closing entries is normally reserved for the year end adjusting and closing process when a careful review of the entire years activities can be made.
   c. **post-closing** trial balance is prepared to insure the accounts remain in balance after the adjusting process. Note that during the preparation of interim period financial statements, the closing entries must be reversed in order to continue to accrue revenues and expenses for the remainder of the accounting period.
   d. **interim financial statements are produced**
3. **S**teps occurring only at fiscal year end:
   a. **year end financial statements are produced** and **adjusting and closing entries are booked to the ledger.**

F. Reversing Entries

1. The purpose of reversing entries is to **simplify** the subsequent recording of recurring accruals of expense and revenue transactions.
2. reversing entries are **optional** and are normally made by the accounting staff in an effort to standardize and simplify the work of less skilled bookkeeping personnel.
3. **Reversing entry illustration**: The process involved in utilizing reversing entries is illustrated below;

Assume the following facts:
--LBSU Inc. signed a 1 year office lease on September 15, 19x1 calling for twelve rental payments of $4,000 per month, payable in advance commencing on September 15, 19x1 and ending on August 15, 19x2.

Event	Accrued Expense is Reversed			Accrued Expense is **not** Reversed		
12/31/x1						
Adjusting entry to	Rent Exp..........	2,000		Rent Exp..........	2,000	
accrue rental expense	Rent Payable....		2,000	Rent Payable.........		2,000
12/31/x1						
Closing entry to	Income Summary....	2,000		Income Summary....	2,000	
accrue rental expense	Rent Expense........		2,000	Rent Expense.....		2,000
1/1/x1						
Reversing Entry	Rent Payable......		2,000	No Entry		
	Rent Expense........		2,000			
1/15/x2						
Payment of Rent	Rent Expense......	4,000		Rent Expense......	2,000	
	Cash............		4,000	Rent Payable......		2,000
				Cash............		4,000

> Note that the result of the reversing entry is to permit the normal ($4,000 per month) rental expense accrual, whereas without the reversing entry, only the $2,000 applicable to expense in the current period is recognized. **The end result is the same whether or not the reversing entry is made**.

4. Reversing entries can minimize the possibility of errors by allowing bookkeeping personnel to make the same entries each period even when the period does not fall on the accrual date.

> **Simple rule for reversing entries:**
> --reverse any previous year's adjusting entry to a nominal account that is followed by a cash payment or receipt at the beginning of the subsequent period.

KEY CONCEPT COMPREHENSION

1. The use of the worksheet permits the preparation of the ________ without posting the adjusting entries.

2. The expense accounts are transferred from the adjusted trial balance columns of the worksheet to the __________ columns.

3. The all balance sheet accounts are referred to as ________ accounts.
4. Reversing entries are always required for ________ accounts.

5. A tool for expediting the process of preparing financial statements is called a________.

6. At the end of an accounting period, the only accounts with balances are the _____ accounts.

7. __________ are required at the end of the accounting period to close the __________ accounts.

8. The accounting cycle ends with the ____________ .

9. _______ and ______ accounts are closed to the ______ account.

TRUE OR FALSE

1. Reversing entries are not required for all adjusting entries.

2. The worksheet must always be prepared before the financial statements are prepared.

3. A post-closing trial balance contains only temporary accounts.

4. Temporary accounts have no effect on retained earnings or shareholders' equity.

5. The balance sheet accounts are the only accounts shown in the post- closing trial balance.

6. The use of a worksheet eliminates the necessity of formally closing an organization's books at the end of the fiscal year.

7. The closing of a revenue or expense account brings its balance to zero.

8. Worksheets eliminate the need for entering and posting the adjusting entries in the general journal and the general ledger, respectively.

9. A balance sheet contains only the balances from permanent ("real") accounts.

Multiple Choice

1.Factors that shape an accounting information system include the
   a. nature of the business.
   b. size of the firm.
   c. volume of data to be handled.
   d. all of these.

2. Which of the following criteria must be met before an event or item should be recorded for accounting purposes?
   a. The event or item can be measured objectively in financial terms.
   b. The event or item is relevant and reliable.
   c. The event or item is an element.
   d. All of these must be met.

3. Which of the following is a recordable event or item?
   a. Changes in managerial policy
   b. The value of human resources
   c. Changes in personnel
   d. None of these

4. Which of the following is *not* an internal event?
   a. Depreciation
   b. Using raw materials in the production process
   c. Dividend declaration and subsequent payment
   d. All 0f these are internal transactions.

5. An accounting record into which the essential facts and figures in connection with all transactions are initially recorded is called the
   a. ledger.
   b. account.
   c. trial balance.
   d. none of these.

6. The debit and credit analysis of a transaction normally takes place

a. before an entry is recorded in a journal.
b. when the entry is posted to the ledger.
c. when the trial balance is prepared.
d. at some other point in the accounting cycle.

*7. Under the cash basis of accounting, revenues are recorded
a. when they are earned and realized.
b. when they are earned and realizable.
c. when they are earned.
d. when they are realized.

*8. When converting from cash basis to accrual basis accounting, which of the following adjustments should be made to cash receipts from customers to determine accrual basis service revenue?
a. Subtract ending accounts receivable.
b. Subtract beginning unearned service revenue.
c. Add ending accounts receivable.
d. Add cash sales.

*9. When converting from cash basis to accrual basis accounting, which of the following adjustments should be made to cash paid for operating expenses to determine accrual basis operating expenses?
a. Add beginning accrued liabilities.
b. Add beginning prepaid expense.
c. Subtract ending prepaid expense.
d. Subtract interest expense.

