

ADJUSTING ENTRIES (Tip Sheet)

Adjusting entries are done at the end of a period. All adjusting entries will affect either an **expense** account or a **revenue** account.

Adjusting entries are divided into five categories:

Prepaid Expenses	Accrued Revenues
Depreciation of Plant Assets	Unearned Revenue
Accrued Expenses	

Prepaid Expenses – advance payment of expenses. For example: Prepaid rent and supplies. Cash is paid in advance so these items are assets until they are used up. Once they are used up they are transferred from an asset to an expense. For example: At the beginning of the month you had \$100 in supplies, when you check your cabinet you now have only \$20 in supplies. You will need to adjust the asset called supplies and expense the supplies you have used.

Supplies Expense	80	
Supplies		80
(to record supplies expense)		

Depreciation of Plant Assets – all plant assets (except land) decline in usefulness as they age. Companies allocate plant asset costs to an expense over its useful life. This is called depreciation. If your depreciation for this year on equipment is \$500, you will need to journalize the depreciation.

Depreciation Expense	500	
Accumulated Depreciation (equipment)		500

Accumulated depreciation is a contra-asset account, which means an asset account with a normal credit balance. This account stays with the asset until the asset is disposed of.

Accrued Expenses – an expense that the business has incurred but not yet paid. The most common of these is payroll. Assume that the month ends on a Wednesday and you pay employees on Friday. This employee receives \$20 per day. Because the month ends on a Wednesday you will need to expense 3 days of payroll to be paid on Friday.

Salary Expense	60	
Salary Payable		60

On Friday the following transaction will take place when the payroll is paid:

Salary Expense	40	
Salary Payable	60	
Cash		100

Accrued Revenues – revenue that has been earned but not yet collected in cash. In many cases a company will perform half of a job during one period and the other half during the next period, but will not get paid until the job is complete. Let's assume that you have a job that, when completed, will pay \$1000. At the end of the month you have completed 80% of the job, this revenue must be recorded in the month earned.

Account Receivable	800	
Service Revenue		800

When the job is complete and the cash is received the following will take place.

Cash	1000	
Account Receivable		800
Service Revenue		200

Unearned Revenue – a liability created when a business collects cash from customers before actually doing the work. Let's say that Joe Smith paid you \$500 to paint his house. At the end of the month you have painted 40% of the house. You must record that you have earned this revenue in the month it was earned.

When you received the payment you recorded the following:

Cash	500	
Unearned Revenue (liability)		500

Adjusting Entry:

Unearned Revenue	200	
Service Revenue		200

Once the job is complete:

Unearned Revenue	300	
Service Revenue		300