

ACCOUNTING FOR ACCRUALS AND DEFERRALS

LAVERNE FUNDERBURK, CPA

UIL ACCOUNTING STATE CONTEST DIRECTOR





BEFORE WE GET STARTED...



Everyone should
remain muted



Submit
questions
through chat



Attendance for
CPE credit

ACCOUNTING FOR ACCRUALS AND DEFERRALS

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FIRST LET'S REVIEW

Basis of Accounting

Revenue Recognition

Matching Principle

Accounting Period Cycle

Basis of Accounting

CASH BASIS—an accounting system that records revenue when cash is received and records expenses in the period the cash is paid.

ACCRUAL BASIS—an accounting system that records revenue when it is earned regardless of when the cash is received **AND** records expenses when they are incurred regardless of when cash is paid out.

Revenue Recognition

The GAAP principle that revenue is RECORDED on the date it is earned, even if the cash has not yet been received.

Matching Principle

Revenue and the expenses associated with earning that revenue are recorded in the SAME accounting period.

Accounting Period Cycle



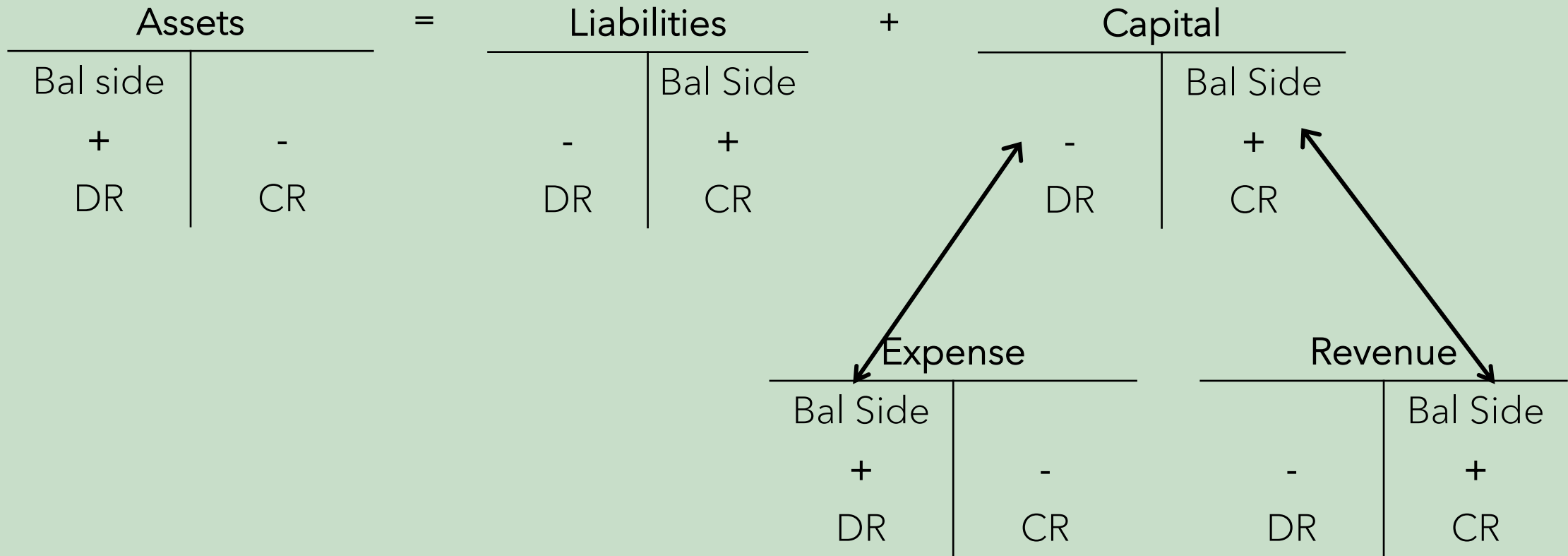
Financial Statements
are prepared
for a
specific period
of time.