10. A trial balance
a. proves that debits and credits are equal in the ledger.
b. supplies a listing of open accounts and their balances that are used in preparing financial statements.
c. is normally prepared three times in the accounting cycle.
d. all of these.

11. A trial balance may prove that debits and credits are equal, but
a. an amount could be entered in the wrong account.
b. a transaction could have been entered twice.
c. a transaction could have been omitted.
d. all of these.

12. Adjusting entries are necessary to
1. obtain a proper matching of revenue and expense.
2. achieve an accurate statement of assets and equities.
3. adjust assets and liabilities to their fair market value.

a. 1
b. 2
c. 3
d. 1 and 2

13. Why are certain costs of doing business capitalized when incurred and then depreciated or amortized over subsequent accounting cycles?
a. To reduce the federal income tax liability
b. To aid management in cash-flow analysis
c. To match the costs of production with revenues as earned
d. To adhere to the accounting constraint of conservatism

14. When an item of expense is paid and recorded in advance, it is normally called a(n)
a. prepaid expense.
b. accrued expense.
c. estimated expense.
d. cash expense.

15. When an item of revenue or expense has been earned or incurred but not yet collected or paid, it is normally called a(n) ____________ revenue or expense.
a. prepaid
b. adjusted

c. estimated
d. none of these

16. When an item of revenue is collected and recorded in advance, it is normally called a(n) ___________ revenue.
a. accrued
b. prepaid
c. unearned
d. cash

17. An accrued expense can best be described as an amount
a. paid and currently matched with earnings.
b. paid and not currently matched with earnings.
c. not paid and not currently matched with earnings.
d. not paid and currently matched with earnings.

18. If, during an accounting period, an expense item has been incurred and consumed but not yet paid for or recorded, then the end-of-period adjusting entry would involve
a. a liability account and an asset account.
b. an asset or contra-asset and an expense account.
c. a liability account and an expense account.
d. a receivable account and a revenue account.

19. Which of the following must be considered in estimating depreciation on an asset for an accounting period?
a. The original cost of the asset
b. Its useful life
c. The decline of its fair market value
d. Both the original cost of the asset and its useful life.

20. Which of the following would *not* be a correct form for an adjusting entry?
a. A debit to a revenue and a credit to a liability
b. A debit to an expense and a credit to a liability
c. A debit to a liability and a credit to a revenue
d. A debit to an asset and a credit to a liability

21. Year-end net assets would be overstated and current expenses would be understated as a result of failure to record which of the following adjusting entries?
a. Expiration of prepaid insurance
b. Depreciation of fixed assets
c. Accrued wages payable
d. All of these

22. A prepaid expense can best be described as an amount
a. paid and currently matched with revenues.
b. paid and not currently matched with revenues.
c. not paid and currently matched with revenues.
d. not paid and not currently matched with revenues.

23. An accrued revenue can best be described as an amount
a. collected and currently matched with expenses.
b. collected and not currently matched with expenses.
c. not collected and currently matched with expenses.
d. not collected and not currently matched with expenses.

24. An unearned revenue can best be described as an amount
a. collected and currently matched with expenses.
b. collected and not currently matched with expenses.
c. not collected and currently matched with expenses.
d. not collected and not currently matched with expenses.

25. Which of the following is a real (permanent) account?
a. Goodwill
b. Sales
c. Accounts Receivable
d. Both Goodwill and Accounts Receivable

26. Which of the following is a nominal (temporary) account?
a. Unearned Revenue
b. Salary Expense
c. Inventory
d. Retained Earnings

27. If the inventory account at the end of the year is understated, the effect will be to
a. overstate the gross profit on sales.
b. understate the net purchases.
c. overstate the cost of goods sold.
d. overstate the goods available for sale.

*28. Reversing entries are

1. normally prepared for prepaid, accrued, and estimated items.
2. necessary to achieve a proper matching of revenue and expense.
3. desirable to exercise consistency and establish standardized procedures.

a. 1
b. 2
c. 3
d. 1 and 2

*29. Adjusting entries that should be reversed include those for prepaid or unearned items that
a. create an asset or a liability account.
b. were originally entered in a revenue or expense account.
c. were originally entered in an asset or liability account.
d. create an asset or a liability account and were originally entered in a revenue or expense account.

*30. Adjusting entries that should be reversed include
a. all accrued revenues.
b. all accrued expenses.
c. those that debit an asset or credit a liability.
d. all of these.

Multiple Choice Answers—Conceptual

1.	d	6.	a	11.	d	16.	c	21.	d	26.	b
2.	d	*7.	d	12.	d	17.	d	22.	b	27.	c
3.	d	*8.	c	13.	c	18.	c	23.	c	*28.	c
4.	c	*9.	c	14.	a	19.	d	24.	b	*29.	d
5.	d	10.	d	15.	d	20.	d	25.	d	*30.	d

Solutions to those Multiple Choice questions for which the answer is “none of these.”
3. Many answers are possible.
5. journal.
15. accrued.

MULTIPLE CHOICE—Computational

31. Gomez Company received $7,200 on April 1, 2001 for one year's rent in advance and recorded the transaction with a credit to a nominal account. The December 31, 2001 adjusting entry is
a. debit Rent Revenue and credit Unearned Rent, $1,800.
b. debit Rent Revenue and credit Unearned Rent, $5,400.
c. debit Unearned Rent and credit Rent Revenue, $1,800.
d. debit Unearned Rent and credit Rent Revenue, $5,400.

