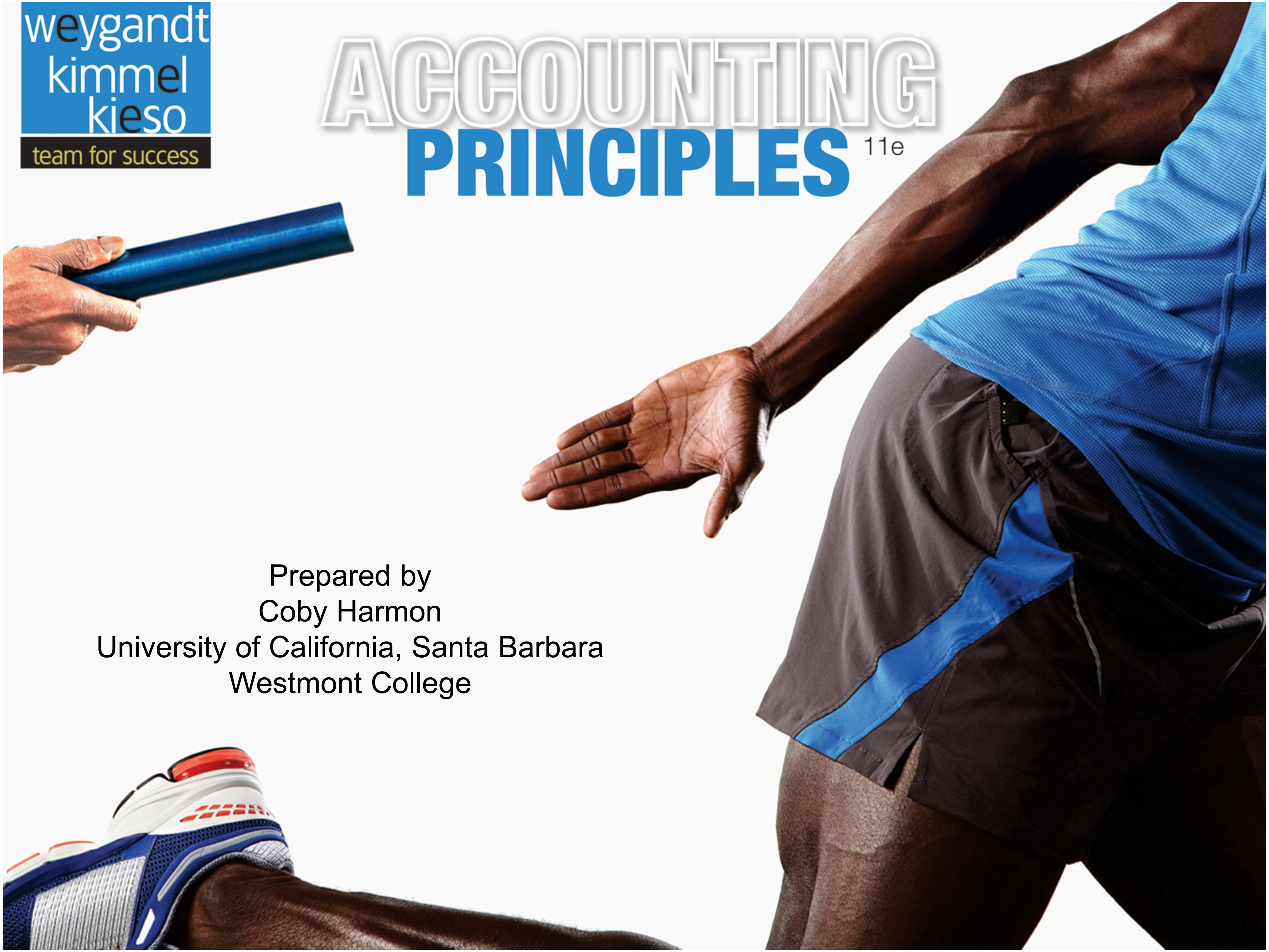
weygandt
kimmel
kieso
team for success

ACCOUNTING PRINCIPLES 11e



Prepared by
Coby Harmon
University of California, Santa Barbara
Westmont College

4 Completing the Accounting Cycle

Learning Objectives

After studying this chapter, you should be able to:

[1] Prepare a worksheet.

[2] Explain the process of closing the books.

[3] Describe the content and purpose of a post-closing trial balance.

[4] State the required steps in the accounting cycle.

[5] Explain the approaches to preparing correcting entries.

[6] Identify the sections of a classified balance sheet.

Preview of Chapter 4

COMPLETING THE ACCOUNTING CYCLE

Using a Worksheet	Closing the Books	Summary of the Accounting Cycle	Classified Balance Sheet
• Steps in preparation • Preparing financial statements • Preparing adjusting entries	• Preparing closing entries • Posting closing entries • Preparing a post-closing trial balance	• Reversing entries—An optional step • Correcting entries—An avoidable step	• Current assets • Long-term investments • Property, plant, and equipment • Intangible assets • Current liabilities • Long-term liabilities • Owner's equity