Accounting Equation:
$$\text{Assets} = \text{Liabilities} + \text{Capital}$$

Increases to Capital
Owner Investments
Revenue

Decreases to Capital
Owner Withdrawals
Expenses

Relationship Between Balance Sheet and Income Statement



Adjusting Journal Entries (AJEs)

- Before financial statements are prepared, the accountant must examine the general ledger accounts to make sure they are up-to-date.
- The accountant may need to examine insurance policies or take a physical inventory of supplies, etc.
- The accounting Work Sheet is an extremely helpful tool.
- There are two kinds of accruals.
- There are two kinds of deferrals.
- Creating adjusting journal entries NEVER affects the Cash account.
- An adjusting entry will always affect a Balance Sheet account and an Income Statement account.



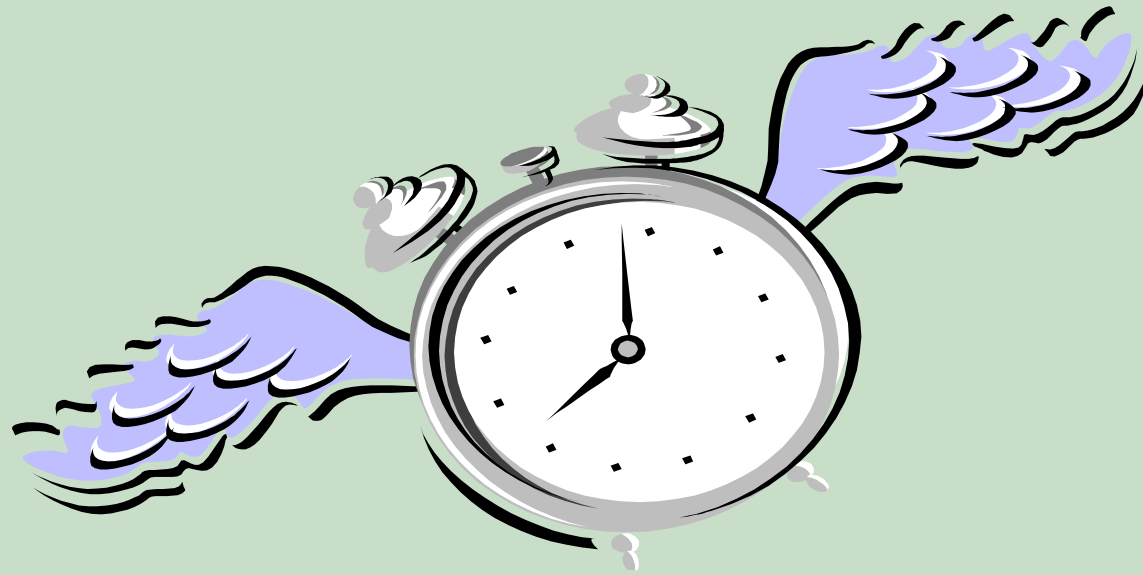
Accrual Basis Financial Statements

Focus on the EVENTS and NOT on Cash

Did we EARN revenue in this fiscal period?

Did we INCUR expense in this fiscal period that needs to match to our revenue of this period?

Timing Is Everything: Accruals



Timing Is Everything (Accruals)