32. Forbes Company paid $4,800 on June 1, 2001 for a two-year insurance policy and recorded the entire amount as Insurance Expense. The December 31, 2001 adjusting entry is
a. debit Insurance Expense and credit Prepaid Insurance, $1,400.
b. debit Insurance Expense and credit Prepaid Insurance, $3,400.
c. debit Prepaid Insurance and credit Insurance Expense, $1,400
d. debit Prepaid Insurance and credit Insurance Expense, $3,400.

33. Lane Company purchased equipment on November 1, 2001 and gave a 3-month, 9% note with a face value of $30,000. The December 31, 2001 adjusting entry is
a. debit Interest Expense and credit Interest Payable, $2,700.
b. debit Interest Expense and credit Interest Payable, $675.
c. debit Interest Expense and credit Cash, $450.
d. debit Interest Expense and credit Interest Payable, $450.

34. Green Company's account balances at December 31, 2001 for Accounts Receivable and the related Allowance for Doubtful Accounts are $460,000 debit and $700 credit, respectively. From an aging of accounts receivable, it is estimated that $15,000 of the December 31 receivables will be uncollectible. The necessary adjusting entry would include a credit to the allowance account for
a. $15,000.
b. $15,700.
c. $14,300.
d. $700.

35. Chen Company's account balances at December 31, 2001 for Accounts Receivable and the Allowance for Doubtful Accounts are $640,000 debit and $1,200 credit. Sales during 2001 were $1,500,000. It is estimated that 1% of sales will be uncollectible. The adjusting entry would include a credit to the allowance account for
a. $16,200.
b. $15,000.
c. $13,800.
d. $6,400.

36. Perez Corporation received cash of $6,000 on August 1, 2001 for one year's rent in advance and recorded the transaction with a credit to Rent Revenue. The December 31, 2001 adjusting entry is
a. debit Rent Revenue and credit Unearned Rent, $2,500.
b. debit Rent Revenue and credit Unearned Rent, $3,500.
c. debit Unearned Rent and credit Rent Revenue, $2,500.
d. debit Cash and credit Unearned Rent, $3,500.

*37. Lane Corporation has an incentive commission plan for its salesmen, entitling them to an additional sales commission when actual quarterly sales exceed budgeted estimates. An analysis of the account "incentive commission expense" for the year ended December 31, 2001, follows:

Amount	For Quarter Ended	Date Paid
$42,000	December 31, 2000	January 23, 2001
36,000	March 31, 2001	April 24, 2001
39,000	June 30, 2001	July 19, 2001
43,000	September 30, 2001	October 22, 2001

The incentive commission for the quarter ended December 31, 2001, was $35,000. This amount was recorded and paid in January 2002. What amount should Lane report as incentive commission expense for 2001?
a. $160,000.
b. $118,000.
c. $153,000.
d. $195,000.

Use the following information for questions 38 through 40:

The income statement of Carsen Corporation for 2001 included the following items:

Interest revenue	$75,500
Salaries expense	65,000
Insurance expense	9,600

The following balances have been excerpted from Carsen Corporation's balance sheets:

	December 31, 2001	December 31, 2000
Accrued interest receivable	$9,100	$7,500
Accrued salaries payable	8,900	4,200
Prepaid insurance	1,100	1,500

*38. The cash received for interest during 2001 was
a. $66,400.
b. $73,900.
c. $75,500.
d. $77,100.

*39. The cash paid for salaries during 2001 was
a. $69,700.
b. $60,300.
c. $60,800.
d. $73,900.

*40. The cash paid for insurance premiums during 2001 was
a. $8,500.
b. $8,100.
c. $10,000.
d. $9,200.

Use the following information for questions 41 through 43:

Poole Company paid or collected during 2001 the following items:

Insurance premiums paid	$ 12,400
Interest collected	25,900
Salaries paid	125,200

The following balances have been excerpted from Poole's balance sheets:

	December 31, 2001	December 31, 2000
Prepaid insurance	$ 1,200	$ 1,500
Interest receivable	3,700	2,900
Salaries payable	12,300	10,600

*41. The insurance expense on the income statement for 2001 was
a. $9,700.

b. $12,100.
c. $12,700.
d. $15,100.

*42. The interest revenue on the income statement for 2001 was
a. $19,300.
b. $25,100.
c. $26,700.
d. $32,500.

*43. The salary expense on the income statement for 2001 was
a. $102,300.
b. $123,500.
c. $126,900.
d. $148,100.

44. Rice Corporation loaned $45,000 to another corporation on December 1, 2001 and received a 3-month, 8% interest-bearing note with a face value of $45,000. What adjusting entry should Rice make on December 31, 2001?
a. Debit Interest Receivable and credit Interest Revenue, $900.
b. Debit Cash and credit Interest Revenue, $300.
c. Debit Interest Receivable and credit Interest Revenue, $300.
d. Debit Cash and credit Interest Receivable, $900.

*45. At the end of 2001, Drew Company made four adjusting entries for the following items:
1. Depreciation expense, $25,000.
2. Expired insurance, $2,200 (originally recorded as prepaid insurance).
3. Interest payable, $6,000.
4. Rental revenue receivable, $10,000.

In the normal situation, to facilitate subsequent entries, the adjusting entry or entries that may be reversed is (are)
a. Entry No. 3.
b. Entry No. 4.
c. Entries No. 3 and No. 4.
d. Entries No. 2, No. 3, and No. 4.

