Closing the Ledger or "closing the books," is done at the end of the accounting year for two reasons:

1.) To update the Capital account so that its balance agrees with the total owner's equity figure (as in the balance sheet and accounting equation) at the end of the accounting period

2.) To prepare the ledger so that the revenue and expense amounts for the next accounting period can be recorded without mixing them with amounts from the previous accounting period.

To Close the Ledger

- all revenue and expense accounts are cleared

  -because these accounts are closed at the end of the accounting period they are known as temporary accounts of the General Ledger.

- balance sheets accounts (except for the owner's Drawings) are not closed. Therefore all balance sheet accounts except Drawings are permanent accounts .

Temporary accounts: revenue, expense, R & E Summary and drawings accounts.

Permanent accounts: asset, liability and capital accounts

Revenue and Expense Summary: a temporary account used to transfer (clear) the net income (net loss) to the owner's capital account.

2 Very Useful Functions in the Accounting Cycle

(1) it simplifies the closing of the temporary revenue and expense accounts

(2) provides a convenient record of the net income (net loss) for the accounting period in the ledger

Closing the Ledger is the 7th Step in the Accounting Cycle

Can you name Steps 1 - 6

Give it a try.

1. Originating
2. Journalizing
3. Posting
4. Preparing a Trial Balance
5. Preparing a Worksheet
6. Preparing the Financial Statements
7. Closing the Ledger

GAAP's

- Matching Principle
- Revenue Principle
- Expense Principle
- Cost Principle
- Objectivity Principle

Two New Concepts

The going-concern concept states that all business will continue to exist and operate indefinitely unless an unforeseen event forces the business operation to cease.
... so business assets are reported at a $$ figure that can be identified and verified.

Going-concern concept: assumes that a business will continue to operate in order to meet planned objectives

Financial statements and the closing of the General Ledger must be done at regular intervals to measure and determine particular accounting information for decision making purposes and to meet government regulations - income tax filing.

The time period concept supports this need. The most common period is one year which is the basis for filing income tax.

All of the GAAP's and concepts build a framework for the practical application of accounting.

Time-period concept: assumes the need to divide the life of a business entity into convenient time periods.