

SOLUTIONS

Learning Goal 16

Multiple Choice

1. d
2. a
3. b
4. d Because drawing is closed directly into the capital account, not into income summary.
5. c
6. b This a permanent account—specifically, a contra asset.
7. a
8. a
9. a
10. c
11. d

Discussion Questions and Brief Exercises

1. Closing entries accomplish three specific objectives:
 - Transfer net income or net loss of the current period into the capital account
 - Transfer the current period balance of the drawing account into the capital account
 - Create zero balances in the temporary accounts at the end of the current period
2. Closing entries are prepared at the end of an accounting period. They are the very last entries of an accounting period. This is to be sure that all other transactions and adjustments have been completed so that the accounts are up to date and correct as of the end of the period.
3. The six types of owner's equity accounts are:
 - Capital
 - Revenue
 - Expense
 - Drawing
 - Gains
 - Losses

In this learning goal we studied the first four accounts. However, gains have the same effect on the capital account as revenues and are closed in the same manner. Expenses have the same effect on the capital account as expenses and are closed in the same manner.

4. A temporary account is an owner's equity account and is closed at the end of an accounting period. The temporary accounts that we studied are revenue, expense, and drawing accounts. (The other two temporary accounts are gain and loss accounts.) These accounts are sometimes referred to as *income statement accounts*. Permanent accounts are accounts that are never closed: asset, liability, and owner's capital accounts, which are sometimes referred to as *balance sheet accounts*.
5. Adjusting entries apply the revenue and recognition and matching principles to ensure that all revenues and expenses are properly recorded in each accounting period. Adjusting entries are also used for valuation purposes to change recorded account values under certain circumstances. Closing entries close temporary accounts into the owner's capital account.
6. The format of the correct closing entry is:

Income Summary	55,400	
XXX, Capital		55,400

This represents net income because the income summary account has a credit balance.

7. The post-closing trial balance verifies that the ledger remains in balance (total debits equal total credits) after the closing entries have been posted.

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8. Service revenue and depreciation expense are temporary accounts and would not appear in a post-closing trial balance.
9. The debit and credit totals of a worksheet income statement column should be the same amounts posted as debit and credit entries to the income summary account. The total of the debit column is the total of all temporary items that reduce net income. The total of the credit column is the total of all temporary items that increase net income.
10. (1) Close revenue accounts into the income summary account (debit each revenue, credit income summary for the total).
(2) Close expense accounts into the income summary account (debit income summary for the total, credit each expense account).
(3) Close the balance of income summary into the capital account.
(4) Close the drawing account into the capital account (debit capital, credit drawing).
11. The drawing account is not an expense. Therefore, it does not belong in income summary because it is not an item that affects net income. Rather, the drawing account shows reductions in the capital account because of assets that are removed from the business by the owner for personal use. Therefore, the drawing account is closed directly into the capital account.

Reinforcement Problems

LG 16-1.

Account Name	Permanent	Temporary	Closed	Appears on the:	
				Balance Sheet	Income Statement
Cash	✓			✓	
Unearned Revenue	✓			✓	
Accumulated Depreciation	✓			✓	
Fees Earned		✓	✓		✓
Insurance Expense		✓	✓		✓
Prepaid Insurance	✓			✓	
Income Summary		✓	✓	—	—
Supplies	✓			✓	
Supplies Expense		✓	✓		✓
Owner's Capital	✓			✓	
Rent Expense		✓	✓		✓
Depreciation Expense		✓	✓		✓
Interest Revenue		✓	✓		✓
Accounts Payable	✓			✓	
Office Equipment	✓			✓	
Drawing		✓	✓	—	—

Note: Notice that only temporary (income statement accounts and withdrawals) are closed. Permanent (balance sheet) accounts are not closed.

SOLUTIONS**Learning Goal 16, continued****LG 16-2.**

a.

