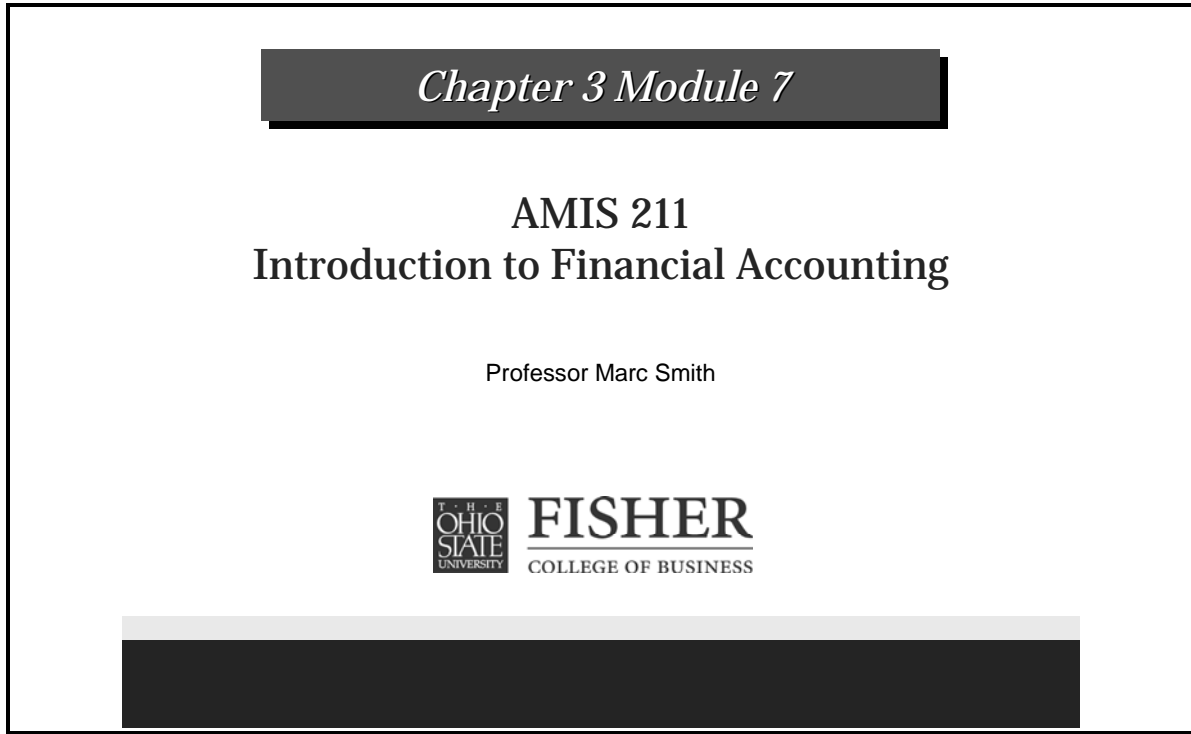


Chapter 3, Module 7 – The Accounting Cycle

Slide 1

The slide content is enclosed in a black rectangular border. At the top, there is a dark grey horizontal bar with the text "Chapter 3 Module 7" in a white, italicized serif font. Below this bar, the text "AMIS 211" is centered in a bold, black, sans-serif font. Underneath "AMIS 211", the text "Introduction to Financial Accounting" is centered in a bold, black, serif font. Below the title, the text "Professor Marc Smith" is centered in a smaller, black, sans-serif font. At the bottom center, there is the logo for Fisher College of Business at Ohio State University, which includes a small square icon with "T · H · E" above "OHIO STATE UNIVERSITY" and the word "FISHER" in a large, bold, serif font above "COLLEGE OF BUSINESS". At the very bottom of the slide, there is a light grey horizontal bar above a dark grey horizontal bar.

Hi everyone. Welcome back.

Now that we know all about Journal Entries, debits and credits, and effects of transactions, let's spend a little bit of time and talk about the basic Accounting Cycle.

Let's start with the first slide.