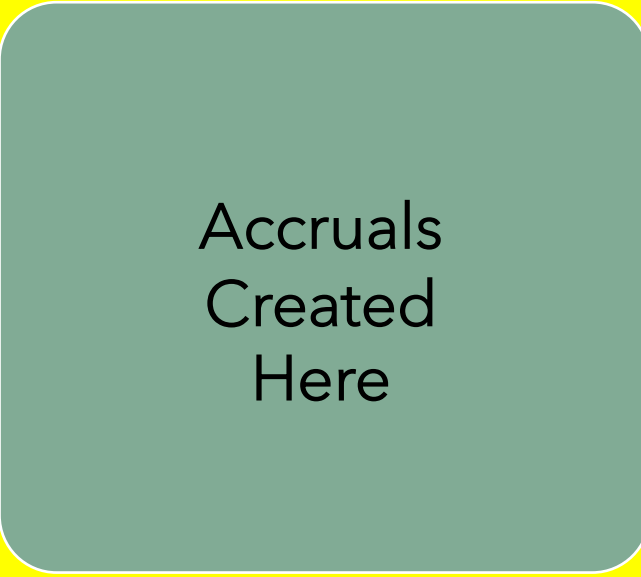
Past



Now

AJE's Prior to Financial
Statements

Accruals
Created
Here



Future

Cash
Action
Here



Accrued Revenue

Now

AJE's Prior to Financial Statements

A/Rec.....DR
Fees Earned.....CR

Accrued Revenue

Future

Cash Action

Cash.....DR
A/Rec.....CR

Relationship for Accrued Revenue: Balance Sheet & Income Statement

Now
AJE's Prior to Financial Statements

A/Rec.....DR
Fees Earned.....CR

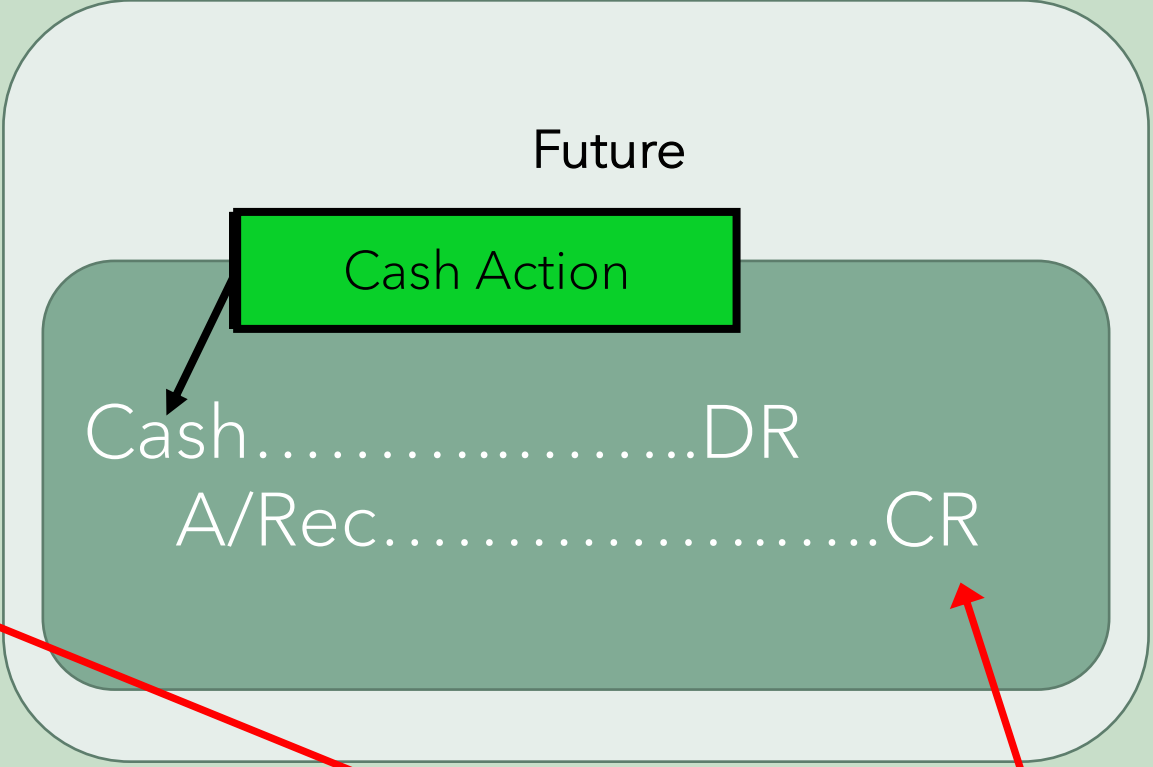
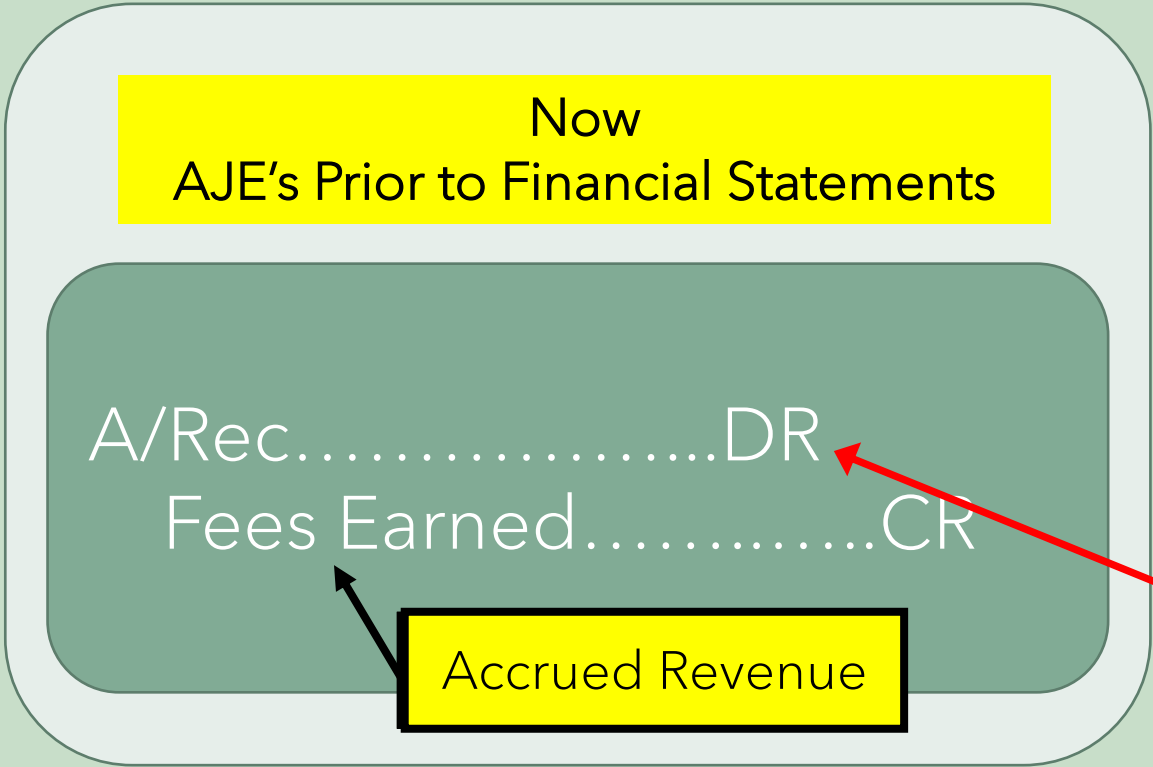
Accrued Revenue