Tallahassee Company										
Worksheet										
For the Year Ended June 30, 2008										
Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Balance Sheet	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	200				200				200	
Accounts Receivable	30		(e) 8		38				38	
Office Supplies	15			(a) 3	12				12	
Prepaid Insurance	20			(b) 10	10				10	
Office Equipment	100				100				100	
Accum. Dep'n.—										
Office Equipment		20		(c) 2		22				22
Marla Greenberg, Capital		332				332				332
Marla Greenberg, Drawing	10				10				10	
Fees Earned		40		(e) 8		48		48		
Salaries Expense	5		(d) 5		10		10			
Rent Expense	12				12		12			
Totals	<u>392</u>	<u>392</u>								
Office Supplies Expense			(a) 3		3		3			
Depreciation Expense			(c) 2		2		2			
Insurance Expense			(b) 10		10		10			
Salaries Payable				(d) 5		5				5
Totals			<u>28</u>	<u>28</u>	<u>407</u>	<u>407</u>	37	48	370	359
Net Income							11			11
Totals							<u>48</u>	<u>48</u>	<u>370</u>	<u>370</u>

Note: The income statement numbers are just extensions from the adjusted trial balance, except for the totals.

SOLUTIONS

Learning Goal 16, continued

LG 16-2, *continued*

b.

GENERAL JOURNAL

J43

Date	Account Titles and Explanation	Post. Ref.	Debit	Credit
June	<i>Closing Entries</i>			
30	Fees Earned		48	
	Income Summary			48
	To close revenue into income summary			
30	Income Summary		37	
	Salaries Expense			10
	Rent Expense			12
	Office Supplies Expense			3
	Depreciation Expense			2
	Insurance Expense			10
	To close expenses into income summary			
30	Income Summary		11	
	Marla Greenberg, Capital			11
	To close income summary into owner's capital			
30	Marla Greenberg, Capital		10	
	Marla Greenberg, Drawing			10
	To close the drawing account into owner's capital			

SOLUTIONS

Learning Goal 16, continued

LG 16-2, *continued*

c and d.

Cash	Accounts Receivable	Office Supplies	Prepaid Insurance	Office Equipment
bal. 200	bal. 30 (e) <u>8</u> 38	bal. <u>15</u> (a) 3 12	bal. <u>20</u> (b) 10 10	bal. 100
Accum. Dep'n Office Equip.	Salaries Payable	Marla Greenberg, Capital	Marla Greenberg, Drawing	Fees Earned
bal. 20 (c) <u>2</u> 22	(d) 5	bal. 332 11 <u>10</u> 333	bal. 10 10 <u>-0-</u>	bal. 40 (e) <u>8</u> 48 <u>48</u> -0-
Salaries Expense	Rent Expense	Office Supplies Expense	Depreciation Expense	Insurance Expense
bal. 5 (d) <u>5</u> 10 <u>10</u> -0-	bal. 12 12 <u>-0-</u>	(a) 3 3 <u>-0-</u>	(c) 2 2 <u>-0-</u>	(b) 10 10 <u>-0-</u>
Income and Expense Summary				
<u>48</u> 37 11 <u>-0-</u>				

Note: Revenue closing entries are shown in **bold** and expense closing entries are shown in *italics*.

SOLUTIONS

Learning Goal 16, continued

LG 16-3.

Note: Part of the skill required here is to be able to distinguish between permanent and temporary accounts, because permanent accounts are never closed.

a.

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J59

Date	Account Titles and Explanation	Post. Ref.	Debit	Credit
2008	<i>Closing Entries</i>			
June	Tennis Instruction Fees		8,500	
30	Dues Revenue		28,500	
	Interest Earned		80	
	Income Summary			37,080
	To close revenue into income summary			
30	Income Summary		12,134	
	Salaries Expense			4,100
	Equipment Rent Expense			1,750
	Utilities Expense			280
	Insurance Expense			200
	Maintenance Expense			750
	Office Supplies Expense			1,050
	Tennis Supplies Expense			1,787
	Depreciation Expense			842
	Interest Expense			1,375
	To close expenses into income summary			
30	Income Summary		24,946	
	J.W. Winslow, Capital			24,946
	To close income summary into owner's capital			
30	J.W. Winslow, Capital		1,880	
	J.W. Winslow, Drawing			1,880
	To close the drawing account into owner's capital			

SOLUTIONS**Learning Goal 16, continued****LG 16-3, continued**

b.