Slide 2

Chapter 3 Module 7: Accounting Cycle

Accounting Cycle – Basic Steps:

- 1. Record transactions in the journal (use journal entries)**
- 2. Post debit and credit amounts from the journal to the ledger (done to determine ending balance in each account)**
- 3. Prepare a trial balance**

Let's list out the basic steps in the Accounting Cycle.

Now, recognize: the steps that we list are not the only steps. In fact, when we come back and go further in the textbook, we will see additional steps that are part of the Cycle.

But, as of right now, these are the steps that we have covered.

Step 1: Record transactions in the Journal using your Journal Entries.

Once the transactions have been recorded, Step 2 is to post them.

Step 2: Post the debits and credits from the Journal into the T-Accounts or the Ledger.

Remember: the reason we post to the Ledger is to figure out the Ending Balance in each individual account.

Once we have the Ending Balance, the third step (Step 3) is to prepare what is called a Trial Balance.

It is this Trial Balance that we need to spend a little bit of time talking about.

Go to the next slide with me.

Slide 3

<i>Chapter 3 Module 7: Trial Balance</i>	
<ul style="list-style-type: none">• The trial balance is a list of accounts and their balances at a given time.• The primary purpose of a trial balance is to prove debits = credits after posting.• If debits and credits do not agree, the trial balance can be used to uncover errors in journalizing and posting.	

A Trial Balance is simply a listing of the accounts with their balances. That is all it is. It is a list of the accounts with their balance.

The reason we do a Trial Balance is to check something—and we are checking a very important idea—and that is: that total debits must equal (=) total credits.

So, we list off the accounts with their balance simply to make sure that the debits and credits equal (=).

If we have a problem—if the debits and credits do not agree—we can use the Trial Balance to figure out what went wrong.

Most likely, we had an error in making a Journal Entry or we had an error in doing posting.

But, the Trial Balance will help us figure it out by narrowing down where the error could be and exactly what the problem is.

If you would go to the next slide with me...

Slide 4

<i>Chapter 3 Module 7: Trial Balance</i>		
PIONEER ADVERTISING AGENCY Trial Balance October 31, 2005		
	Debit	Credit
Cash	\$ 15,200	
Accounts Receivable	2,500	
Inventory	600	
Office Equipment	5,000	
Notes Payable		\$ 5,000
Accounts Payable		2,500
Common Stock		7,000
Retained Earnings		4,200
Dividends	500	
Sales Revenue		10,000
Cost of Goods Sold	4,000	
Rent Expense	900	
	<u>\$ 28,700</u>	<u>\$ 28,700</u>

The total debits must equal the total credits.

You can see an example of a Trial Balance—a listing of accounts with their balances.

Notice something: notice that it is very important that the total debits—in this case, \$28,700—are equal to (=) the total credits: \$28,700.

That tells us the Trial Balance is in balance and we can move forward with the Accounting Cycle.

Go to the next slide.

Slide 5

Chapter 3 Module 7: Trial Balance

Question: If a trial balance is in balance (i.e., debits = credits), does that mean no errors have been made?

Answer: No. A trial balance does not prove all transactions have been recorded or the ledger is correct.

And, let's talk about this question.

If a Trial Balance is in balance (i.e., the total debits equal (=) the total credits) like we just saw a second ago, does that mean that no errors have occurred? Does that mean that we have no problems at all?

The answer to that is: No.

A Trial Balance simply tells us if the debits and credits are equal (=). It does not guarantee that no errors have occurred.

There are lots of different types of errors that could occur that the Trial Balance won't pick up.

Let's look at a couple of those.

Move to the next slide with me.

Slide 6

Chapter 3 Module 7: Trial Balance

- Numerous errors may exist even though the trial balance columns agree. For example, the trial balance may balance even when:
 - incorrect accounts used in journalizing or posting

Recording the purchase of supplies for \$100 cash as:

Cash	100
Accounts Receivable	100

So we know that there are many errors that could exist that will not be detected by this Trial Balance.

For example: We could have an incorrect account being used when we are journalizing or posting.

For example: We could record the purchase of Supplies—which should be recorded with a debit to Supplies and a credit to Cash.

