

CONCEPT: RETAINED EARNINGS -- PRIOR PERIOD ADJUSTMENT

- GAAP requires an adjustment to the _____ balance of retained earnings in the following cases:
 - The discovery of an error from a previous period (i.e. an expense that was not taken in the previous year)
 - An unrecorded expense/loss from a previous period will _____ the retained earnings balance
 - An unrecorded revenue/gain from a previous period will _____ the retained earnings balance

The accountant at Overlook Corporation discovered a \$40,000 legal fee that was capitalized into the Prepaid Expenses account. However, the legal fees were related to a court case that was settled during the previous year.

Journal Entry:

- A change in accounting _____ used in record-keeping also requires a restatement of retained earnings
 - The most common example is a change in inventory methods (FIFO, Weighted-Average, LIFO)
 - In this course, you will not need to calculate the amount, it will be given

The Inventory Company has consistently used the weighted-average method to account for inventory and COGS. During the current year, the company decided to switch to the FIFO method. The cumulative effect of the change in accounting principle was a \$40,000 increase to Inventory.