Winslow Tennis Club Post-Closing Trial Balance June 30, 2008		
Account	Dr.	Cr.
Cash	\$45,750	
Dues Receivable	2,800	
Office Supplies	50	
Tennis Supplies	215	
Notes Receivable	12,000	
Prepaid Insurance	500	
Office Equipment	14,520	
Accum. Dep'n—Office Equipment		\$11,858
Building	345,000	
Accum. Dep'n—Building		20,100
Accounts Payable		855
Notes Payable		275,000
J. Winslow, Capital		110,227
Unearned Tennis Fees		1,000
Salaries and Wages Payable		500
Interest Receivable	80	
Interest Payable		1,375
Totals	<u><u>\$420,915</u></u>	<u><u>\$420,915</u></u>

- c. The net income of \$24,946 and the drawing of \$1,880 have been closed into the owner's capital account resulting in the ending balance of \$110,227 as follows: $\$87,161 + \$24,946 - \$1,880 = \$110,227$.

SOLUTIONS

Learning Goal 16, continued

LG 16-4, continued

Date	Account	Post. Ref.	Dr.	Cr.
2008	<i>Closing Entries</i>			
Dec. 31	Service Revenue		248,100	
	Rental Revenue		20,000	
	Interest Revenue		450	
	Income and Expense Summary			268,550
31	Income and Expense Summary		199,100	
	Depreciation Expense—Office Equipment			2,500
	Advertising Expense			22,400
	Travel Expense			4,500
	Utilities Expense			5,700
	Miscellaneous Expense			300
	Interest Expense			7,500
	Rent Expense			26,000
	Wages Expense			115,300
	Insurance Expense			9,900
	Depreciation Expense—Automotive			5,000
31	Income and Expense Summary		69,450	
	Income and Expense Summary			69,450
31	Debbie Vo, Capital		35,000	
	Debbie Vo, Drawing			35,000

Comments: Any prepaid expense is an asset; therefore, Prepaid Insurance Expense and Prepaid Rent Expense are assets (permanent accounts) and are not closed. Unearned revenue is always a liability and therefore also a permanent account and never closed.

SOLUTIONS

Learning Goal 16, continued

LG 16-4.

b.

Service Revenue		Rental Revenue		Interest Revenue		Dep'n Expense Office Equipment		Advertising Expense	
	248,100		20,000		450	2,500		22,400	
248,100		20,000		450			<i>2,500</i>		<i>22,400</i>
	-0-		-0-		-0-	-0-		-0-	

Travel Expense		Utilities Expense		Miscellaneous Expense		Interest Expense		Rent Expense	
4,500		5,700		300		7,500		26,000	
	<i>4,500</i>		<i>5,700</i>		<i>300</i>		<i>7,500</i>		<i>26,000</i>
-0-		-0-		-0-		-0-		-0-	

Wages Expense		Insurance Expense		Dep'n Expense—Automotive Equipment		Debbie Vo, Drawing		Debbie Vo, Capital	
115,300		9,900		5,000		35,000			170,300
	<i>115,300</i>		<i>9,900</i>		<i>5,000</i>		<i>35,000</i>	<i>35,000</i>	<i>69,450</i>
-0-		-0-		-0-		-0-			204,750

Income and Expense Summary	
	268,550
199,100	
69,450	

Note: Revenue closing entries are shown in **bold** and expense closing entries are shown in *italics*.

SOLUTIONS

Learning Goal 16, continued

LG 16-5.

a.

