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Accounts on the Expenses tab, or Items on the Items tab?

For tracking that I both incur something and charge it back, there are two options in QB. Please note that this discussion does not involve Inventory.

1. Using Accounts (this seems the most obvious method to use, but often is NOT the better method to use):

On Purchase Transactions (check, credit card charge, Bill), I enter the data on the Expenses tab and I "job track" it (assign the customer to the detail lines) to note this is a Direct cost. I also mark it as Billable.

On the "Sale" to the customer (invoice, sales receipt, or as Statement Charge), I use the Add Time & Costs button, and these Billable entries show on the Expenses tab.

This typically results in the data flow of Income offsetting the Expense account used from the Purchase transaction = "netting in the account." Net = just the difference. For instance, a Profit and Loss by Job will show $0 for my Building Permit expense account, but I incurred $450 and I charged that back to the customer at $450. "Netting in the accounts" obscures all of this information and makes for bad reporting for management needs.

Buying and selling, even if this chargeback is "at cost," really is Expense and Income for us. Whether goods, services, or other costs such as Postage, the IRS expects us to list Gross Sales and all expenses, not "show us the difference." When I buy a roll of stamps and charge it to you, my net is 0. But, if I buy a roll of stamps and charge anything over my costs or my client pays me in a period that is different than when I incurred that cost, not only does the "invoicing" result in "negative expense" but given the difference due to time or value, I might end the tax year with a total "negative" expense.

Further, the 1099 provisions mean the Gross income I might be reporting for tax purposes doesn't match to what was reported on my behalf, since I "netted" some of that back into expense account. This really becomes a problem when sales taxes are involved, because now Taxable and Nontaxable sales income aren't going to be correct relative to sales taxes owed, where applicable.

Remember that reporting it as Gross Income and actual expense, Vs Net only, does not change the P&L Net Income or the taxable income. It simply gives separation and clarity to the separate activities of Purchases on behalf of, and of Charges to, customers.

There is a provision in QB Edit menu > Preferences, Time & Expenses, Company Preferences tab, to checkmark "Track Reimbursed Expenses as Income." This enables the field to link accounts; we can teach QB which data to track, separately based on the transaction Type (purchase = expense; sales = income). Unfortunately, this will be a "one to one" relationship, so it can result in micromanagement in the Chart of Accounts.

Once you enable that function, you edit an Expense account and you link it to an income account to track it as income, and not "net" into the original expense account, when that expense has been marked as billable to a customer and then put on a sales form.

You can make this change to a data file at any time. When you link an expense account to an income account and try to save that setting, you will get a pop up from the QB program telling you this will be used from now on, and offering to move Existing data for you. Let it!

Remember, this does not change the financial data. It simply organizes it, so that expense stays in Expense and the chargebacks to customers move to the linked Income account. The net is not changed, but the visibility is now separate, for better reporting of the customer-related activities.

Due to the limitation of "one to one" linking, I like this account structure:

Reimbursed Income (parent level, not used), then Subaccounts:
Reimb postage and shipping
Reimb supplies
Reimb travel

Reimbursed Expense accounts typically are:
Shipping and Postage (linked to appropriate subaccount seen above)
Misc Supplies (linked to appropriate subaccount seen above)
Travel Costs (linked to appropriate subaccount seen above)

As I point out, it is "link this expense to an income account, and that way, when I charge to a client something that I incurred, flow that NOT to net into the original expense account." However, the limitations are that you cannot use Quantity, Cost and Pricing; you are limited to the one-to-one relationship; and if you run Job Reports (Job Profitability Detail, for instance), you see "No Item" and everything that is entered on an Expenses tab is in one generic bucket of costs.

So, the better method is:

2. Using Items:

Items are what we make, do, sell, charge, buy, or buy and sell. They allow use to use Quantity and set up account links but use the same item to both purchase and sell. They also offer a "many to one" relationship. Items control the flow of the data to the accounts and offer more control.

This applies to Service Items, Noninventory Part Items and Other Charge Type items. I set it up and mark the box on the left side; the specific wording varies, but the essence is, "I both buy and sell this, and need to show QB how to separately control the flow of the data into different accounts, depending on how and where I use this item."

When you first set up an item, at the bottom right you see a dropdown for "Account" and this is where you link it to expense if you buy this, or income if you charge this to customers.

Once you checkmark that box on the left edge, about half-way down, you see a "Two Sided" item. It is called this because it Reveals the TWO SIDES.

Now you specifically see a Purchase Side, on the left, and you can link this to Expense or Cost of Goods Sold, and this is the financial data flow that is used when I use this Item on a Purchase transaction.

On the Right, you see the Sales Side, and there is a specific dropdown here to link this to an Income account. This controls the financial data flow when I use this item on a Sales transaction, whether I add it to an invoice or sales receipt manually, or when I use Billable Items, with the Add Time & Costs button for charges Billable to customers.

I enter data on the Items tab of purchase transactions, when I incur this as a direct cost for a job (customer name is assigned). I mark it Billable if it will be charged to the customer. I select it as an Add Time & Costs entry. QB controls the flow of the data to the expense account and to the income account based on the Set Up and now I also can run Item Profitability reports, or Job Profitability Detail reports, to see, for example, "I incurred $450 of building permits and I charged $450 to the customer." Better yet, I now can also use Quantity, Cost and Pricing, as applicable to these activities.

Items allow a "many to one" relationship to the accounts, which eliminates the need to micromanage the Chart of accounts, better meeting the reporting needs for the IRS and other tax reporting forms.

I like to use something like this:

Reimbursed Income (just this one account for the Income)

Expense accounts typically are:
Shipping and Postage
Misc Supplies
Travel Costs

Set up Other Charge Type items to meet the names you want the customer to see. ALL are linked to the one Remibursed Income account, but EACH linked to the appropriate Expense account as listed above:

Item Names:
Shipping and Postage
Misc Supplies
Travel – Airfare ← linked to the Travel Cost expense and reimbursed income accounts
Travel – Lodging ← linked to the Travel Cost expense and reimbursed income accounts
Travel – Ground transportation ← linked to the Travel Cost expense and reimbursed income accounts

Use the Items on the Items tab, on the purchase transactions, mark if Billable, and when using Add Time & Costs, charges to customers on sales forms will ALL result in a flow of invoiced data to the one Reimbursed Income account.

If I incur Airfare expense on a Credit Card Charge, some of which is indirect (overhead) and Not Billable nor even Job Tracked, I put this overhead split amount on the Expenses. Then, I put the Job Tracked (billable or not) Item on the Items tab, reiterating it and allocating each amount to each customer name. The total of the Enter Credit Card Charge is the total of the Items tab and the Expenses tab, and the data is correctly Job Tracked, will show on the P&L, and my own share will NOT report on Job reports or Item reports.

Items really are the most powerful tool to use for customer- related activity.