Assets	
Bal side	
+	-
DR	CR



Revenue	
	Bal Side
-	+
DR	CR

Accrued Revenue: Asset & Revenue



Notice that when the accrual is created, the Buddy Asset is INCREASED.
When Cash Action takes place in the future, the Buddy Asset (A/Rec) is DECREASED.

Accrued Revenue's Future Cash Action Disposes of It's Buddy

Now

AJE's Prior to Financial Statements

A/Rec.....	DR
Fees Earned.....	CR

Future

Cash.....	DR
A/Rec.....	CR





Are We All Clear about
Accrued Revenue?

Accrued Expense

Now
AJE's Prior to Financial Statements

Accrued Expense

Gasoline Expense....DR
Accounts Payable.....CR

Future

Accounts Payable....DR
Cash.....CR

Cash Action

Relationships for Accrued Expense: Balance Sheet & Income Statement

Now
AJE's Prior to Financial Statements

Accrued Expense

Gasoline Expense....DR
Accounts Payable.....CR

Liabilities

	Bal Side
-	+
DR	CR

Expense

Bal Side	
+	-
DR	CR

Accrued
Expense's
Buddy is a
Liability

Accrued Expense

Now

AJE's Prior to Financial Statements

Accrued Expense

Gasoline Expense.....DR
Accounts Payable.....CR

Future

Cash.....DR
Accounts Payable.....CR

Cash Action

Notice that when the accrual is created, the Buddy Liability is INCREASED.
When Cash Action takes place in the future, the Buddy Liability is DECREASED.

Accrued Expense's Future Cash Action Disposes of Its Buddy

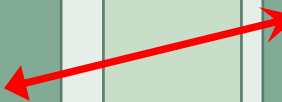
Now

AJE's Prior to Financial Statements

Gasoline Expense....DR
Accounts Payable.....CR

Future

Accounts Payable.....DR
Cash.....CR



Accruals: Recap & Compare

Now

AJE's Prior to Financial Statements

Accrued Revenue

A/Rec.....DR
Fees Earned.....CR

Accrued Expense

Gasoline Expense...DR
Accounts Payable.....CR

Future

Future Cash Action

Cash.....DR
A/Rec.....CR

Future Cash Action

Accounts Payable....DR
Cash.....CR



Are We All Clear about
Accrued Expense?

