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**Assignment:- accounting**

**Topic:- Adjusting entries**

**(Adjusting Entries)**

Adjusting entries are changes to journal entries you’ve already recorded. They make sure that the numbers you have recorded match up to the correct accounting periods.

Journal entries track how money moves—how it enters your business, leaves it, and moves between different accounts.

Here’s an example of an adjusting entry: In August, you bill a customer $5,000 for services you performed. They pay you in September.

In August, you record that money in accounts receivable—as income you’re expecting to receive. Then, in September, you record the money as cash deposited in your bank account.

To make an adjusting entry, you don’t literally go back and change a journal entry—there’s no eraser or delete key involved. Instead, you make a new entry amending the old one.

For example, going back to the example above, say your customer called after getting the bill and asked for a 5% discount. If you granted the discount, you could post an adjusting journal entry to reduce accounts receivable and revenue by $250 (5% of $5,000).

Making adjusting entries is a way to stick to the matching principle—a principle in accounting that says expenses should be recorded in the same accounting period as revenue related to that expense.

In the accounting cycle, adjusting entries are made prior to preparing a trial balance and generating financial statements.

**Why make adjusting entries**

When you make an adjusting entry, you’re making sure the activities of your business are recorded accurately in time. If you don’t make adjusting entries, your books will show you paying for expenses before they’re actually incurred, or collecting unearned revenue before you can actually use the money.

So, your income and expenses won’t match up, and you won’t be able to accurately track revenue. Your financial statements will be inaccurate—which is bad news, since you need financial statements to make informed business decisions and accurately file taxes.

One more thing: Adjusting journal entries are essential for depreciating assets. Which is important for reporting tax deductions and balancing your books.

**Who needs to make adjusting entries?**

If you do your own accounting, and you use the accrual system of accounting, you’ll need to make your own adjusting entries.

If you do your own accounting and you use the cash basis system, you likely won’t need to make adjusting entries.

No matter what type of accounting you use, if you have a bookkeeper, they’ll handle any and all adjusting entries for you.

Spreadsheets vs. accounting software vs. bookkeepers

Adjusting entries will play different roles in your life depending on which type of bookkeeping system you have in place.

If you do your own bookkeeping using spreadsheets, it’s up to you to handle all the adjusting entries for your books. Then, you’ll need to refer to those adjusting entries while generating your financial statements—or else keep extensive notes, so your accountant knows what’s going on when they generate statements for you.

If you use accounting software, you’ll also need to make your own adjusting entries. The software streamlines the process a bit, compared to using spreadsheets. And it will likely generate financial statements for you. But you’re still 100% on the line for making sure those adjusting entries are accurate and completed on time.

If you have a bookkeeper, you don’t need to worry about making your own adjusting entries, or referring to them while preparing financial statements. They’ll do both for you.

If you don’t have a bookkeeper yet, check out Bench—we’ll pair you with a dedicated bookkeeping team, and give you access to simple software to track your finances.

**1. Accrued revenues**

Under the accrual method of accounting, a business is to report all of the revenues (and related receivables) that it has earned during an accounting period. A business may have earned fees from having provided services to clients, but the accounting records do not yet contain the revenues or the receivables. If that is the case, an accrual-type adjusting entry must be made in order for the financial statements to report the revenues and the related receivables.

If a business has earned $5,000 of revenues, but they are not recorded as of the end of the accounting period, the accrual-type adjusting entry will be as follows:

61X-journal-06

**2. Accrued expenses**

Under the accrual method of accounting, the financial statements of a business must report all of the expenses (and related payables) that it has incurred during an accounting period. For example, a business needs to report an expense that has occurred even if a supplier's invoice has not yet been received.

To illustrate, let's assume that a company utilized a worker from a temporary personnel agency on December 27. The company expects to receive an invoice on January 2 and remit payment on January 9. Since the expense and the payable occurred in December, the company needs to accrue the expense and liability as of December 31 with the following adjusting entry:

61X-journal-07

**3. Deferred revenues**

Under the accrual method of accounting, the amounts received in advance of being earned must be deferred to a liability account until they are earned.

Let's assume that Servco Company receives $4,000 on December 10 for services it will provide at a later date. Prior to issuing its December financial statements, Servco must determine how much of the $4,000 has been earned as of December 31. The reason is that only the amount that has been earned can be included in December's revenues. The amount that is not earned as of December 31 must be reported as a liability on the December 31 balance sheet.

If $3,000 has been earned, the Service Revenues account must include $3,000. The remaining $1,000 that has not been earned will be deferred to the following accounting period. The deferral will be evidenced by a credit of $1,000 in a liability account such as Deferred Revenues or Unearned Revenues.

The adjusting entry for this deferral depends on how the receipt of $4,000 was recorded on December 10. If the receipt of $4,000 was recorded with a credit to Service Revenues (and a debit to Cash), the December 31 adjusting entry will be:

61X-journal-08

If the entire receipt of $4,000 had been credited to Deferred Revenues on December 10 (along with a debit to Cash), the adjusting entry on December 31 would be:

61X-journal-09

**4. Deferred expenses**

Under the accrual method of accounting, any payments for future expenses must be deferred to an asset account until the expenses are used up or have expired.

To illustrate, let's assume that a new company pays $6,000 on December 27 for the insurance on its vehicles for the six-month period beginning January 1. For December 27 through 31, the company should have an asset Prepaid Insurance or Prepaid Expenses of $6,000.

In each of the months January through June, the company must reduce the asset account by recording the following adjusting entry:

61X-journal-10

**5. Depreciation expense**

Depreciation is associated with fixed assets (or plant assets) that are used in the business. Examples of fixed assets are buildings, machinery, equipment, vehicles, furniture, and other constructed assets used in a business and having a useful life of more than one year. (However, land is not depreciated.)

Depreciation allocates the asset's cost (minus any expected salvage value) to expense in the accounting periods in which the asset is used. Hence, office equipment with a useful life of 5 years and no salvage value will mean monthly depreciation expense of 1/60 of the equipment's cost. A building with a useful life of 25 years and no salvage value will result in a monthly depreciation expense of 1/300 of the building's cost.