

Adjusting Entries

Why do we prepare adjusting entries?

- If we do not, our Financial Statements will be incorrect.

What are the different categories and types of adjusting entries?

1) Prepaid and Unearned Items

a) **Prepaid Expenses (Assets)** - Certain expenses that were paid for in advance.

Examples: Prepaid Rent, Prepaid Insurance, Supplies

General Rule:

Dr: _____ Expense
Cr: Prepaid Asset

Used or Expired

b) **Unearned Revenues** - The business received payment for the service/goods but have not provided the service/goods as of yet.

Account affected - "Unearned".....

General Rule:

Dr: Unearned Revenue Account
Cr: Revenue Account

Earned

2) Accrued Items

a) **Accrued Expenses** - Expenses that have been incurred but unrecorded.

General Rule:

Dr: _____ Expense
Cr: _____ Payable

Incurred (Taken place)

b) **Accrued Revenues** - These are revenues that have been earned and they are unrecorded.

General Rule:

Dr: _____ Receivable
Cr: Revenue Account

Earned

3) Estimated Items

a) Depreciation

General Rule:

Dr: **Depreciation Expense** - "Asset's Name"
Cr: **Accumulated Depreciation** - "Asset's Name"

Given

b) **Bad Debts** - This will be covered in Chapter 9

Multi-Step Income Statement

Sections:

Random Example

1) <u>Sales (Net Sales)</u>		
Sales Revenue		
Less: Sales Returns and Allowances		
Sales Discounts		
Net Sales		420,000
2) <u>Cost of Goods Sold</u>		
Merchandise Inventory, Beginning		50,000
Purchases	120,000	
Less: Purchases Returns and Allowances	(12,000)	
Purchases Discounts	<u>(5,000)</u>	
Net Purchases	103,000	
Add: Freight-In	<u>7,000</u>	
Cost of Goods Purchased		<u>110,000</u>
Cost of Goods Available for sale		160,000
Less: Inventory, Ending		<u>(43,000)</u>
Cost of Goods Sold		<u>117,000</u>
Gross Profit		303,000
3) Operating Expenses		
List all of your Operating Expenses		<u>(103,000)</u>
Income from Operations		200,000
Other Revenues and Gains		4,000
	Non-Operating Items	
Other Expenses and Losses		(3,000)
Net Income		201,000

Statement of Owners' Equity

Capital, Beginning

Add:

Investment made by the Owner

Net Income

Subtotal

Less:

Owners' Drawings

Net Loss

Capital, Ending

Classified Balance Sheet:

Assets

Current Assets - Listed according to Liquidity

Long-Term Investments

Property, Plant, and Equipment

Intangible Assets

Liabilities

Current Liabilities

Long-Term Liabilities

Owners' Equity

Owners' Capital (Usually from the Statement of Owners' Equity)

4 Closing Entries

- 1) Closed all Income Statement accounts with credit balances into the Income Summary Account
Dr: Income Statement Accounts with Credit Balances
Cr: Income Summary
- 2) Closed all Income Statement accounts with Debit balances into the Income Summary Account
Dr: Income Summary
Cr: Income Statement Accounts with Debit Balances
- 3) Closed the Income Summary Account into the Owners' Capital
 - a) If Income Summary has a Debit balance, the entry is:
Dr: Owners' Capital
Cr: Income Summary
 - OR**
 - b) If Income Summary has a Credit balance, the entry is:
Dr: Income Summary
Cr: Owners' Capital
- 4) Closed the Owners' Drawings Account into the Owners' Capital
Dr: Owners' Capital
Cr: Owners' Drawings