Sample Theory Questions over Accruals 2019 State, Group 4

Match each situation with the best term using the following code:

	Terms		
A	Accrued Revenue	C	Deferred Expense
B	Accrued Expense	D	Deferred Revenue

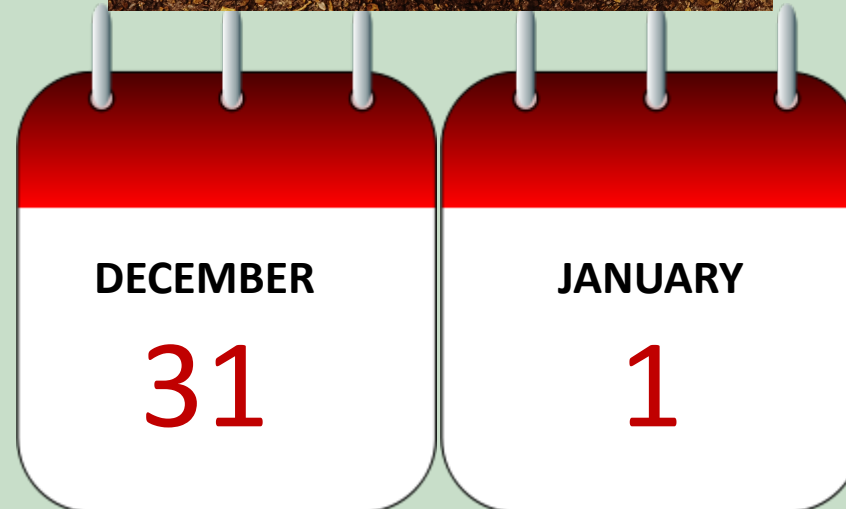
21. Owes property taxes assessed; but has not yet recorded or paid the taxes. **B**

24. Rent not yet collected; already earned but not yet recorded. **A**

25. An expense is incurred; not yet paid or recorded. **B**

26. A revenue is earned; not yet recorded or collected. **A**

Timing Is Everything: Deferrals



Deferrals

The definition of “defer” as we use it in Accounting, is to postpone or put off.

With a deferral, the Cash Action takes place FIRST!

We defer an expense when we have PAID CASH for it, but we have not yet USED or CONSUMED it to earn revenue. This is a Prepaid Expense.

We defer a revenue when we have RECEIVED CASH for it, but we have not yet EARNED it. This is an Unearned Revenue.

Cash Action Happens FIRST

Past

Cash
Action
Here

Now

AJE's Prior to Financial
Statements

Adjust
Deferral
Here

Future

Prepaid Expense: Supplies

Past

Deferred Expense
Created

Supplies.....DR
Cash.....CR

Now

AJE's Prior to Financial Statements

EXPIRED Cost

Supplies Expense....DR
Supplies.....CR

AJE to Adjust the
Deferral



Prepaid Expense: Insurance

Past

Deferred Expense Created

Prepaid Insurance...DR
Cash.....CR

Now
AJE's Prior to Financial Statements

EXIRED Cost

Insurance Expense....DR
Prepaid Insurance.....CR

AJE to Adjust the Deferral



Think About Assets in a New Way

Why does a business want the Cash account to grow?

- ❖ To use in current operations (buy things that help us earn revenue)
- ❖ To expand operations
- ❖ So the owner can have cash for personal use

Why is Accounts Receivable on the Balance Sheet?

- ❖ The business is waiting for it to turn into Cash

Why do we need Deferred Expenses?

- ❖ To be used in the future to help the business earn revenue

Why are Deferred Expenses on the Balance Sheet?