Use the following information for questions 46 and 47:

A company receives interest on a $30,000, 8%, 5-year note receivable each April 1. At December 31, 2000, the following adjusting entry was made to accrue interest receivable:

Interest Receivable	1,800	
Interest Revenue		1,800

46. Assuming that the company does *not* use reversing entries, what entry should be made on April 1, 2001 when the annual interest payment is received?

a.	Cash	600	
	Interest Revenue		600
b.	Cash	1,800	
	Interest Receivable		1,800
c.	Cash	2,400	
	Interest Receivable		1,800
	Interest Revenue		600
d.	Cash	2,400	
	Interest Revenue		2,400

*47. Assuming that the company *does* use reversing entries, what entry should be made on April 1, 2001 when the annual interest payment is received?

a.	Cash	600	
	Interest Revenue		600
b.	Cash	1,800	
	Interest Receivable		1,800
c.	Cash	2,400	
	Interest Receivable		1,800
	Interest Revenue		600
d.	Cash	2,400	
	Interest Revenue		2,400

*48. The following information is available concerning the accounts of Franz Company:

Accounts payable, January 1, 2001	$18,000
Cash payments on account during 2001	65,000
Purchase discounts taken during 2001 on 2001 purchases	1,200
Accounts payable, December 31, 2001	10,000

Assuming the company records purchases at the gross amounts, the total purchases for 2001 would be
a. $72,200.
b. $55,800.
c. $58,200.
d. $57,000.

*49. The following information is available for Carr Company:

Payment for goods during 2001	$62,000
Accounts payable, January 1, 2001	9,000
Inventory, January 1, 2001	10,400

Accounts payable, December 31, 2001	7,200
Inventory, December 31, 2001	9,700

Cost of goods sold for 2001 is
a. $59,500.
b. $60,900.
c. $67,100.
d. $68,500.

Multiple Choice Answers—Computational

31.	a	34.	c	*37.	c	*40.	d	*43.	c	46.	c	*49.	b
32.	d	35.	b	*38.	b	*41.	c	44.	c	47.	d		
33.	d	36.	b	*39.	b	*42.	c	45.	c	*48.	c		

MULTIPLE CHOICE—CPA Adapted

50. On September 1, 2000, Lett Co. issued a note payable to National Bank in the amount of $750,000, bearing interest at 12%, and payable in three equal annual principal payments of $250,000. On this date, the bank's prime rate was 11%. The first payment for interest and principal was made on September 1, 2001. At December 31, 2001, Lett should record accrued interest payable of
a. $30,000.
b. $27,500.
c. $20,000.
d. $18,333.

51. Denny Co. sells major household appliance service contracts for cash. The service contracts are for a one-year, two-year, or three-year period. Cash receipts from contracts are credited to Unearned Service Revenues. This account had a balance of $900,000 at December 31, 2001 before year-end adjustment. Service contract costs are charged as incurred to the Service Contract Expense account, which had a balance of $225,000 at December 31, 2001.

Service contracts still outstanding at December 31, 2001 expire as follows:

During 2002	$190,000
During 2003	285,000
During 2004	125,000

What amount should be reported as Unearned Service Revenues in Denny's December 31, 2001 balance sheet?
a. $675,000.
b. $600,000.
c. $375,000.
d. $300,000.

52. In November and December 2001, Lowe Co., a newly organized magazine publisher, received $60,000 for 1,000 three-year subscriptions at $20 per year, starting with the January 2002 issue. Lowe included the entire $60,000 in its 2001 income tax return. What amount should Lowe report in its 2001 income statement for subscriptions revenue?
a. $0.
b. $3,333.
c. $20,000.
d. $60,000.

53. On June 1, 2001, Mays Corp. loaned Farr $500,000 on a 12% note, payable in five annual installments of $100,000 beginning January 2, 2002. In connection with this loan, Farr was required to deposit $6,000 in a noninterest-bearing escrow account. The amount held in escrow is to be returned to Farr after all principal and interest payments have been made. Interest on the note is payable on the first day of each month beginning July 1, 2001. Farr made timely payments through November 1, 2001. On January 2, 2002, Mays received payment of the first principal installment plus all interest due. At December 31, 2001, Mays' interest receivable on the loan to Farr should be
a. $0.
b. $5,000.
c. $10,000.
d. $15,000.

54. Baker Corp.'s liability account balances at June 30, 2002 included a 10% note payable in the amount of $1,500,000. The note is dated October 1, 2000 and is payable in three equal annual payments of $500,000 plus interest. The first interest and principal payment was made on October 1, 2001. In Baker's June 30, 2002 balance sheet, what amount should be reported as accrued interest payable for this note?
a. $112,500.
b. $75,000.
c. $37,500.

d. $25,000.

55. Cole Co. pays all salaried employees on a biweekly basis. Overtime pay, however, is paid in the next biweekly period. Cole accrues salaries expense only at its December 31 year end. Data relating to salaries earned in December 2001 are as follows:

Last payroll was paid on 12/26/01, for the 2-week period ended 12/26/01.
Overtime pay earned in the 2-week period ended 12/26/01 was $5,000.
Remaining work days in 2001 were December 29, 30, 31, on which days there was no overtime.
The recurring biweekly salaries total $80,000.

Assuming a five-day work week, Cole should record a liability at December 31, 2001 for accrued salaries of
a. $24,000.
b. $29,000.
c. $48,000.
d. $53,000.

56. Yung Corp.'s trademark was licensed to Dent Co. for royalties of 15% of sales of the trademarked items. Royalties are payable semiannually on March 15 for sales in July through December of the prior year, and on September 15 for sales in January through June of the same year. Yung received the following royalties from Dent:

	March 15	September 15
2000	$5,000	$7,500
2001	6,000	8,500

Dent estimated that sales of the trademarked items would total $60,000 for July through December 2001. In Yung's 2001 income statement, the royalty revenue should be
a. $17,500.
b. $19,000.
c. $23,500.
d. $25,000.

