

**Penang Sangam High School**

**Accounting-Year 11**

**Lesson Notes- Week 7**

**Strand 4: Measuring Periodic Income 1**

**Sub-strand: Balance Day Adjustments**

**( Copy in your note book)**

**Learning outcome:** Examine balance day adjustments and account for them in the financial records of the business.

Balance day adjustments are adjustments that need to be made on some accounts at the end of the financial year, so that they accurately reflect the performance of the business.

These are only required when a company is using an accrual accounting system, as income or expenses may be recognized and paid or received at different times.

**Purpose of Balance Day Adjustments**

- Is to match costs against related income and also to up – date the accounts at the end of the financial period.

**Cash Basis Accounting**

- Means that revenues and expenses are not recognized until the cash is received or paid.

**Accrual Basis Accounting**

- Means that revenue is recognized when earned and expenses when incurred, irrespective of whether they are cash or credit transaction.
- It takes into account all the revenues and expenses during the period to measure profit and loss.
- Accrual basis is better than cash basis because revenue is matched against expenses incurred in earning them.

**Prepayments**

They represent expenses which are paid during the year but relates to next accounting period. They are also termed as Unexpired Cost, Expenses paid in advance or Prepaid Expenses.

### **Rules for posting**

<b>Date</b>	<b>Particulars</b>	<b>Debit \$</b>	<b>Credit \$</b>
	Prepaid expenses Related expense account	xxx	xxx

- ❖ Deduct the amount of prepayment from the related expense figure on the debit side of profit and loss account/Statement of Financial Performance.
- ❖ Record the amount of prepayment under current assets in the balance sheet.

### **e.g. 1                      Trial Balance (extract)**

	<b>\$</b>		<b>\$</b>
Insurance	550		

### **Additional Information**

1. Insurance paid in advance/ unexpired \$100.

### **Solution:**

#### **General Journal Entry**

<b>Date</b>	<b>Particulars</b>	<b>Debit \$</b>	<b>Credit \$</b>
	Insurance prepaid	100	
	Insurance (to record insurance prepaid)		100

#### **Profit and loss extract**

	<b>\$</b>		<b>\$</b>
Insurance (550 - 100)	450		

#### **Balance sheet extract**

	<b>\$</b>		<b>\$</b>
<u>Current Assets</u> Insurance prepaid	100		