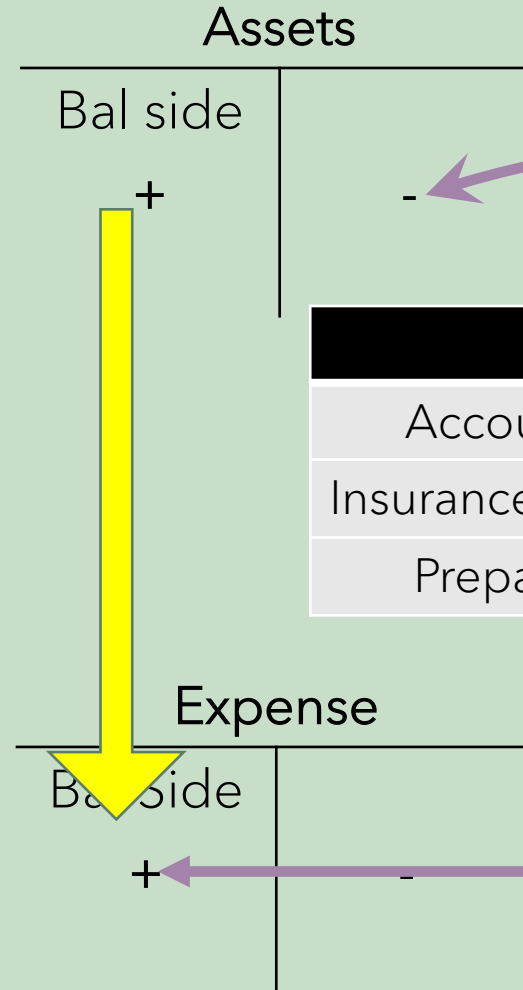
- ❖ They are sitting on the Balance Sheet WAITING to grow up to become an expense

Adjusting Entry for a Deferred Expense

Prepaid Expense

Asset
(Unexpired Cost)

Expense
(Expired Cost)



Adjusting Journal Entry

Account Name	Debit	Credit
Insurance Expense	100	
Prepaid Insurance		100



Are We All Clear about
Deferred Expense?

Timing Is Everything: (Deferred Revenue)