57. At December 31, 2001, Ann's Boutique had 1,000 gift certificates outstanding, which had been sold to customers during 2001 for $50 each. Ann's operates on a gross margin of 60% of its sales. What amount of revenue pertaining to the 1,000 outstanding gift certificates should be deferred at December 31, 2001?
a. $0.
b. $20,000.
c. $30,000.
d. $50,000.

*58. Compared to the accrual basis of accounting, the cash basis of accounting overstates income by the net increase during the accounting period of the

	Accounts Receivable	Accrued Expenses Payable
a.	No	No
b.	No	Yes
c.	Yes	No
d.	Yes	Yes

*59. Hall Corp. reported revenue of $1,100,000 in its accrual basis income statement for the year ended June 30, 2001. Additional information was as follows:

Accounts receivable June 30, 2000	$250,000
Accounts receivable June 30, 2001	530,000
Uncollectible accounts written off during the fiscal year	13,000

Under the cash basis, Hall should report revenue of
a. $587,000.
b. $600,000.
c. $807,000.
d. $833,000.

*60. Jim Vance, M.D., keeps his accounting records on the cash basis. During 2001, Dr. Vance collected $150,000 from his patients. At December 31, 2000, Dr. Vance had accounts receivable of $25,000. At December 31, 2001, Dr. Vance had accounts receivable of $35,000 and unearned revenue of $5,000. On the accrual basis, how much was Dr. Vance's patient service revenue for 2001?
a. $125,000.
b. $155,000.
c. $160,000.
d. $165,000.

Multiple Choice Answers—CPA Adapted

50. c	52. a	54. b	56. a	*58. b	*60. b
51. b	53. c	55. b	57. d	*59. c	

PROBLEM 1
(Worksheet preparation)

The following accounts and balances have been taken from the trial balance of Marlin Inc.at the company's year-end, March 31, 19X3 before the adjusting entries have been made:

Cash	$ 12,600
Accounts Receivable	2,500
Prepaid Insurance	840
Prepaid Rent	1,400
Supplies	650
Equipment	4,500
Truck	10,800
Accounts Payable	3,440
Loans Payable	4,500
Unearned Revenue	800
Common Stock	10,000
Retained Earnings	1,200
Service Fees Revenue	16,500
Advertising Expense	600
Interest Expense	200
Miscellaneous Expense	550
Salaries Expense	1,800

An analysis of Marlin Inc. records discloses the following information:

a. The prepaid insurance is for a 2-year policy from April 1, 19X2.

b. There were $180-worth of supplies on hand on March 31, 19X3.

c. During the year Marlin completed work worth $600, for which payment had been recorded as unearned revenue.

d. On April 1, 19X2 the company paid one year's rent in advance.

e. The truck was purchased on May 1, 19X2 with a 3-year life and no salvage value. It is company policy to depreciate all assets in the month of use if it is used before the 15th of the month.

f. The equipment was purchased on April 6, 19X2 and was put into operation on April 21, 19X2. It has an estimated life of 5 years and no salvage value.

g. The company collected $850 from customers for work to be completed in July 19X3. The bookkeeper incorrectly credited this payment to Rental Revenue.

Required:
1. Set up a worksheet and enter the given information from the unadjusted March 31, 19X3 trial balance.

2. Enter all the adjustments on the worksheet.

3. Complete the worksheet; extend the adjusted trial balance to the income statement and the balance sheet columns.

PROBLEM 2 (Financial statement preparation from the worksheet)

Charter Investments Inc. has just prepared its trial balance for the year ended December 19X2.

Charter Investments Inc.
TRIAL BALANCE
December 31, 19X2

Account Title	Debit	Credit
Cash	$ 3,600	
Accounts Receivable	2,200	
Supplies	860	
Land	32,000	
Rental Buildings	150,000	
Furniture	12,500	
Office Equipment	7,000	
Accumulated Depreciation-Rental Buildings		$ 31,000
Accumulated Depreciation-Furniture		1,875
Accumulated Depreciation-Office Equipment		1,760
Accounts Payable		4,870
Mortgage Payable		100,000
Common Stock		50,000
Retained Earnings		11,500
Rental Revenue		58,790
Advertising Expense	1,300	
Depreciation Expense-Rental Buildings	11,000	
Depreciation Expense-Furniture	1,375	
Depreciation Expense-Office Equipment	1,210	
Insurance Expense	3,600	
Interest Expense	10,500	
Rent Expense	6,600	
Supplies Used	6,200	
Utilities Expense	1,400	
Wages Expense	8,450	
Totals	$ 259,795	$ 259,795

Supplementary information concerning the adjustments to be made are as follows:

a. A $3,600 insurance premium was paid on March 1, 19X2 for 2-year comprehensive coverage on the rental properties. The entire premium was debited to Insurance Expense.

b. The depreciation expense is $1,235 ($110 for office equipment, $125 for furniture, and $1,000 for the rental buildings).

c. December's rent of $600 has not been paid.

d. An inventory count of supplies on hand at the end of December was taken; $250-worth of supplies were found to be still on hand.

e. Monthly adjusting entries were prepared to the end of November.

Required:

1. Set up a worksheet and enter the given information from the trial balance.
2. Enter all adjustments on the worksheet.
3. Complete the worksheet as shown in the text.

PROBLEM 3 (Worksheet, financial statement preparations, closing entries, and reversing entries)

The following accounts and balances have been taken from the general ledger trial balance of Wangor Repairs Inc. as at September 30, 19X2 after its first year of operation but before any adjusting entries have been made for the year.