But, we could record it as we see here on the slide (Slide 6)—a debit to Cash and a credit to Accounts Receivable.

That is a mess up. We screwed up.

But, the debits and credits are still going to equal (=). The Trial Balance is still going to balance. But, we still have an error.

Go to the next slide.

Slide 7

Chapter 3 Module 7: Trial Balance

- Numerous errors may exist even though the trial balance columns agree. For example, the trial balance may balance even when:
 - incorrect accounts used in journalizing or posting
 - incorrect amounts used in journalizing or posting

Recording the purchase of supplies for \$100 cash as:

Supplies	10,000	
Cash		10,000

Another type of error that could exist that will still enable the Trial Balance to balance:

We could post incorrect amounts or put incorrect amounts in a Journal Entry.

For example: let's say we record the purchase of Supplies for \$100.00 cash.

Hey, we know the Journal Entry. We are not going to screw that up. Debit: Supplies; Credit: Cash.

But, we add a couple of extra zeroes. So, instead of putting it down for \$100.00; we record it as \$10,000.

Will the Trial Balance still balance?

Well, yeah, of course. Debits still equal (=) credits.

Is it right?

No! It is the wrong amount. We showed a purchase of \$10,000. It should have only been \$100.00.

Go to the next slide with me.

Slide 8

Chapter 3 Module 7: Trial Balance

- **Numerous errors may exist even though the trial balance columns agree. For example, the trial balance may balance even when:**
 - **incorrect accounts used in journalizing or posting**
 - **incorrect amounts used in journalizing or posting**
 - **a journal entry is not recorded**

Recording the purchase of supplies for \$100 cash as:

Another example of an error that could occur and would still allow the Trial Balance to be in balance:

We could just not bother to record a Journal Entry. We could just forget to make the Entry.

For example, we could record the purchase of Supplies for \$100.00 cash as nothing. There would be just blank paper there. No Entry was made.

So, the Trial Balance is still going to balance. The debits and credits are still equal (=).

But, we forgot to make an Entry! We have a problem.

The key idea for the Trial Balance is simply to check to make sure that your total dollar debits equal (=) your total dollar credits.

It does not guarantee no errors exist.

Go to the next slide with me.

Slide 9

<i>Chapter 3 Module 7: Trial Balance</i>		
PIONEER ADVERTISING AGENCY		
Trial Balance		
October 31, 2005		
	Debit	Credit
Cash	\$ 15,200	
Accounts Receivable	2,500	
Inventory	600	
Office Equipment	5,000	
Notes Payable		\$ 5,000
Accounts Payable		2,500
Common Stock		7,000
Retained Earnings		4,200
Dividends	500	
Sales Revenue		10,000
Cost of Goods Sold	4,000	
Rent Expense	900	
	<u>\$ 28,700</u>	<u>\$ 28,700</u>

There is our Trial Balance again.

I just want you to look at it.

It is a listing of accounts with their balances to ensure that debits equal (=) credits.

Now, remember what that looks like and go to the last slide.

Slide 10

Chapter 3 Module 7: Accounting Cycle

Accounting Cycle – Basic Steps:

- 1. Record transactions in the journal**
- 2. Post debit and credit amounts from the journal to the ledger**
- 3. Prepare a trial balance**
- 4. From the trial balance, prepare financial statements**

Let's list out our basic steps of the Accounting Cycle one more time—at least the steps that we have so far covered.

Step 1): Record transactions in the Journal with Journal Entries.

Step 2): Post the debits and credits from the Journal to the Ledger to figure out the Ending Balance in each account.

Step 3): Prepare the Trial Balance: the listing of accounts with their balances to check that debits and credits are equal (=).

Now, remember back to the Trial Balance—the listing of accounts:

What can you do using the Trial Balance with relative ease? What can we do that really won't be that difficult now? Something that we have already talked about.

We can use the Trial Balance to go ahead and prepare our financial statements.

We can use the accounts from the Trial Balance to go ahead and make Income Statements and Balance Sheets.

And, that is where we are going to go ahead and leave off.

When we come back, we will add to our Accounting Cycle.