Past

Cash
Action
Here

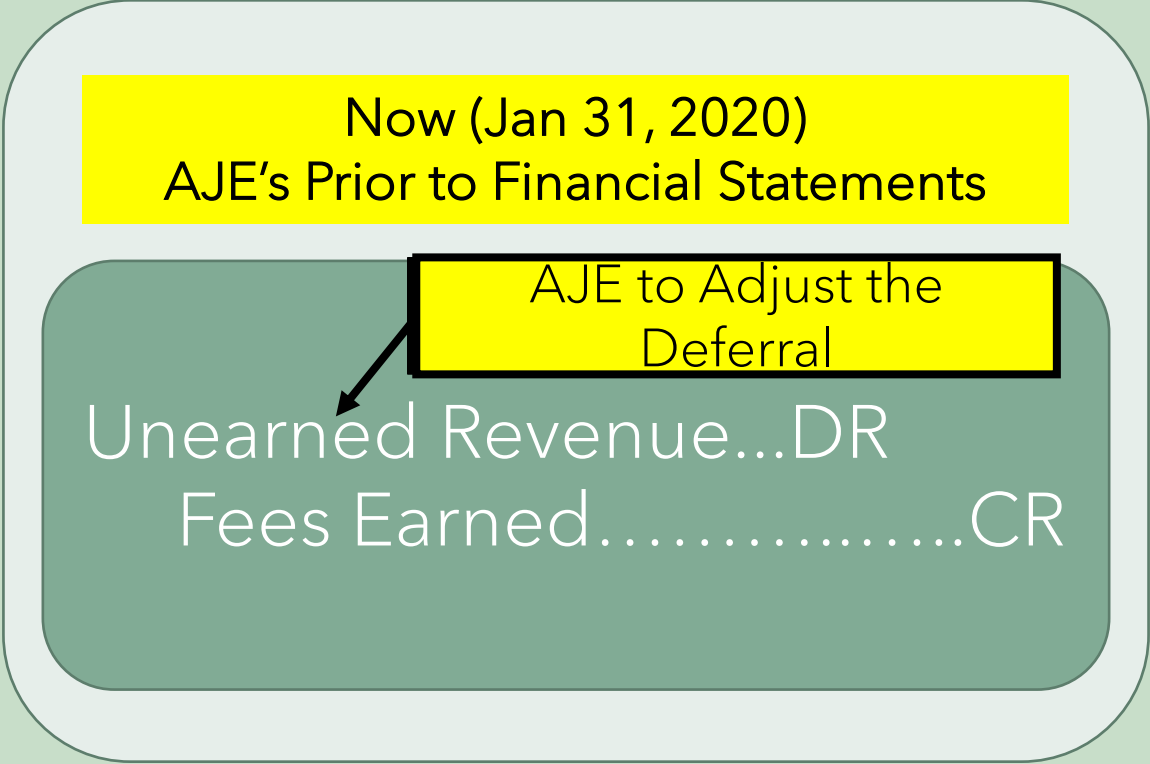
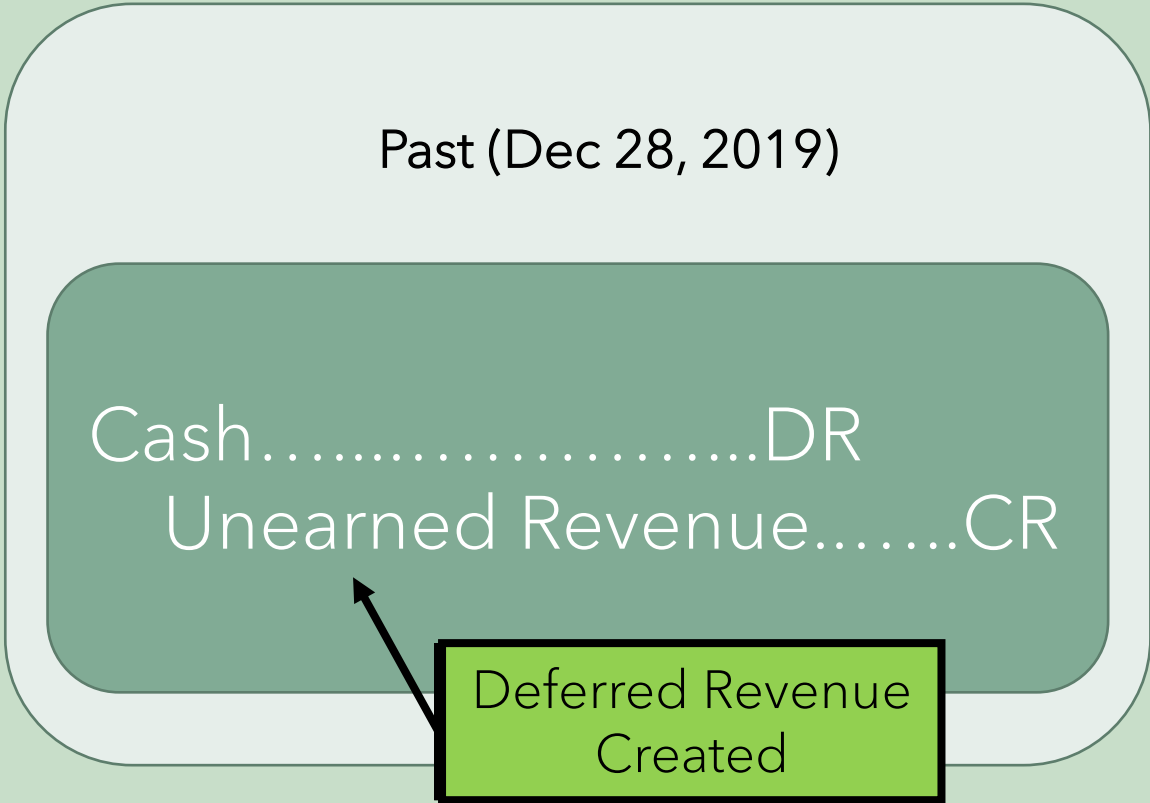
Now

AJE's Prior to Financial
Statements

Adjust
Deferral
Here

Future

Deferred Revenue



A Deferred Revenue SITS on the Balance Sheet as a Liability
WAITING to grow up to be a Revenue.