Accounts Payable	$ 3,950	
Accounts Receivable	4,200	
Advertising Expense	1,650	
Cash	1,850	
Common Stock	12,000	
Equipment	9,500	
Furniture and Fixtures	3,500	
Insurance Expense	960	
Miscellaneous Expense	1,700	
Notes Receivable	4,000	
Office Supplies Used		600
Rent Expense	3,380	
Repair Revenue	34,690	
Repair Supplies Used	1,170	
Salaries Expense	5,450	
Truck	12,000	
Utilities Expense	680	

Additional information:

a.

Asset	Estimated Useful Life	Salvage Value
Furniture and Fixtures	5 years	$ 440
Equipment	10 years	1,500
Truck	3 years	1,500

All assets were purchased on October 1, 19x1

b. The company paid a $600 advertising bill in August for television and radio ads to begin in November 19X2.

c. Wangor Repairs Inc. was required to pay the last month's rent at the time of signing a 5-year lease.

d. A physical inventory taken September 30 showed that office supplies on hand totalled $120 and repair supplies on hand were $360.

e. The insurance premium of $960 paid in October 19X1 was for a 2-year policy.

f. The company billed and included in revenue $700 for work to be completed in November 19X2.

Required:
1. Prepare a worksheet to reflect the appropriate adjustments
2. Prepare all three financial statements.
3. Prepare the necessary closing entries in general journal form.
4. Prepare a post-closing trial balance.
5. Prepare the reversing entries required at the beginning of the next accounting period.

PROBLEM 4-4 (Preparation of closing entries)

An alphabetical listing of the account balance of Toker Management Services after its second complete year of operations is shown below. All necessary adjustments as of December 31 have been recorded and posted.

Accounts Payable	$ 2,501	Miscellaneous Expense	$ 450
Accounts Receivable	6,582	Prepaid Insurance	1,770
Advertising Expense	2,000	Rent Expense	3,850
Cash	4,375	Salaries Expense	23,235
Common Stock	10,000	Supplies	1,470
Insurance Expense	3,000	Supplies Used	1,969
Management Fees Earned	38,800	Utilities Expense	2,600

Required:

Prepare all necessary general journal entries to close the books at December 31. Explanation lines may be omitted.

SOLUTIONS

Key Concept Comprehension

1. financial statement
2. income statement
3. permanent
4. mixed income statement accounts
5. worksheet
6. balance sheet accounts
7. Closing entries / temporary accounts
8. post-closing trial balance
9. Revenue / expense / Income Summary

True or False Questions

1. T
2. F The adjusting entries may be entered in the general journal and posted to the general ledger; an adjusted trial balance would then provide the data for the preparation of the financial statements.
3. F The post-closing trial balance contains only permanent accounts.
4. F The temporary accounts are closed to the Retained Earnings.
5. T
6. F The closing entries must be prepared at the end of the fiscal year regardless of whether a worksheet was used or not.
7. T
8. F The worksheet allows for the preparation of the financial statements before the entries and postings are done; however, the formal accounting process must still be completed.
9. T

SOLUTION TO PROBLEM 1

Marlin Inc.
WORKSHEET
For the Year Ended March 31,19X3

	Trial Balance		Adjustments				Adjusted Trial Balance		Income Statement		Retained Earnings		Balance Sheet	
Account Title	Dr	CR		Dr		CR	Dr	CR	Dr	CR	Dr	CR	Dr	CR
Cash	12,600						12,600	0					12,600	
Accounts Receivable	2,500						2,500	0					2,500	
Prepaid Insurance	840				a	(420)	420	0					420	
Prepaid Rent	1,400				d	(1,400)	0	0					0	
Supplies	650				b	(470)	180	0					180	
Equipment	4,500						4,500	0					4,500	
Truck	10,800						10,800	0					10,800	
Accounts Payable		(3,440)					0	(3,440)						(3,440)
Unearned Revenue		(800)	c	600	g	(850)	0	(1,050)						(1,050)
							0	0						0
Loans Payable		(4,500)					0	(4,500)						(4,500)
							0	0						0
Common Stock		(10,000)					0	(10,000)						(10,000)
Ret Earnings (BOY)		(1,200)					0	(1,200)				(1,200)		
							0	0						
Service Fees Rev		(16,500)	g	850	c	(600)	0	(16,250)		(16,250)				
Advertising Exp	600						600	0	600					
Interest Exp	200						200	0	200					
Misc. Exp	550						550	0	550					
Salaries Exp	1,800						1,800	0	1,800					
Balance	36,440	(36,440)												
Insurance Exp			a	420			420	0	420	0				
Supplies Exp			b	470			470	0	470	0				
Rent Exp			d	1,400			1,400	0	1,400	0				
Depreciation Exp-Truck			e	3,300			3,300	0	3,300	0				
Depreciation Exp-Equp			f	825			825	0	825	0				
Accum Deprec. Truck					e	(3,300)	0	(3,300)					0	(3,300)
Accum Deprec. Equip					f	(825)	0	(825)					0	(825)
Balance				7,865		(7,865)	40,565	(40,565)	9,565	(16,250)		(1,200)	31,000	(23,115)
Net Income									6,685			(6,685)		
									16,250	(16,250)	7,885			(7,885)
Ret Earnings (EOY)											7,885	(7,885)	31,000	(31,000)

Calculation of adjustments:

a. **Insurance Expense**: $840/2 years = $420 per year

b. **Supplies Used**: Purchases - Inventory = Amount Used = $650 - $180 = $470

e. **Depreciation Expense-Truck**: $10,800 cost/36 months (expected life) = $300/month x 11 months (period of use) = $3,300

f. **Depreciation Expense-Equipment**: $4,500 cost/60 months (expected life) = $75/month x 11 months (period of use) = $825