Accounting Principles
Eleventh Edition
Weygandt • Kimmel • Kieso

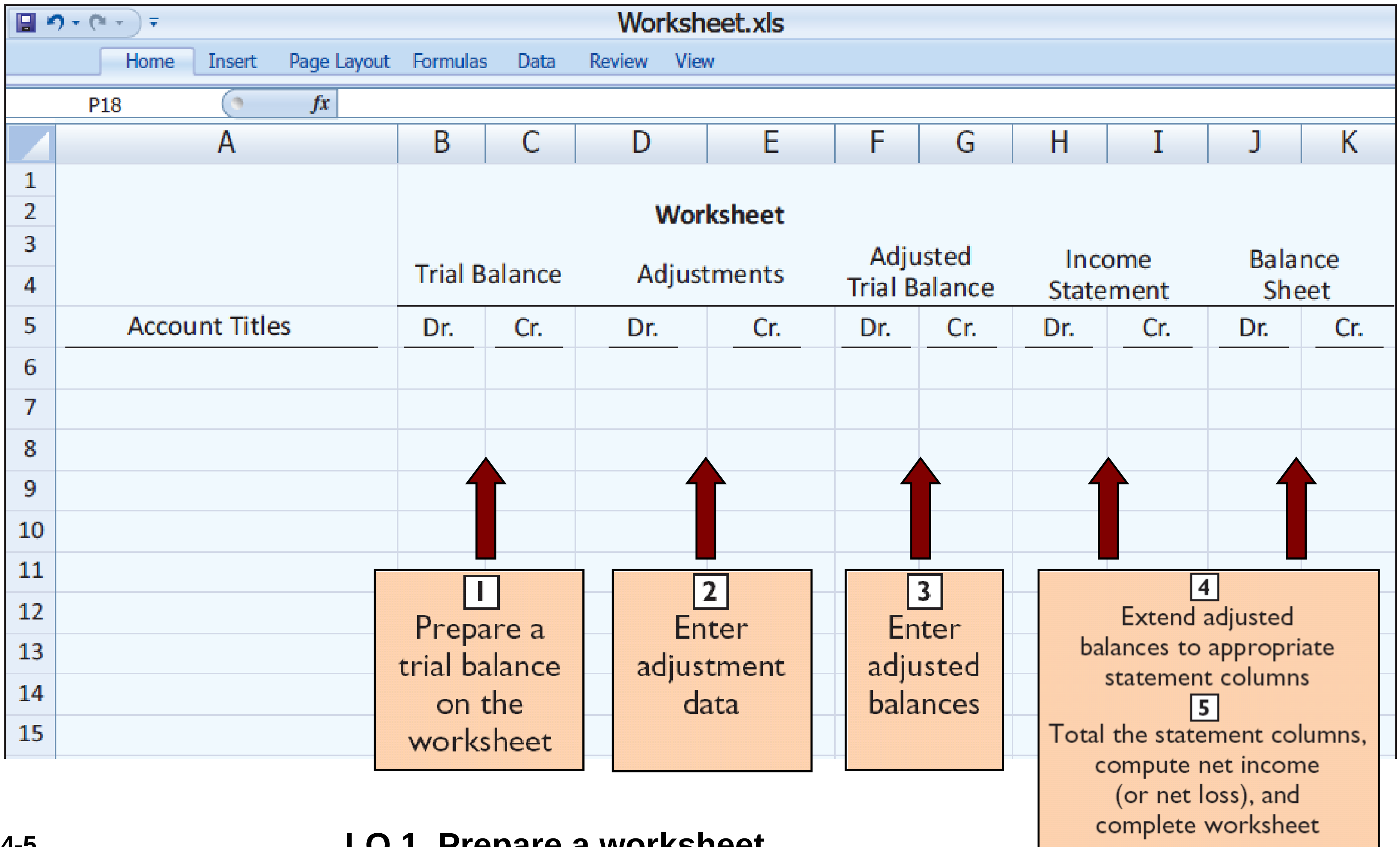
Using a Worksheet

Steps in Preparing a Worksheet

- Multiple-column form used in preparing financial statements.
- Not a permanent accounting record.
- Five step process.
- Use of worksheet is optional.

Steps in Preparing a Worksheet

Illustration 4-1



LO 1 Prepare a worksheet.

Steps in Preparing a Worksheet

1. Prepare a Trial Balance on the Worksheet

Illustration 4-2

Account Titles	Trial Balance Dr.	Trial Balance Cr.	Adjustments Dr.	Adjustments Cr.	Adjusted Trial Balance Dr.	Adjusted Trial Balance Cr.	Income Statement Dr.	Income Statement Cr.	Balance Sheet Dr.	Balance Sheet Cr.
Cash	15,200									
Supplies	2,500									
Prepaid Insurance	600									
Office Equipment	5,000									
Notes Payable		5,000								
Accounts Payable		2,500								
Unearned Revenue		1,200								
Owner's Capital		10,000								
Owner's Drawing	500									
Service Revenue		10,000								
Salaries Expense	4,000									
Rent Expense	900									
Totals	28,700	28,700								

Trial balance amounts come directly from ledger accounts.

Include all accounts with balances.

Steps in Preparing a Worksheet

Illustration 3-23
General journal showing adjusting entries

Adjusting Journal Entries

(Chapter 3)

General Journal				J2
Date	**Account Titles and Explanation**	**Ref.**	**Debit**	**Credit**
2014	Adjusting Entries			
Oct. 31	Supplies Expense	631	1,500	
	Supplies	126		1,500
	(To record supplies used)			
31	Insurance Expense	722	50	
	Prepaid Insurance	130		50
	(To record insurance expired)			
31	Depreciation Expense	711	40	
	Accumulated Depreciation—Equipment	158		40
	(To record monthly depreciation)			
31	Unearned Service Revenue	209	400	
	Service Revenue	400		400
	(To record revenue for services performed)			
31	Accounts Receivable	112	200	
	Service Revenue	400		200
	(To record revenue for services performed)			
31	Interest Expense	905	50	
	Interest Payable	230		50
	(To record interest on notes payable)			
31	Salaries and Wages Expense	726	1,200	
	Salaries and Wages Payable	212		1,200
	(To record accrued salaries and wages)			

LO 1 Prepare a worksheet.

Steps in Preparing a Worksheet

2. Enter the Adjustments in the Adjustments Columns

Account Titles	Trial Balance Dr.	Trial Balance Cr.	Adjustments Dr.	Adjustments Cr.	Adjusted Trial Balance Dr.	Adjusted Trial Balance Cr.	Income Statement Dr.	Income Statement Cr.	Balance Sheet Dr.	Balance Sheet Cr.
Cash	15,200									
Supplies	2,500			(a) 1,500						
Prepaid Insurance	600			(b) 50						
Office Equipment	5,000									
Notes Payable		5,000								
Accounts Payable		2,500								
Unearned Revenue		1,200	(d) 400							
Owner's Capital		10,000								
Owner's Drawing	500									
Service Revenue		10,000		(d) 400 (e) 200						
Salaries Expense	4,000		(g) 1,200							
Rent Expense	900									
Totals	28,700	28,700								
Supplies Expense			(a) 1,500							
Insurance Expense			(b) 50							
Accumulated Depreciation				(c) 40						
Depreciation Expense			(c) 40							
Accounts Receivable			(e) 200							
Interest Expense			(f) 50							
Interest Payable				(f) 50						
Salaries Payable				(g) 1,200						
Totals			3,440	3,440						

Adjustments Key:

(a) Supplies Used.
(b) Insurance Expired.
(c) Depreciation Expensed.
(d) Service Revenue Earned.
(e) Service Revenue Accrued.
(f) Interest Accrued.
(g) Salaries Accrued.

Enter adjustment amounts, total adjustments columns, and check for equality.

Add additional accounts as needed.

LO 1 Prepare a worksheet.

Steps in Preparing a Worksheet

3. Complete the Adjusted Trial Balance Columns

Account Titles	Trial Balance Dr.	Trial Balance Cr.	Adjustments Dr.	Adjustments Cr.	Adjusted Trial Balance Dr.	Adjusted Trial Balance Cr.	Income Statement Dr.	Income Statement Cr.	Balance Sheet Dr.	Balance Sheet Cr.
Cash	15,200				15,200					
Supplies	2,500			(a) 1,500	1,000					
Prepaid Insurance	600			(b) 50	550					
Office Equipment	5,000				5,000					
Notes Payable		5,000				5,000				
Accounts Payable		2,500				2,500				
Unearned Revenue		1,200	(d) 400			800				
Owner's Capital		10,000				10,000				
Owner's Drawing	500				500					
Service Revenue		10,000		(d) 400		10,600				
				(e) 200						
Salaries Expense	4,000		(g) 1,200		5,200					
Rent Expense	900				900					
Totals	28,700	28,700								
Supplies Expense			(a) 1,500		1,500					
Insurance Expense			(b) 50		50					
Accumulated Depreciation				(c) 40		40				
Depreciation Expense			(c) 40		40					
Accounts Receivable			(e) 200		200					
Interest Expense			(f) 50		50					
Interest Payable				(f) 50		50				
Salaries Payable				(g) 1,200		1,200				
Totals			3,440	3,440	30,190	30,190				

Total the adjusted trial balance columns and check for equality.

