What is the Expense Recognition Principle?

Worksheet

The expense recognition (matching) principle states that expenses must be recognized in the period in which the related revenue is earned, regardless of when cash changes hands.

Questions

1. A company earns $50,000 in revenue in December but pays the related $8,000 supplier cost in January. Under the matching principle, when is the $8,000 expense recognized?

A) January, when cash is paid
B) December, with the related revenue
C) Split evenly between both months
D) Whenever the company chooses

2. The expense recognition principle is also known as the:

A) Revenue recognition principle
B) Matching principle
C) Going concern principle
D) Cost principle

3. Which accounting method is required to properly apply the expense recognition principle?

A) Cash basis
B) Accrual basis
C) Tax basis
D) Modified cash basis

4. A $24,000 piece of equipment with a 4-year useful life is used evenly to generate revenue. How much expense should be recognized each year under the matching principle?

A) $24,000
B) $12,000
C) $6,000
D) $2,000

5. A company pays a $12,000 annual insurance premium upfront in January. How much expense should it recognize in March under the matching principle?

6. A retailer pays sales commissions of $4,500 in the month after a $90,000 sale is made. When should the commission expense be recognized?

7. A machine costing $60,000 is expected to be used for 5 years with no salvage value. How much depreciation expense should be recognized each year?

8. Define: What is the expense recognition principle?

9. Define: Another name for this principle?

10. Define: Which accounting basis uses it?

Answer Key

1. B) December, with the related revenue - The matching principle recognizes expenses in the same period as the revenue they helped generate - December.

2. B) Matching principle - It is commonly called the matching principle.

3. B) Accrual basis - Accrual accounting records transactions when they occur, enabling proper matching.

4. C) $6,000 - 24,000 / 4 = $6,000 per year, matched to the revenue each year the equipment helps generate.

5. Total premium = $12,000 covers 12 months Monthly expense = 12,000 / 12 = $1,000 March recognizes $1,000, not the full $12,000 paid in January

6. The $90,000 revenue is recognized when the sale occurs (Month 1) Matching principle requires the related $4,500 commission to also be recognized in Month 1 Even though cash is paid in Month 2, the expense is recorded in Month 1 via an accrued liability

7. Total cost to allocate = $60,000 Useful life = 5 years Annual depreciation = 60,000 / 5 = $12,000 per year, matched against the revenue the machine helps produce

8. It requires expenses to be recorded in the same period as the revenue they help generate, not when cash is paid.

9. The matching principle.

10. Accrual-basis accounting (required under GAAP and IFRS).