Date	Account	Post. Ref.	Dr.	Cr.
20XX	<i>Closing Entries</i>			
Aug. 31	Service Revenue		64,900	
	Income and Expense Summary			64,900
31	Income and Expense Summary		43,000	
	Wages Expense			8,000
	Rent Expense			3,700
	Office Supplies Expense			600
	Depreciation Expense			25,000
	Advertising Expense			5,700
31	Income and Expense Summary		21,900	
	Income and Expense Summary			21,900
31	Max Cleland, Capital		5,000	
	Max Cleland, Withdrawals			5,000

SOLUTIONS

Learning Goal 16, continued

LG 16-5, continued

b.

Cash	Accounts Receivable	Office Supplies	Prepaid Insurance	Office Equipment
49,800	76,100 (a) 6,000 82,100	2,000 1,500	11,100 7,400	125,000
		(b) 500	(c) 3,700	
Accum. Dep'n Office Equip.	Accounts Payable	Unearned Revenue	Max Cleland, Capital	Max Cleland, Withdrawals
18,750 (d) 25,000 43,750	44,900 (f) 1,500 45,400	7,000 (e) 900 6,100	5,000 153,650 21,900 170,550	5,000 5,000 -0-
Service Revenue	Wages Expense	Rent Expense	Office Supplies Expense	Depreciation Expense
58,000 (a) 6,000 (e) 900 64,900	8,000 8,000 -0-	(c) 3,700 3,700 -0-	100 (b) 500 600 -0-	(d) 25,000 25,000 -0-
Advertising Expense	Income and Expense Summary			
4,200 (f) 1,500 5,700 -0-	64,900 43,000 21,900 -0-			

SOLUTIONS

Learning Goal 16, continued

LG 16-6.

a.

Johnson's Cleaning Service										
Worksheet										
For the Month Ended December 31, 2008										
Account Titles	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Balance Sheet	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	17,800				17,800				17,800	
Short-Term Investments	10,200				10,200				10,200	
Accounts Receivable	9,620				9,620				9,620	
Cleaning Supplies	5,700			(b) 3,850	1,850				1,850	
Prepaid Insurance	4,600			(a) 575	4,025				4,025	
Office Equipment	18,400				18,400				18,400	
Accum. Dep'n—Off.		9,150		(c) 150		9,300				9,300
Cleaning Equipment	58,000				58,000				58,000	
Accum. Dep'n—Clean.		5,000		(c) 500		5,500				5,500
Vans	123,500				123,500				123,500	
Accum. Dep'n—Vans		28,980		(c) 2,500		31,480				31,480
Accounts Payable		25,850		(f) 310		26,160				26,160
Unearned Revenue		7,500	(d) 5,500			2,000				2,000
Note Payable		40,100				40,100				40,100
S. Johnson, Capital		118,940				118,940				118,940
S. Johnson, Withdrawals	5,000				5,000				5,000	
Cleaning Service		68,100		(d) 5,500		73,600		73,600		
Wages Expense	41,300				41,300		41,300			
Rent Expense	4,500				4,500		4,500			
Auto & Gas Expense	550		(f) 310		860		860			
Advertising Expense	2,900				2,900		2,900			
Utilities Expense	450				450		450			
Repairs Expense	1,100				1,100		1,100			
Insurance Expense			(a) 575		575		575			
Supplies Expense			(b) 3,850		3,850		3,850			
Depreciation Expense			(c) 3,150		3,150		3,150			
Interest Expense			(e) 270		270		270			
Interest Payable				(e) 270		270				270
Totals	<u>303,620</u>	<u>303,620</u>	<u>13,655</u>	<u>13,655</u>	<u>307,350</u>	<u>307,350</u>	58,955	73,600	248,395	233,750
							14,645			14,645
							<u>73,600</u>	<u>73,600</u>	<u>248,395</u>	<u>248,395</u>

SOLUTIONS**Learning Goal 16, continued**LG 16-6, *continued*

b.