Steps in Preparing a Worksheet

4. Extend Amounts to Financial Statement Columns

	Trial Balance		Adjustments		Adjusted Trial Balance		Income Statement		Balance Sheet	
Account Titles	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	15,200				15,200					
Supplies	2,500			(a) 1,500	1,000					
Prepaid Insurance	600			(b) 50	550					
Office Equipment	5,000				5,000					
Notes Payable		5,000				5,000				
Accounts Payable		2,500				2,500				
Unearned Revenue		1,200	(d) 400			800				
Owner's Capital		10,000				10,000				
Owner's Drawing	500				500					
Service Revenue		10,000		(d) 400		10,600		10,600		
				(e) 200						
Salaries Expense	4,000		(g) 1,200		5,200		5,200			
Rent Expense	900				900		900			
Totals	28,700	28,700								
Supplies Expense			(a) 1,500		1,500		1,500			
Insurance Expense			(b) 50		50		50			
Accumulated Depreciation				(c) 40		40				
Depreciation Expense			(c) 40		40		40			
Accounts Receivable			(e) 200		200					
Interest Expense			(f) 50		50		50			
Interest Payable				(f) 50		50				
Salaries Payable				(g) 1,200		1,200				
Totals			3,440	3,440	30,190	30,190	7,740	10,600		

Extend all revenue and expense account balances to the income statement columns.

LO 1 Prepare a worksheet.

Steps in Preparing a Worksheet

5. Total Columns, Compute Net Income (Loss)

Account Titles	Trial Balance Dr.	Trial Balance Cr.	Adjustments Dr.	Adjustments Cr.	Adjusted Trial Balance Dr.	Adjusted Trial Balance Cr.	Income Statement Dr.	Income Statement Cr.	Balance Sheet Dr.	Balance Sheet Cr.
Cash	15,200				15,200				15,200	
Supplies	2,500			(a) 1,500	1,000				1,000	
Prepaid Insurance	600			(b) 50	550				550	
Office Equipment	5,000				5,000				5,000	
Notes Payable		5,000				5,000				5,000
Accounts Payable		2,500				2,500				2,500
Unearned Revenue		1,200	(d) 400			800				800
Owner's Capital		10,000				10,000				10,000
Owner's Drawing	500				500				500	
Service Revenue		10,000		(d) 400		10,600		10,600		
				(e) 200						
Salaries Expense	4,000		(g) 1,200		5,200		5,200			
Rent Expense	900				900		900			
Totals	28,700	28,700								
Supplies Expense			(a) 1,500		1,500		1,500			
Insurance Expense			(b) 50		50		50			
Accumulated Depreciation				(c) 40		40				40
Depreciation Expense			(c) 40		40		40			
Accounts Receivable			(e) 200		200				200	
Interest Expense			(f) 50		50		50			
Interest Payable				(f) 50		50				50
Salaries Payable				(g) 1,200		1,200				1,200
Totals			3,440	3,440	30,190	30,190	7,740	10,600	22,450	19,590
Net Income							2,860			2,860
Totals							10,600	10,600	22,450	22,450

Compute Net Income or Net Loss.

LO 1 Prepare a worksheet.

Steps in Preparing a Worksheet

Review Question

Net income is shown on a worksheet in the:

a. income statement debit column only.

b. balance sheet debit column only.

c. income statement credit column and balance sheet debit column.

d. income statement debit column and balance sheet credit column.

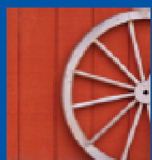
Using a Worksheet

Preparing Statements from a Worksheet

- Income statement is prepared from the income statement columns.
- Balance sheet and owner's equity statement are prepared from the balance sheet columns.
- Companies journalize and post adjusting entries.

Preparing Statements from a Worksheet

Illustration 4-4



PIONEER ADVERTISING AGENCY
Income Statement
For the Month Ended October 31, 2014

Revenues		
Service revenue		$10,600
Expenses		
Salaries and wages expense	$5,200	
Supplies expense	1,500	
Rent expense	900	
Insurance expense	50	
Interest expense	50	
Depreciation expense	40	
Total expenses		7,740
Net income		$ 2,860

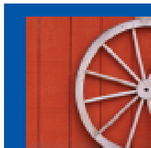
Preparing Statements from a Worksheet

Illustration 4-4

PIONEER ADVERTISING AGENCY
Owner's Equity Statement
For the Month Ended October 31, 2014

Owner's capital, October 1		$ –0–
Add: Investments	$10,000	
Net income	2,860	12,860
		12,860
Less: Drawings		500
Owner's capital, October 31		$12,360

Preparing Statements from a Worksheet



PIONEER ADVERTISING AGENCY
Balance Sheet
October 31, 2014

Illustration 4-4

Assets		
Cash		$15,200
Accounts receivable		200
Supplies		1,000
Prepaid insurance		550
Equipment	$5,000	
Less: Accumulated depreciation—equipment	40	4,960
Total assets		$21,910
Liabilities and Owner's Equity		
Liabilities		
Notes payable	$5,000	
Accounts payable	2,500	
Interest payable	50	
Unearned service revenue	800	
Salaries and wages payable	1,200	
Total liabilities		$ 9,550
Owner's equity		
Owner's capital		12,360
Total liabilities and owner's equity		$21,910

LO 1

Using a Worksheet

Preparing Adjusting Entries from a Worksheet

- Adjusting entries are prepared from the adjustments columns of the worksheet.
- Journalizing and posting of adjusting entries follows the preparation of financial statements when a worksheet is used.

> DO IT!