SOLUTION TO PROBLEM 2

Charter Investments Inc.
WORKSHEET
For the Year Ended December 31,19X2

	Trial Balance			Adjustments			Adjusted Trial Balance		Income Statement		Retained Earnings		Balance Sheet	
Account Title	Dr	CR		Dr		CR	Dr	CR	Dr	CR	Dr	CR	Dr	CR
Cash	3,600						3,600	0					3,600	0
Accounts Receivable	2,200						2,200	0					2,200	0
Supplies	860				d	(610)	250	0					250	0
Land	32,000						32,000	0					32,000	0
Rental Building	150,000						150,000	0					150,000	0
Furniture	12,500						12,500	0					12,500	0
Office Equipment	7,000						7,000	0					7,000	0
A/D Rental Bulding		(31,000)			b	(1,000)	0	(32,000)					0	(32,000)
A/D Furniture		(1,875)			b	(125)	0	(2,000)					0	(2,000)
A/D Office Equip		(1,760)			b	(110)	0	(1,870)					0	(1,870)
Accounts Payable		(4,870)					0	(4,870)						(4,870)
							0	0						0
							0	0						0
Mortgage Payable		(100,000)					0	(100,000)						(100,000)
Common Stock		(50,000)					0	(50,000)						(50,000)
Retained Earnings (BOY)		(11,500)					0	(11,500)				(11,500)		
							0	0						
Rental Revenue		(58,790)					0	(58,790)		(58,790)				
Advt Exp	1,300						1,300	0	1,300					
Depr. Exp. Rental Building	11,000		b	1,000			12,000	0	12,000					
Depr. Exp. Furniture	1,375		b	125			1,500	0	1,500					
Depr. Exp. Office Equip	1,210		b	110			1,320	0	1,320					
Insurance Exp	3,600				a	(2,100)	1,500	0	1,500					
Interest Exp	10,500						10,500	0	10,500					
Rent Expense	6,600		c	600			7,200		7,200					
Utilities Exp	6,200		d	610			6,810		6,810					
Wages Exp	1,400						1,400		1,400					
	8,450						8,450		8,450					
	259,795	(259,795)												
Prepaid Insurance			a	2,100			2,100	0					2,100	0
Rent payable					c	(600)	0	(600)					0	(600)
Balance				4,545		(4,545)	261,630	(261,630)	51,980	(58,790)		(11,500)	209,650	(191,340)
Net Income									6,810			(6,810)		
									58,790	(58,790)	18,310			(18,310)
Ret Earnings (EOY)											18,310	(18,310)	209,650	(209,650)

Calculation of adjustments:

a. **Unexpired Insurance**: \$3,600 policy cost/24 months (term of the policy) = \$150/month x 14 months = \$2,100

d. **Supplies:** Beginning Balance \$860 less Ending Balance \$250 = Supplies used \$610

SOLUTION TO PROBLEM 3 **(4-3 Requirement 1: Preparation of Work Sheet)**

Wangor Repairs Inc.
WORKSHEET
For the Year Ended September 30, 19X2

Account Title	Trial Balance Dr	Trial Balance CR		Adjustments Dr		Adjustments CR	Adjusted Trial Balance Dr	Adjusted Trial Balance CR	Income Statement Dr	Income Statement CR	Retained Earnings Dr	Retained Earnings CR	Balance Sheet Dr	Balance Sheet CR
Cash	1,850						1,850	0					1,850	0
Accounts Rec	4,200						4,200	0					4,200	0
Notes Rec	4,000						4,000	0					4,000	0
Furniture and Fixtures	3,500						3,500	0					3,500	0
Equipment	9,500						9,500	0					9,500	0
Truck	12,000						12,000	0					12,000	0
Accounts Payble		(3,950)					0	(3,950)						(3,950)
Common Stock		(12,000)					0	(12,000)						(12,000)
Retained Earnings (BOY)							0	0				0		
							0	0						
Repair Revenue		(34,690)	f	700			0	(33,990)		(33,990)				
							0	0		0				
Advertising Expense	1,650				b	(600)	1,050	0	1,050					
Insurance Expense	960				e	(480)	480	0	480					
Misc. Exp	1,700						1,700	0	1,700					
Office Supplies Used	600				d	(120)	480	0	480					
Rent Exp	3,380				c	(260)	3,120	0	3,120					
Repair Supplies Exp	1,170				d	(360)	810	0	810					
Salaries Exp	5,450						5,450		5,450					
Utilities Exp	680						680		680					
	50,640	(50,640)												
Depr Exp.--Furn/Fixture			a	612			612	0	612	0				
Depr Exp-Equip			a	800			800	0	800	0				
Depr Exp-Truck			a	3,500			3,500	0	3,500	0				
Accum Depr-Furn/Fixture					a	(612)	0	(612)					0	(612)
Accum Depr-Equip					a	(800)	0	(800)					0	(800)
Accum Depr-Truck					a	(3,500)	0	(3,500)					0	(3,500)
Prepaid Advt			b	600			600	0					600	0
Prepaid Insurance			e	480			480	0					480	0
Prepaid Rent			c	260			260	0					260	0
Unearned Refenue					f	(700)	0	(700)					0	(700)
Office Supplies			d	120			120	0					120	0
Repair Supplies			d	360			360	0					360	0
Balance				7,432		(7,432)	55,552	(55,552)	18,682	(33,990)		0	36,870	(21,562)
Net Income									15,308			(15,308)		
									33,990	(33,990)	15,308			(15,308)
Ret Earnings (EOY)											15,308	(15,308)	36,870	(36,870)

