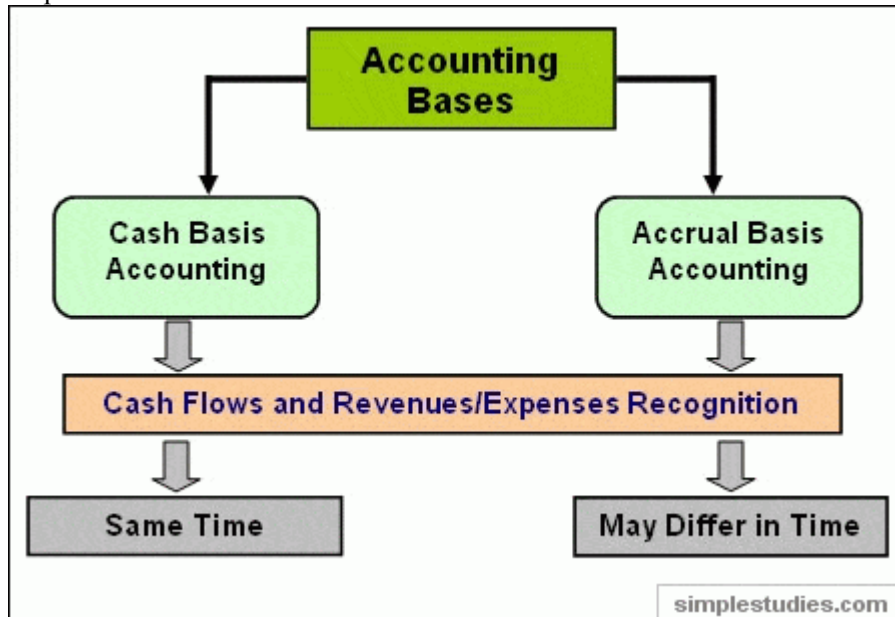


Financial Accounting-The Adjusting Process

Let's start with the terms **cash basis** and **accrual basis**. Accounting is done using either one of these methods. When we record everything that we *pay and receive* right away to our income and expenses- we are employing the **cash basis** of accounting. Think about it though. We may get paid for something BEFORE we actually earned it. Or we might not be paid in time and have already provided a service. To account for these nuances, we would be using the **accrual basis** of accounting. It is a more accurate picture of how we are doing and is used by most mid-size to large companies.