Adjusting Entry for a Deferred Revenue

Deferred Revenue

Liability
(Unearned Revenue)

Revenue
(Earned)

Liability

Bal Side
- +

Account Name	Debit	Credit
Unearned Revenue	1,000	
Fees Earned		1,000

Fees Earned

Bal Side
- +

Review of Account Relationships When Accruals are Created and When Deferrals Are ADJUSTED

***Write the two types of
accounts in relationship
for each item at the left***

Accrued Revenue	Asset	Revenue
Accrued Expense	Expense	Liability
Deferred Revenue	Liability	Revenue
Deferred Expense	Expense	Asset

Affect on Financial Statements When We Fail to Make Adjusting Entries for Accruals & Deferrals

Type of Adjusting Entry	Balance Sheet	Income Statement
Accrued Revenue	Assets Understated	Revenue Understated
Accrued Expense	Liabilities Understated	Expense Understated
Deferred Revenue	Liabilities Overstated	Revenue Understated
Deferred Expense	Assets Overstated	Expense Understated

Account Titles for Accruals & Deferrals

- ❖ Naming accounts is up to the individual accountant or the company policy.
- ❖ May depend on if Reversing Entries are used or not used.
- ❖ Accrued Expense
 - ❖ Accrued Salary Expense (or Salary Expense)
 - ❖ Accrued Salary Payable (or Salary Payable)
- ❖ Accrued Revenue
 - ❖ Accrued Interest Receivable (or Interest Receivable)
 - ❖ Accrued Interest Payable (or Interest Payable)

Reversing Entries

- ❖ Reversing Entries are Optional.
- ❖ A Reversing Entry is the EXACT OPPOSITE of a specific ADJUSTING Entry.
- ❖ One of our high school texts suggests to record a reversing entry whenever an adjusting entry creates a balance in an asset or a liability account that initially had a zero balance.
- ❖ Reversing Entries are made on the FIRST day of the new accounting period.
- ❖ Reversing Entries simplify the recordkeeping in the new period.
- ❖ Reversing Entries (for our textbooks) are not used on Deferrals.



Are We All Clear about
Deferred Revenue?



Sample Theory Questions over Accruals & Deferrals

2019 State, Group 4

Match each situation with the best term using the following code:

Terms			
A	Accrued Revenue	C	Deferred Expense
B	Accrued Expense	D	Deferred Revenue

20. An expense not yet incurred; paid in advance.
21. Owes property taxes assessed; but has not yet recorded or paid the taxes.
22. A revenue not yet earned; collected in advance.
23. Office supplies on hand and paid for; will be used next accounting period.
24. Rent not yet collected; already earned but not yet recorded.
25. An expense is incurred; not yet paid or recorded.
26. A revenue is earned; not yet recorded or collected.

20	21	22	23	24	25	26
C	B	D	C	A	B	A

Sample Theory Questions

2018 State, Group 2

A Asset

B Liability

C Capital

D Revenue

E Expense

	Debit	Credit
1. When a deferred expense is purchased	Supplies	Cash
2. When a revenue has been earned but not yet received	A/Receivable	Fees Earned
3. When an expense has been incurred but not yet paid	Expense	A/Payable
4. When a previously deferred expense has now been used	Expense	Supplies
5. When a previously unearned revenue has now been earned	Unearned Rev.	Fees Earned
6. When an unearned revenue is received	Cash	Unearned Rev.

Sample Theory Questions over Accruals & Deferrals

2009 State, Group 4

Assume fiscal year end is Dec 31. Match each situation with the best term using the following code:

A Prepaid Expense

B Unearned Revenue

C Accrued Expense

D Accrued Revenue

19. A company's employees worked Dec 29 and Dec 30 and will receive holiday pay for Dec 31, but the company will not issue the paycheck until Jan 5.
20. Cash received by a ballpark in January for season tickets to all home baseball games to be played in the summer.
21. A two-year premium paid on Dec 30 on an insurance policy.
22. Interest on an interest-bearing note receivable for the last 15 days of December when that note matures on February 14

19

C

20

B

21

A

22

D

Any
Questions

SOME of the Various THEORY Formats Found on
Prior Year UIL Exams on the topic of
Accruals and Deferrals

2019 State, Group 4

2018 State, Group 2

2015 State, Group 2

2011 State, Group 1

For Problems that APPLY Theory:
Every Work Sheet Problem
Includes Accruals and Deferrals

To All UIL Accounting Coaches:

If you would like to be added to the
UIL Accounting State Contest Director's Coaches Contacts,
please email LaVerne Funderburk

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UIL Accounting Website:
www.funderburkcpa.com/UIL

the MORE
YOU PRACTICE
THE PRACTICE
BETTER
YOU GET

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Thank you for watching
this presentation!

Accountants, Stay Balanced!