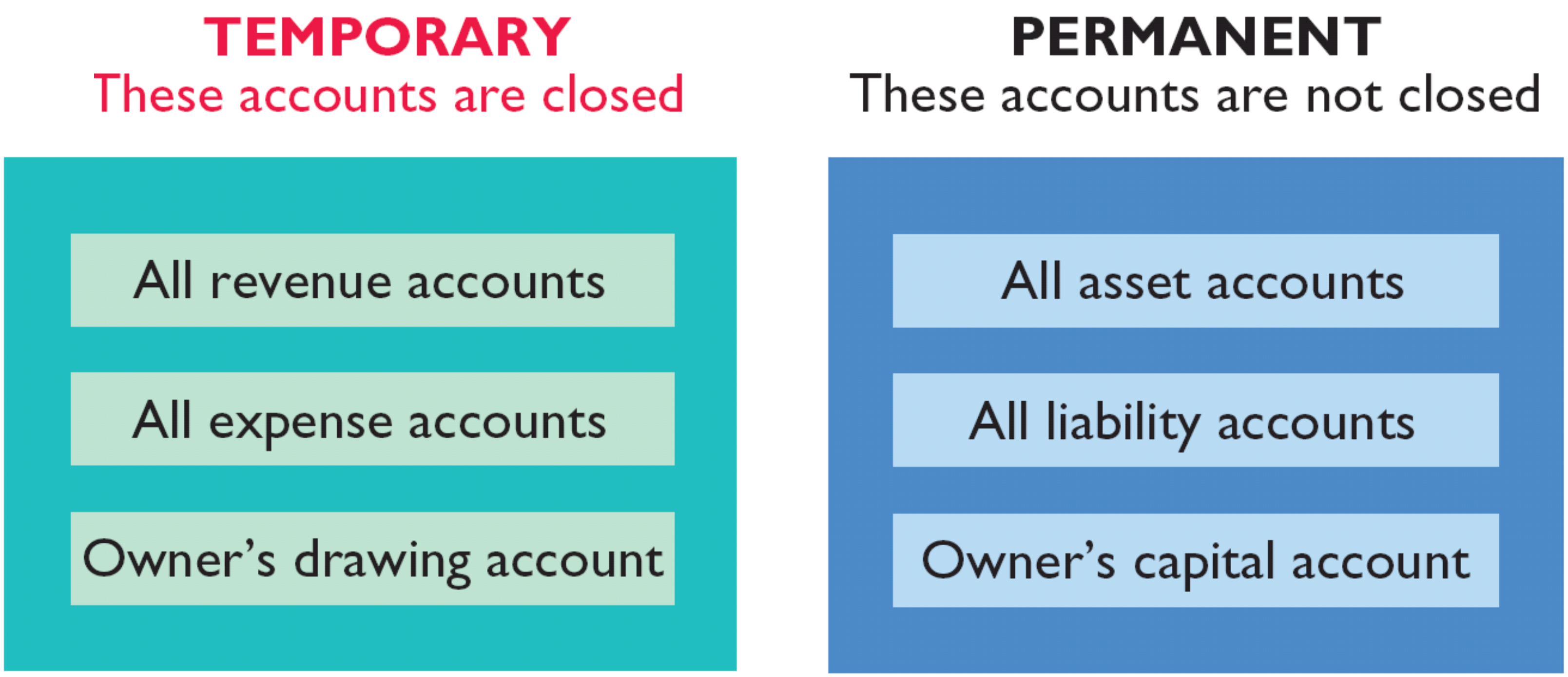
Susan Elbe is preparing a worksheet. Explain to Susan how she should extend the following adjusted trial balance accounts to the financial statement columns of the worksheet.

Cash	Balance sheet (debit column)
Accumulated Depreciation	Balance Sheet (credit column)
Accounts Payable	Balance Sheet (credit column)
Owner’s Drawings	Balance sheet (debit column)
Service Revenue	Income statement (credit column)
Salaries and Wages Expense	Income statement (debit column)

Closing the Books

At the end of the accounting period, the company makes the accounts ready for the next period.

Illustration 4-5



LO 2 Explain the process of closing the books.

Closing the Books

Preparing Closing Entries

Closing entries formally recognize, in the general ledger, the transfer of

- net income (or net loss) and
- owner's drawing

to owner's capital.

Closing entries are only made at the end of the annual accounting period.

Closing the Books

Note:

Owner's Drawing is closed directly to Capital and *not* to Income Summary because Owner's Drawing is not an expense.

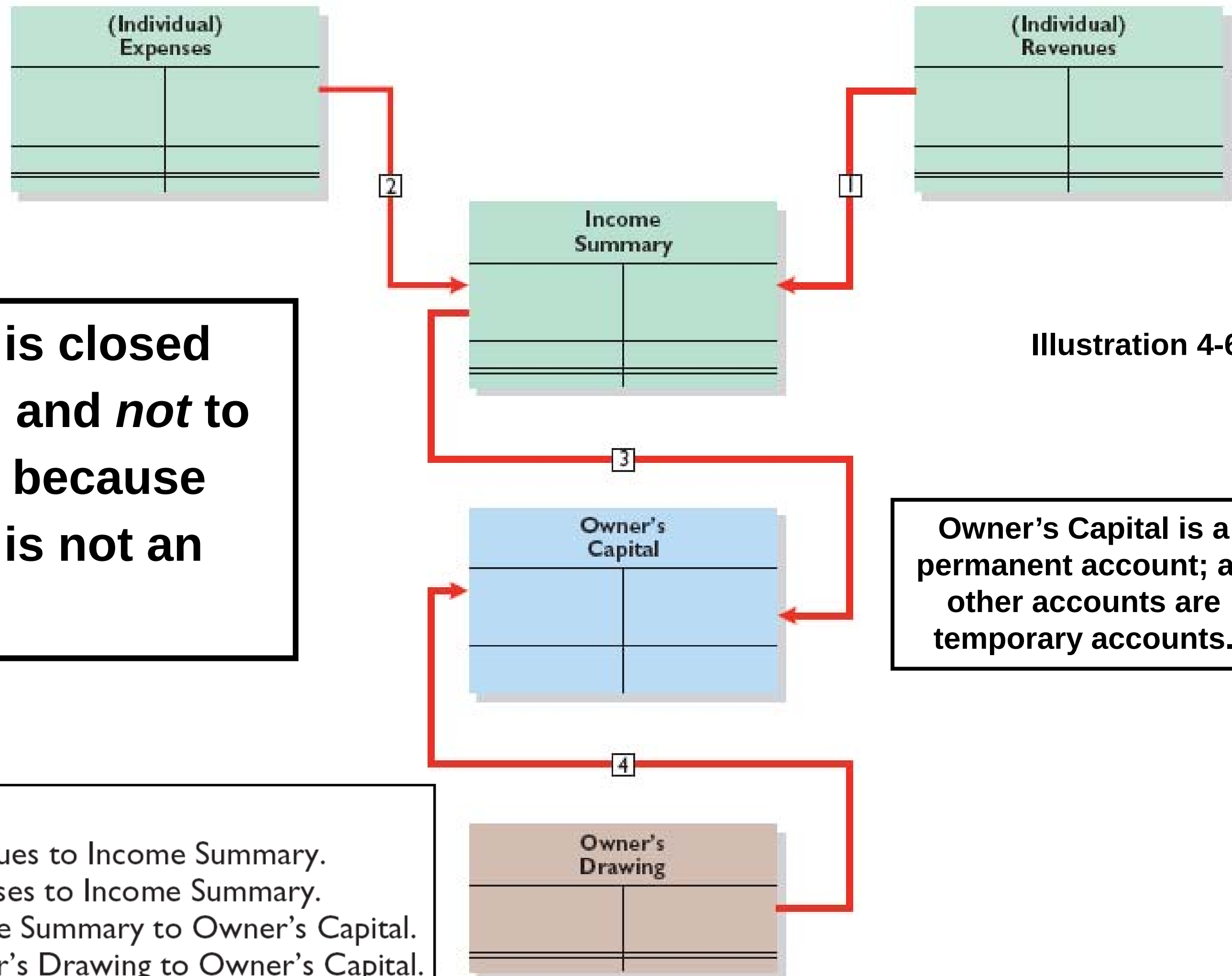


Illustration 4-6

Owner's Capital is a permanent account; all other accounts are temporary accounts.