Johnson's Cleaning Service		
Income Statement		
For the Month Ended December 31, 2008		
Revenues:		
Cleaning service revenue		\$73,600
Expenses		
Wages expense	\$41,300	
Rent expense	4,500	
Supplies expense	3,850	
Depreciation expense	3,150	
Advertising expense	2,900	
Repairs expense	1,100	
Auto and gas expense	860	
Insurance expense	575	
Utilities expense	450	
Interest expense	<u>270</u>	
Total expenses		<u>58,955</u>
Net income		<u>\$14,645</u>

Johnson's Cleaning Service		
Statement of Owner's Equity		
For the Month Ended December 31, 2008		
S. Johnson, capital December 1	\$118,940	
Add: Net income	<u>14,645</u>	
		133,585
Less: Withdrawals	<u>5,000</u>	
S. Johnson, capital December 31		<u>\$128,585</u>

SOLUTIONS

Learning Goal 16, continued

LG 16-6, continued

Johnson's Cleaning Service		
Balance Sheet		
December 31, 2008		
Assets		
Current assets		
Cash	\$17,800	
Short-term investments	10,200	
Accounts receivable	9,620	
Cleaning supplies	1,850	
Prepaid insurance	<u>4,025</u>	
Total current assets		\$43,495
Property, plant, and equipment		
Office equipment	\$18,400	
Less: Accumulated depreciation	<u>9,300</u>	9,100
Cleaning equipment	58,000	
Less: Accumulated depreciation	<u>5,500</u>	52,500
Vans	123,500	
Less: Accumulated depreciation	<u>31,480</u>	<u>92,020</u>
Total property, plant, and equipment		<u>153,620</u>
Total assets		<u><u>\$197,115</u></u>
Liabilities and Owner's Equity		
Current liabilities:		
Accounts payable	\$26,160	
Unearned revenue	2,000	
Interest payable	<u>270</u>	
Total current liabilities		\$28,430
Long-term liabilities		
Note payable		<u>40,100</u>
Total liabilities		68,530
Owner's equity		
S. Johnson, capital		<u>128,585</u>
Total liabilities and owner's equity		<u><u>\$197,115</u></u>

SOLUTIONS

Learning Goal 16, continued

LG 16-6, *continued*

c and d.

GENERAL JOURNAL

Date	Account	Post. Ref.	Dr.	Cr.
2008	<i>Adjusting Entries</i>			
Dec.	(a)			
31	Insurance Expense		575	
	Prepaid Insurance			575
	(b)			
31	Supplies Expense		3,850	
	Cleaning Supplies			3,850
	(c)			
31	Depreciation Expense		3,150	
	Accumulated Depreciation—Office Equip.			150
	Accumulated Depreciation—Cleaning Equip.			500
	Accumulated Depreciation—Office Equip.			2,500
	(d)			
31	Unearned Revenue		5,500	
	Cleaning Service Revenue			5,500
	(e)			
31	Interest Expense		270	
	Interest Payable			270
	(f)			
31	Auto and Gas Expense		310	
	Accounts Payable			310

SOLUTIONS

Learning Goal 16, continued

LG 16-6, continued

Date	Account	Post. Ref.	Dr.	Cr.
2008	<i>Closing Entries</i>			
31	Cleaning Service Revenue		73,600	
	Income Summary			73,600
31	Income Summary		58,955	
	Wages Expense			41,300
	Rent Expense			4,500
	Auto & Gas Expense			860
	Advertising Expense			2,900
	Utilities Expense			450
	Repairs Expense			1,100
	Insurance Expense			575
	Supplies Expense			3,850
	Depreciation Expense			3,150
	Interest Expense			270
31	Income Summary		14,645	
	S. Johnson, Capital			14,645
31	S. Johnson, Capital		5,000	
	S. Johnson, Withdrawals			5,000

- e. Although total current assets exceed current liabilities, accounts payable and interest payable totaling \$26,430 will come due in January, requiring cash to pay these liabilities. The sources of cash available to the business are the cash account, short-term investments, and accounts receivable. It is likely that the cash and short-term investment accounts will be significantly reduced in January. (Estimating the “liquidity” situation is always important.)