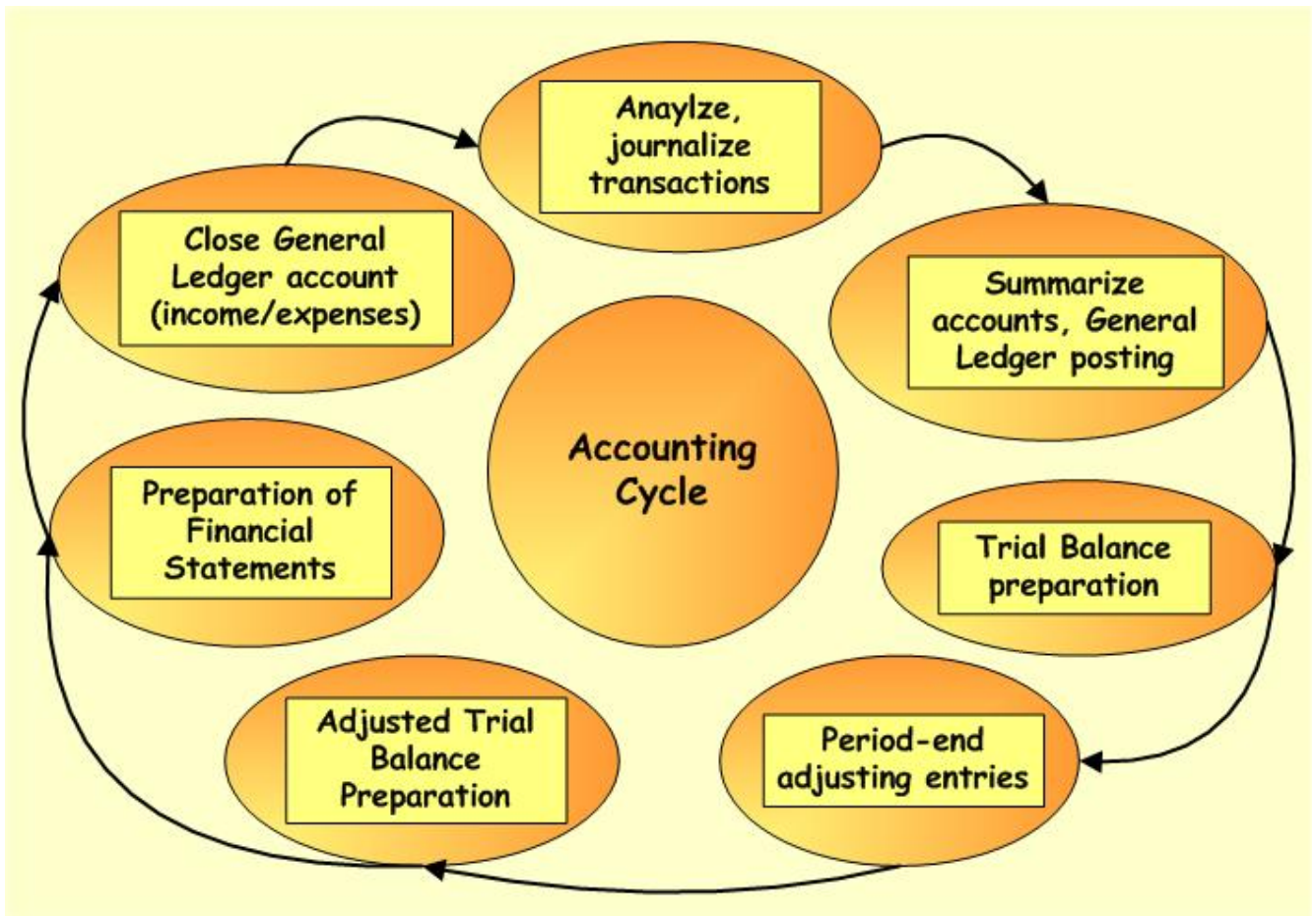


****Video Alert****

Also, here is a really cool video that I found for you! Just copy/paste the link into your browser. It covers the difference between the cash and accrual basis of accounting!

http://www.youtube.com/watch?v=3RxJFyUPu_o

There is the next question of WHEN do we record these entries.



Now we are ready to hear about **Adjusting Entries**. Each month after the accountants (you) finish the month's activities, there are some additional entries that are necessary to close the books. These items can vary from company to company. However, they are usually items such as:

- Prepaid Expenses
- Depreciation
- Accrued Expenses
- Accrued Income
- Unearned Revenue

The reason these items need to be adjusted manually at the end of the month is because we are fine-tuning the books to be as accurate as possible. Let's say we paid our rent in advance and it is the end of the month. We may have paid \$3,000.00 in December for January's rent expense. We should adjust the books so that we don't have such a large expense in December that really benefits us in January (January's rent). So that is one entry we would make. There are various others that we make monthly. In my office, we keep a checklist for adjusting entries that MAY be needed each month. We look at that to ensure we aren't leaving any out as we close the books. It really helps!

****Video Alert**** (bonus! There are two!)

The following videos covers adjusting entries:

<http://www.youtube.com/watch?v=flf2sWTuWLU>

<http://www.youtube.com/watch?v=C2dccEZaaF4&feature=relmfu>

After the books are closed, we begin preparing financial statements. These include (in order that they are completed):

- Income Statement
- Statement of Equity
- Balance Sheet

Accounting takes a lot of time to study. Remember this is a new language- the language of BUSINESS. And we want to master it!

Enjoy your week!

Debra Touhey, MSA, CFE

Reference

Horngren, C.T., Harrison, W.T. Jr. & Oliver, S. M. (2012). Accounting (9th edition). New Jersey: Prentice Hall.