



Cash vs. Accrual Accounting

Cash-basis accounting is the recognition of accounting transactions when cash is either received or paid out. Cash basis is most appropriate for small, stable associations with relatively few transactions. The drawbacks to cash accounting include the following:

- ✦ Limited accounting information
- ✦ A shortened and limited-use balance sheet
- ✦ An inability to highlight a weakened financial position

Accrual accounting is the recognition of accounting transactions when they actually take place. Revenue is recognized when earned and expenses are recognized when incurred, not necessarily when cash is received or when cash is paid out. Where cash accounting is weak, accrual accounting is strong. Accrual accounting provides:

- ✦ More detailed and in-depth accounting information
- ✦ A detailed balance sheet
- ✦ The ability to highlight a weakened financial position

The following is a list of major accrual accounts:

- ✦ Assessments receivable
- ✦ Other accounts receivable
- ✦ Prepaid insurance
- ✦ Mortgages and notes payable
- ✦ Accounts payable
- ✦ Accrued expenses
- ✦ Prepaid assessments

Community associations rarely use a full accrual system. Modified-accrual systems are implemented more frequently. Only the major balance sheet accounts, such as assessments receivable and accounts payable, are established under the modified-accrual system. Expenses, such as prepaid insurance and all minor payables and accrued expenses are not set up. A modified-accrual system generally provides reasonable financial information to the treasurer and the board without the major cost and time commitment associated with full accrual accounting. The treasurer must ensure that the association's accounting system is set up accurately and is followed consistently, no matter which method is used.

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