Key:
1 Close Revenues to Income Summary.
2 Close Expenses to Income Summary.
3 Close Income Summary to Owner's Capital.
4 Close Owner's Drawing to Owner's Capital.

LO 2 Explain the process of closing the books.

Closing the Books

Closing Entries Illustrated

GENERAL JOURNAL				J3
Date	**Account Titles and Explanation**	**Ref.**	**Debit**	**Credit**
	Closing Entries			
	(1)			
2014 Oct. 31	Service Revenue	400	10,600	
	Income Summary	350		10,600
	(To close revenue account)			
	(2)			
31	Income Summary	350	7,740	
	Supplies Expense	631		1,500
	Depreciation Expense	711		40
	Insurance Expense	722		50
	Salaries and Wages Expense	726		5,200
	Rent Expense	729		900
	Interest Expense	905		50
	(To close expense accounts)			
	(3)			
31	Income Summary	350	2,860	
	Owner's Capital	301		2,860
	(To close net income to capital)			
	(4)			
31	Owner's Capital	301	500	
	Owner's Drawings	306		500
	(To close drawings to capital)			

Illustration 4-7
Closing entries journalized

Closing the Books

Posting Closing Entries

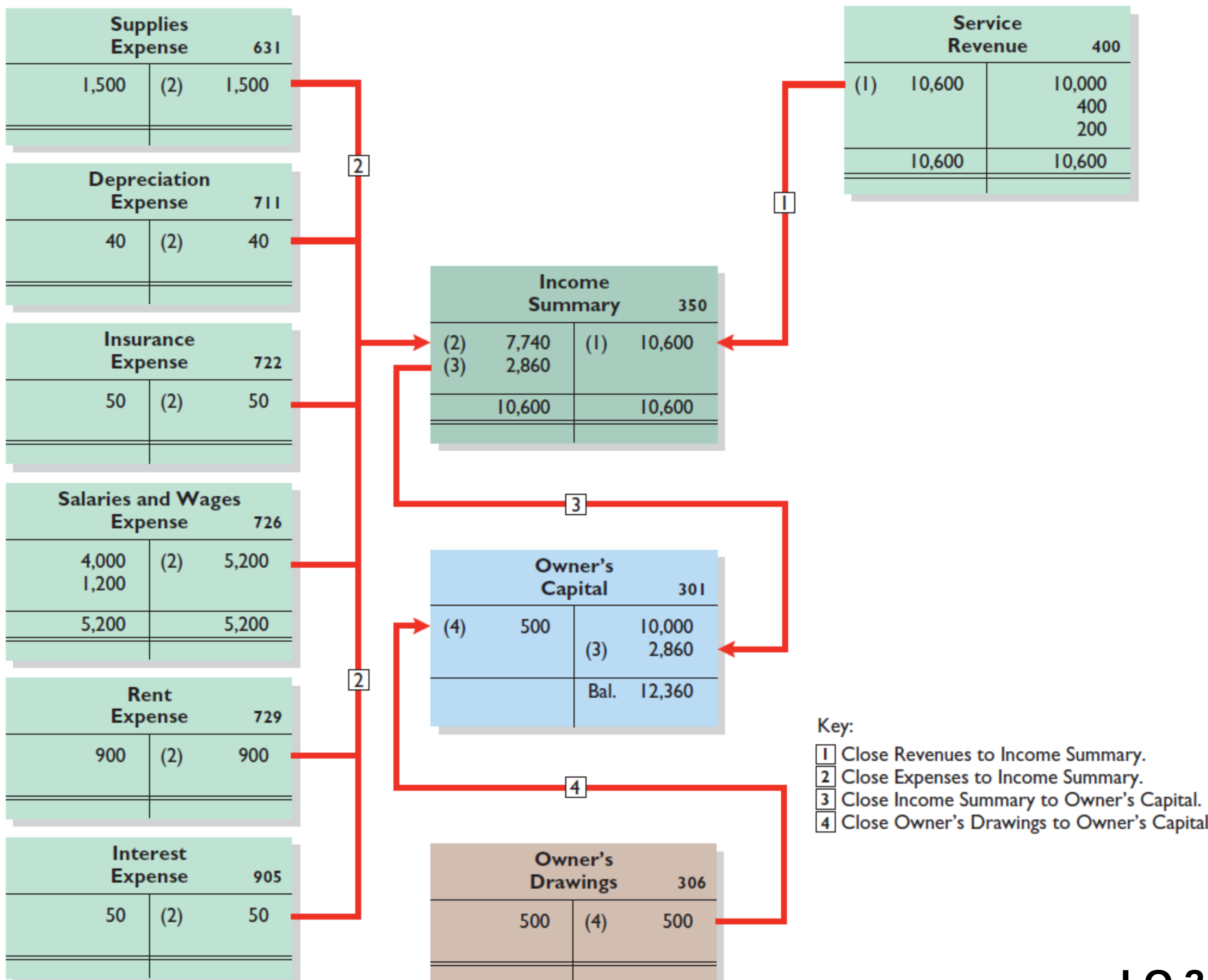


Illustration 4-8

LO 2

ACCOUNTING ACROSS THE ORGANIZATION

Cisco Performs the Virtual Close

Technology has dramatically shortened the closing process. Recent surveys have reported that the average company now takes only six to seven days to close, rather than 20 days. But a few companies do much better. Cisco Systems can perform a "virtual close"—closing within 24 hours on any day in the quarter. The same is true at Lockheed Martin Corp., which improved its closing time by 85% in just the last few years. Not very long ago, it took 14 to 16 days. Managers at these companies emphasize that this increased speed has not reduced the accuracy and completeness of the data.

This is not just showing off. Knowing exactly where you are financially all of the time allows the company to respond faster than competitors. It also means that the hundreds of people who used to spend 10 to 20 days a quarter tracking transactions can now be more usefully employed on things such as mining data for business intelligence to find new business opportunities.

Source: "Reporting Practices: Few Do It All," *Financial Executive* (November 2003), p. 11.

? Who else benefits from a shorter closing process? (See page 211.)

Preparing a Post-Closing Trial Balance

Purpose is to prove the equality of the permanent account balances after journalizing and posting of closing entries.