Calculation of Adjustments:

a. **Depreciation Expense-Furniture & Fixtures:** \$3,500 cost - \$440 salvage value =\$3,060/5 years (expected life) = \$612/year
Depreciation Expense-Equipment: \$9,500 cost - \$1,500 salvage value =\$8,000/10 years (expected life) = \$800/year
Depreciation Expense-Truck: \$12,000 cost - \$1,500 salvage value = \$10,500/3 years (expected life) = \$3,500/year - used for the entire year

c. **Rent Expense:** \$3,380 shown in the expense account/13 months paid = \$260/month x 12 months = \$3,120

e. **Insurance Expense:** \$960 policy cost/2 years (term of the policy) = \$480/year

(4-3 Requirement 2: Preparation of Financial Statements)

Wangor Repairs Inc.
INCOME STATEMENT
For the Year Ended September 30, 19X2

REPAIR REVENUE		\$ 33,990
EXPENSES		
Advertising Expense	\$ 1,050	
Depreciation Expense-Furniture & Fixtures	612	
Depreciation Expense-Equipment	800	
Depreciation Expense-Truck	3,500	
Insurance Expense	480	
Miscellaneous Expense	1,700	
Office Supplies Used	480	

Note also how the nominal accounts are all in the income statement and the real accounts flow to the balance sheet and retained earnings statement.

Rent Expense	3,120	
Repair Supplies Used	810	
Salaries Expense	5,450	
Utilities Expense	680	
Total Expenses		18,682
Net Income *		$ 15,308

* Carry net inc. figure to the statement of retained earnings

(Problem 3 Requirement 2: Preparation of Financial Statements continued)

Wangor Repairs Inc.
STATEMENT OF RETAINED EARNINGS
For the Year Ended September 30, 19X2

Balance (Oct. 1, 19X1)	-0-
Add: Net Income for the year	$ 15,308
Balance (Sep. 30, 19X2) **	$ 15,308

** Carry Retained Earnings balance September 30 to the balance sheet

Wangor Repairs Inc.
BALANCE SHEET
At September 30, 19X2

Assets			
Cash			$ 1,850
Accounts Receivable			4,200
Notes Receivable			4,000
Prepaid Advertising			600
Prepaid Insurance			480
Prepaid Rent			260
Office Supplies			120
Repair Supplies			360
Furniture and Fixtures	$ 3,500		
Less: Accumulated Depreciation	612		2,888
Equipment	$ 9,500		
Less: Accumulated Depreciation	800	8,700	
Truck	$ 12,000		
Less: Accumulated Depreciation	3,500		8,500
Total Assets			$ 31,958
Liabilities and Shareholders' Equity			
Accounts Payable			$ 3,950
Unearned Revenue			700
Total Liabilities			$ 4,650
Common Stock	$ 12,000		
Retained Earnings	15,308		
Total Shareholders' Equity			27,308
Total Liabilities and Shareholders' Equity			$ 31,958

(Problem 3 Requirement 3: Preparation of Closing entries in general journal format)

GENERAL JOURNAL

Date	Description		
Sep. 30	Repair Revenue	33,990	
	Income Summary		33,990
	To close revenue account balance.		
Sep. 30	Income Summary	18,682	
	Advertising Expense		1,050
	Depreciation Expense-Furniture and Fixtures		612
	Depreciation Expense-Equipment		800
	Depreciation Expense-Truck		3,500
	Insurance Expense		480
	Miscellaneous Expense Office		1,700
	Supplies Used		480
	Rent Expense		3,120
	Repair Supplies Used		810
	Salaries Expense		5,450
	Utilities Expense		680
	To close expense account balances.		
Sep 30.	Income Summary	15,308	
	Retained Earnings		15,308
	To close Income Summary account.		

Note that these are **closing entries, which means we are closing the accounts to the expense and revenue summary;**

(Problem 3 Requirement 4: Preparation of the post-closing trial balance).

Wangor Repairs Inc.
POST-CLOSING TRIAL BALANCE
September 30, 19X2

Account Title	Debit	Credit
Cash	$ 1,850	
Accounts Receivable	4,200	
Notes Receivable	4,000	
Prepaid Advertising	600	
Prepaid Insurance	480	
Prepaid Rent	260	
Office Supplies	120	
Repair Supplies	360	
Furniture and Fixtures	3,500	
Equipment	9,500	
Truck	12,000	
Accum. Depreciation-Furniture and Fixtures		$ 612
Accum. Depreciation-Equipment		800
Accum. Depreciation-Truck		3,500
Accounts Payable		3,950
Unearned Revenue		700
Common Stock		12,000
Retained Earnings		15,308
Totals	$ 36,870	$ 36,870

(Problem 3 Requirement 5: Preparation of reversing entries)

GENERAL JOURNAL

Journal No.	Description	Debit	Credit
a.	Advertising Expense	600	
	Prepaid Advertising		600
d.	Office Supplies Used	120	
	Repair Supplies Used	360	
	Office Supplies		120
	Repair Supplies		360
e.	Insurance Expense	480	
	Prepaid Insurance		480
f.	Unearned Revenue	700	
	Repair Revenue		700

SOLUTION TO PROBLEM 4

GENERAL JOURNAL

Date	Description	Debit	Credit
Dec. 31	Management Fees Earned	38,800	
	Income Summary		38,000
Dec. 31	Income Summary	37,104	
	Advertising Expense		2,000
	Insurance Expense		3,000
	Miscellaneous Expense		450
	Rent Expense	3,850	
	Salaries Expense		23,235
	Supplies Used		1,969
	Utilities Expense		2,600
Dec. 31	Income Summary	1,696	
	Retained Earnings		1,696