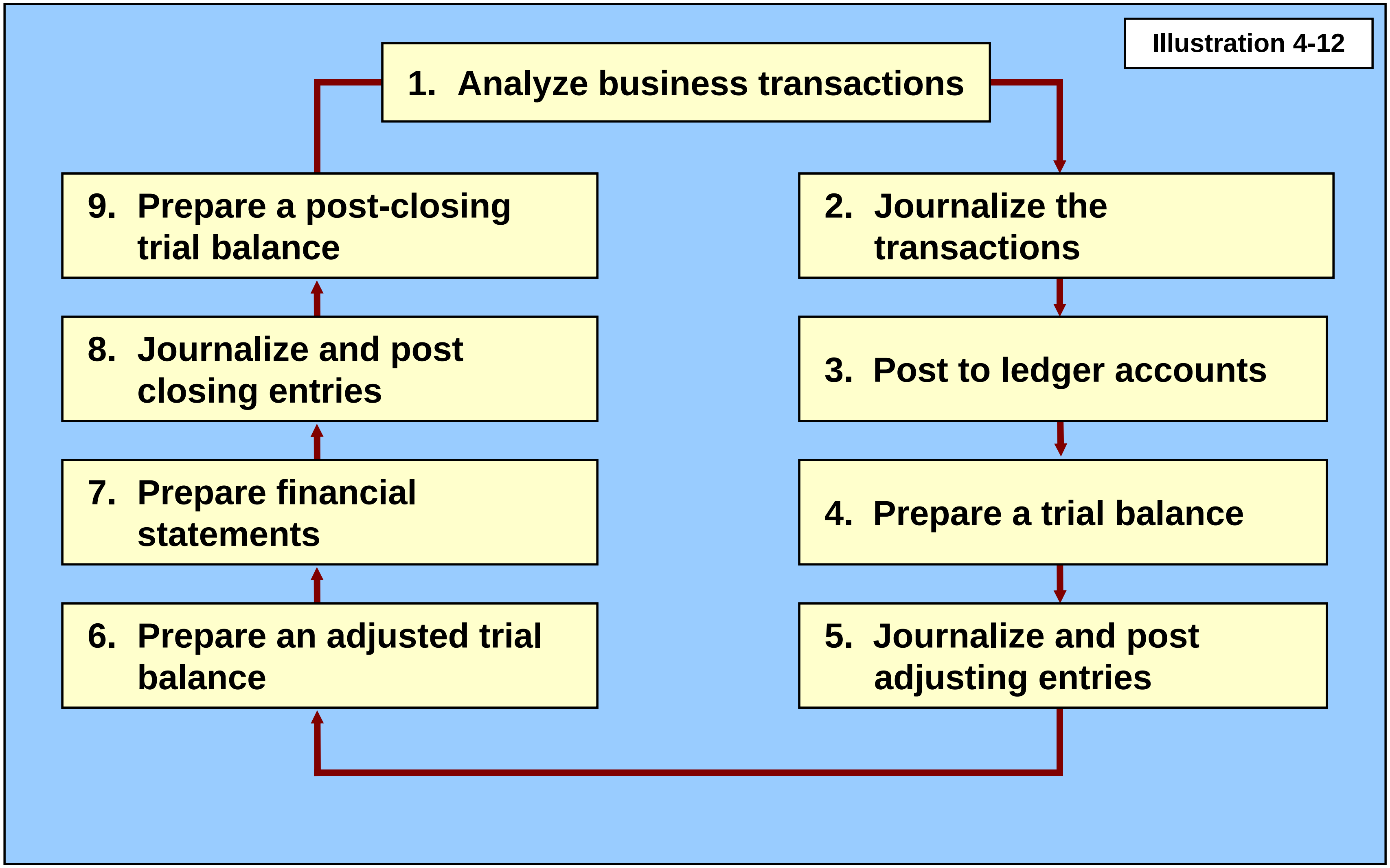
PIONEER ADVERTISING AGENCY
Post-Closing Trial Balance
October 31, 2014

Illustration 4-9

	Debit	Credit
Cash	$ 15,200	
Accounts Receivable	200	
Supplies	1,000	
Prepaid Insurance	550	
Equipment	5,000	
Accumulated Depreciation—Equipment		$ 40
Notes Payable		5,000
Accounts Payable		2,500
Unearned Service Revenue		800
Salaries and Wages Payable		1,200
Interest Payable		50
Owner's Capital		12,360
	$21,950	$21,950

LO 3

Summary of the Accounting Cycle



LO 4 State the required steps in the accounting cycle.

Summary of the Accounting Cycle

Correcting Entries—An Avoidable Step

- Unnecessary if the records are error-free.
- Made whenever an error is discovered.
- Must be posted before closing entries.

Instead of preparing a correcting entry, it is possible to reverse the incorrect entry and then prepare the correct entry.

LO 5 Explain the approaches to preparing correcting entries.

Correcting Entries—An Avoidable Step

Illustration (Case 1): On May 10, Mercato Co. journalized and posted a $50 cash collection on account from a customer as a debit to Cash $50 and a credit to Service Revenue $50. The company discovered the error on May 20, when the customer paid the remaining balance in full.

Incorrect entry	Cash	50	
	Service Revenue		50
Correct entry	Cash	50	
	Accounts Receivable		50
Correcting entry	Service Revenue	50	
	Accounts Receivable		50

Correcting Entries—An Avoidable Step

Illustration (Case 2): On May 18, Mercato purchased on account equipment costing $450. The transaction was journalized and posted as a debit to Equipment $45 and a credit to Accounts Payable $45. The error was discovered on June 3,

	Account	Debit	Credit
Incorrect entry	Equipment	45	
	Accounts Payable		45
Correct entry	Equipment	450	
	Accounts Payable		450
Correcting entry	Equipment	405	
	Accounts Payable		405

ACCOUNTING ACROSS THE ORGANIZATION

Yale Express Loses Some Transportation Bills

Yale Express, a short-haul trucking firm, turned over much of its cargo to local truckers to complete deliveries. Yale collected the entire delivery charge. When billed by the local trucker, Yale sent payment for the final phase to the local trucker. Yale used a cutoff period of 20 days into the next accounting period in making its adjusting entries for accrued liabilities. That is, it waited 20 days to receive the local truckers' bills to determine the amount of the unpaid but incurred delivery charges as of the balance sheet date.

On the other hand, Republic Carloading, a nationwide, long-distance freight forwarder, frequently did not receive transportation bills from truckers to whom it passed on cargo until months after the year-end. In making its year-end adjusting entries, Republic waited for months in order to include all of these outstanding transportation bills.

When Yale Express merged with Republic Carloading, Yale's vice president employed the 20-day cutoff procedure for both firms. As a result, millions of dollars of Republic's accrued transportation bills went unrecorded. When the company detected the error and made correcting entries, these and other errors changed a reported profit of $1.14 million into a loss of $1.88 million!

? What might Yale Express's vice president have done to produce more accurate financial statements without waiting months for Republic's outstanding transportation bills? (See page 211.)

The Classified Balance Sheet

- Presents a snapshot at a point in time.
- To improve understanding, companies group similar assets and similar liabilities together.

Standard Classifications

Illustration 4-17

Assets	Liabilities and Owner's Equity
Current assets	Current liabilities
Long-term investments	Long-term liabilities
Property, plant, and equipment	Owner's (Stockholders') equity
Intangible assets	

The Classified Balance Sheet

FRANKLIN COMPANY
Balance Sheet
October 31, 2014

Illustration 4-18

Assets			
Current assets			
Cash		$ 6,600	
Debt investments		2,000	
Accounts receivable		7,000	
Notes receivable		1,000	
Inventory		3,000	
Supplies		2,100	
Prepaid insurance		400	
Total current assets			$22,100
Long-term investments			
Stock investments		5,200	
Investment in real estate		2,000	7,200
Property, plant, and equipment			
Land		10,000	
Equipment	$24,000		
Less: Accumulated depreciation—equipment	5,000	19,000	29,000
Intangible assets			
Patents			3,100
Total assets			$61,400

LO 6

The Classified Balance Sheet

FRANKLIN COMPANY
Balance Sheet
October 31, 2014

Illustration 4-18

Liabilities and Owner's Equity		
Current liabilities		
Notes payable	$11,000	
Accounts payable	2,100	
Unearned service revenue	900	
Salaries and wages payable	1,600	
Interest payable	450	
Total current liabilities		$16,050
Long-term liabilities		
Mortgage payable	10,000	
Notes payable	1,300	
Total long-term liabilities		11,300
Total liabilities		27,350
Owner's equity		
Owner's capital		34,050
Total liabilities and owner's equity		$61,400

The Classified Balance Sheet

Current Assets

- Assets that a company expects to **convert to cash** or **use up** within one year or the operating cycle, whichever is longer.
- **Operating cycle** is the average time it takes from the purchase of inventory to the collection of cash from customers.

The Classified Balance Sheet

Current Assets

Illustration 4-19

SOUTHWEST AIRLINES CO. Balance Sheet (partial) (in millions)	
Current assets	
Cash and cash equivalents	$1,390
Short-term investments	369
Accounts receivable	241
Inventories	181
Prepaid expenses and other current assets	420
Total current assets	$2,601

Usually listed in the order they expect to convert them into cash.

The Classified Balance Sheet

Question

Cash, and other resources that are reasonably expected to be realized in cash or sold or consumed in the business within one year or the operating cycle, are called:

a. Current assets.

b. Intangible assets.

c. Long-term investments.

d. Property, plant, and equipment.

The Classified Balance Sheet

Long-Term Investments

- Investments in stocks and bonds of other companies.
- Investments in long-term assets such as land or buildings that a company is not currently using in its operating activities.

Illustration 4-20

YAHOO! INC. Balance Sheet (partial) (in thousands)	
Long-term investments	
Investments in securities	$90,266

The Classified Balance Sheet

Property, Plant, and Equipment

- Long useful lives.
- Currently used in operations.
- **Depreciation** - allocating the cost of assets to a number of years.
- **Accumulated depreciation** - total amount of depreciation expensed thus far in the asset's life.

Alternative Terminology
Property, plant, and equipment is sometimes called *fixed assets* or *plant assets*.

LO 6 Identify the sections of a classified balance sheet.

The Classified Balance Sheet

Property, Plant, and Equipment

Illustration 4-21

COOPER TIRE & RUBBER COMPANY Balance Sheet (partial) (in thousands)		
Property, plant, and equipment		
Land and land improvements	$ 41,553	
Buildings	298,706	
Machinery and equipment	1,636,091	
Molds, cores, and rings	268,158	$2,244,508
Less: Accumulated depreciation		1,252,692
		$ 991,816

LO 6 Identify the sections of a classified balance sheet.

The Classified Balance Sheet

Intangible Assets

- Assets that do not have physical substance.

Illustration 4-22

TIME WARNER, INC.
Balance Sheet (partial)
(in millions)

Intangible assets	
Goodwill	$40,953
Film library	2,690
Customer lists	2,540
Cable television franchises	38,048
Sports franchises	262
Brands, trademarks, and other intangible assets	8,313
	$92,806

The Classified Balance Sheet

Question

Patents and copyrights are

a. Current assets.

b. Intangible assets.

c. Long-term investments.

d. Property, plant, and equipment.

PEOPLE, PLANET, AND PROFIT INSIGHT

Regaining Goodwill

After falling to unforeseen lows amidst scandals, recalls, and economic crises, the American public's positive perception of the reputation of corporate America is on the rise. Overall corporate reputation is experiencing rehabilitation as the American public gives high marks overall to corporate America, specific industries, and the largest number of individual companies in a dozen years. This is according to the findings of the *2011 Harris Interactive RQ Study*, which measures the reputations of the 60 most visible companies in the United States.

The survey focuses on six reputational dimensions that influence reputation and consumer behavior. Four of these dimensions, along with the five corporations that ranked highest within each, are as follows.

- **Social Responsibility**: (1) Whole Foods Market, (2) Johnson & Johnson, (3) Google, (4) The Walt Disney Company, (5) Procter & Gamble Co.
- **Emotional Appeal**: (1) Johnson & Johnson, (2) Amazon.com, (3) UPS, (4) General Mills, (5) Kraft Foods
- **Financial Performance**: (1) Google, (2) Berkshire Hathaway, (3) Apple, (4) Intel, (5) The Walt Disney Company
- **Products and Services**: (1) Intel Corporation, (2) 3M Company, (3) Johnson & Johnson, (4) Google, (5) Procter & Gamble Co.

Source: www.harrisinteractive.com.

? Name two industries today which are probably rated low on the reputational characteristics of "being trusted" and "having high ethical standards." (See page 212.)

DO IT!

Baxter Hoffman recently received the following information related to Hoffman Company's December 31, 2014, balance sheet.

Prepaid insurance	$ 2,300	Inventory	$3,400
Cash	800	Accumulated depreciation—	
Equipment	2,700	Equipment	10,700
Accounts receivable	1,100		

Prepare the asset section of Hoffman Company's balance sheet.

Assets

Current assets	
Total current assets	$ 7,600
Property, plant, and equipment	
Total assets	$15,600

LO 6

The Classified Balance Sheet

Current Liabilities

- Obligations company is to pay within the coming year or its operating cycle, whichever is longer.
- Usually list notes payable first, followed by accounts payable. Other items follow in order of magnitude.
- Liquidity - ability to pay obligations expected to be due within the next year.

The Classified Balance Sheet

Current Liabilities

Illustration 4-23

MARCUS CORPORATION Balance Sheet (partial) (in thousands)	
Current liabilities	
Notes payable	$ 239
Accounts payable	24,242
Current maturities of long-term debt	57,250
Other current liabilities	27,477
Income taxes payable	11,215
Salaries and wages payable	6,720
Total current liabilities	$127,143

LO 6 Identify the sections of a classified balance sheet.

ACCOUNTING ACROSS THE ORGANIZATION

Can a Company Be Too Liquid?

There actually is a point where a company can be too liquid—that is, it can have too much working capital (current assets less current liabilities). While it is important to be liquid enough to be able to pay short-term bills as they come due, a company does not want to tie up its cash in extra inventory or receivables that are not earning the company money.

By one estimate from the REL Consultancy Group, the thousand largest U.S. companies have on their books cumulative excess working capital of $764 billion. Based on this figure, companies could have reduced debt by 36% or increased net income by 9%. Given that managers throughout a company are interested in improving profitability, it is clear that they should have an eye toward managing working capital. They need to aim for a "Goldilocks solution"—not too much, not too little, but just right.

Source: K. Richardson, "Companies Fall Behind in Cash Management," *Wall Street Journal* (June 19, 2007).

? What can various company managers do to ensure that working capital is managed efficiently to maximize net income? (See page 212.)

The Classified Balance Sheet

Long-Term Liabilities

- Obligations a company expects to pay after one year.

Illustration 4-24

THE PROCTER & GAMBLE COMPANY Balance Sheet (partial) (in millions)	
Long-term liabilities	
Long-term debt	$23,375
Deferred income taxes	12,015
Other noncurrent liabilities	5,147
Total long-term liabilities	$40,537

The Classified Balance Sheet

Question

Which of the following is not a long-term liability?

a. Bonds payable

b. Current maturities of long-term obligations

c. Long-term notes payable

d. Mortgages payable

The Classified Balance Sheet

Owner's Equity

- Proprietorship - one capital account.
- Partnership - capital account for each partner.
- Corporation - Capital Stock and Retained Earnings.

Alternative Terminology
Common stock is sometimes called *capital stock*.

NORDSTROM, INC.
Balance Sheet (partial)
($ in thousands)

Illustration 4-25

Stockholders' equity	
Common stock, 271,331 shares	$ 685,934
Retained earnings	1,406,747
Total stockholders' equity	$2,092,681

Reversing Entries

- It is often helpful to reverse some of the adjusting entries before recording the regular transactions of the next period.
- Companies make a reversing entry at the beginning of the next accounting period.
- Each reversing entry is the exact opposite of the adjusting entry made in the previous period.
- The use of reversing entries does not change the amounts reported in the financial statements.

APPENDIX 4A Reversing Entries

Illustration: To illustrate the optional use of reversing entries for accrued expenses, we will use the salaries expense transactions for Pioneer Advertising Agency.

1. October 26 (initial salary entry): Pioneer pays $4,000 of salaries earned between October 15 and October 26.
2. October 31 (adjusting entry): Salaries earned between October 29 and October 31 are $1,200. The company will pay these in the November 9 payroll.
3. November 9 (subsequent salary entry): Salaries paid are $4,000. Of this amount, $1,200 applied to accrued wages payable and $2,800 was earned between November 1 and November 9.

APPENDIX 4A Reversing Entries

Illustration 4A-1

Without Reversing Entries (per chapter)

	Initial Salary Entry		
Oct. 26	Salaries and Wages Expense	4,000	
	Cash		4,000
	Adjusting Entry		
Oct. 31	Salaries and Wages Expense	1,200	
	Salaries and Wages Payable		1,200
	Closing Entry		
Oct. 31	Income Summary	5,200	
	Salaries and Wages Expense		5,200
	Reversing Entry		
Nov. 1	No reversing entry is made.		
	Subsequent Salary Entry		
Nov. 9	Salaries and Wages Payable	1,200	
	Salaries and Wages Expense	2,800	
	Cash		4,000

With Reversing Entries (per appendix)

	Initial Salary Entry		
Oct. 26	Same entry		
	Adjusting Entry		
Oct. 31	Same entry		
	Closing Entry		
Oct. 31	Same entry		
	Reversing Entry		
Nov. 1	Salaries and Wages Payable	1,200	
	Salaries and Wages Expense		1,200
	Subsequent Salary Entry		
Nov. 9	Salaries and Wages Expense	4,000	
	Cash		4,000

APPENDIX 4A Reversing Entries

Illustration 4A-2
Postings with reversing entries

Salaries and Wages Expense

10/26	Paid	4,000	10/31	Closing	5,200
31	Adjusting	1,200			
		5,200			5,200
11/9	Paid	4,000	**11/1**	**Reversing**	**1,200**

Salaries and Wages Payable

11/1	**Reversing**	**1,200**	10/31	Adjusting	1,200

LO 7 Prepare reversing entries.

A Look at IFRS

Key Points

- The procedures of the closing process are applicable to all companies, whether they are using IFRS or GAAP.
- IFRS recommends but does not require the use of the title "statement of financial position" rather than balance sheet.
- The format of statement of financial position information is often presented differently under IFRS. Although no specific format is required, most companies that follow IFRS present statement of financial position information in this order:
  - Noncurrent assets
  - Current assets
  - Equity
  - Noncurrent liabilities
  - Current liabilities

A Look at IFRS

Key Points

- IFRS requires a classified statement of financial position except in very limited situations. IFRS follows the same guidelines as this textbook for distinguishing between current and noncurrent assets and liabilities.
- Under IFRS, current assets are usually listed in the reverse order of liquidity. For example, under GAAP cash is listed first, but under IFRS it is listed last.
- Some companies report the subtotal net assets, which equals total assets minus total liabilities.
- IFRS has many differences in terminology that you will notice in this textbook.

A Look at IFRS

Key Points

- Both IFRS and GAAP require disclosures about (1) accounting policies followed, (2) judgments that management has made in the process of applying the entity's accounting policies, and (3) the key assumptions and estimation uncertainty that could result in a material adjustment to the carrying amounts of assets and liabilities within the next financial year.
- Comparative prior-period information must be presented and financial statements must be prepared annually.
- Both GAAP and IFRS are increasing the use of fair value to report assets. However, at this point IFRS has adopted it more broadly. As examples, under IFRS companies can apply fair value to property, plant, and equipment; natural resources; and in some cases intangible assets.

A Look at IFRS

Looking to the Future

The IASB and the FASB are working on a project to converge their standards related to financial statement presentation. A key feature of the proposed framework is that each of the statements will be organized in the same format, to separate an entity's financing activities from its operating and investing activities and, further, to separate financing activities into transactions with owners and creditors. Thus, the same classifications used in the statement of financial position would also be used in the income statement and the statement of cash flows. The project has three phases. You can follow the joint financial presentation project at the following link:

http://www.fasb.org/project/financial_statement_presentation.shtml.

LO 8 Compare the procedures for the closing process under GAAP and IFRS.

A Look at IFRS

IFRS Self-Test Questions

Which of the following statements is false?

a) Assets equals liabilities plus equity.

b) Under IFRS, companies sometimes net liabilities against assets to report “net assets.”

c) The FASB and IASB are working on a joint conceptual framework project.

d) Under IFRS, the statement of financial position is usually referred to as the statement of assets and equity.

LO 8 Compare the procedures for the closing process under GAAP and IFRS.

A Look at IFRS

IFRS Self-Test Questions

A company has purchased a tract of land and expects to build a production plant on the land in approximately 5 years. During the 5 years before construction, the land will be idle. Under IFRS, the land should be reported as:

a) land expense.

b) property, plant, and equipment.

c) an intangible asset.

d) a long-term investment.

LO 8 Compare the procedures for the closing process under GAAP and IFRS.

A Look at IFRS

IFRS Self-Test Questions

Current assets under IFRS are listed generally:

a) by importance.

b) in the reverse order of their expected conversion to cash.

c) by longevity.

d) alphabetically.

LO 8 Compare the procedures for the closing process under GAAP and IFRS.

Copyright