

Other Data

1. Records show that \$4,400 in studio revenue had not yet been billed or recorded as of December 31.
2. Studio supplies on hand at December 31 amount to \$6,900.
3. On August 1, 2005, the studio purchased a six-month insurance policy for \$1,500. The entire premium was initially debited to Unexpired Insurance.
4. The studio is located in a rented building. On November 1, 2005, the studio paid \$6,000 rent in advance for November, December, and January. The entire amount was debited to Prepaid Studio Rent.
5. The useful life of the studio's recording equipment is estimated to be five years (or 60 months). The straight-line method of depreciation is used.
6. On May 1, 2005, the studio borrowed \$16,000 by signing a 12-month, 9 percent note payable to First Federal Bank of St. Louis. The entire \$16,000 plus 12 months' interest is due in full on April 30, 2006.
7. Records show that \$3,600 of cash receipts originally recorded as Unearned Studio Revenue had been earned as of December 31.
8. Salaries earned by recording technicians that remain unpaid at December 31 amount to \$540.
9. The studio's accountant estimates that income taxes expense for the *entire year* ended December 31, 2005, is \$19,600. (Note that \$17,900 of this amount has already been recorded.)

Instructions

- a. For each of the above numbered paragraphs, prepare the necessary adjusting entry (including an explanation).
- b. Using figures from the company's unadjusted trial balance in conjunction with the adjusting entries made in part a, compute net income for the year ended December 31, 2005.
- c. Was the studio's monthly rent for the last 2 months of 2005 more or less than during the first 10 months of the year? Explain your answer.
- d. Was the studio's monthly insurance expense for the last five months of 2005 more or less than the average monthly expense for the first seven months of the year? Explain your answer.
- e. If the studio purchased all of its equipment when it first began operations, for how many months has it been in business? Explain your answer.
- f. Indicate the effect of each adjusting entry prepared in part a on the major elements of the company's income statement and balance sheet. Organize your answer in tabular form using the column headings shown. Use the symbols **I** for increase, **D** for decrease, and **NE** for no effect. The answer for the adjusting entry number 1 is provided as an example.

| Adjusting Entry | Income Statement | | | Balance Sheet | | |
|-----------------|------------------|----------|------------|---------------|-------------|----------------|
| | Revenue | Expenses | Net Income | Assets | Liabilities | Owners' Equity |
| 1 | I | NE | I | I | NE | I |

PROBLEM 4.6

Preparing Adjusting Entries from a Trial Balance



Clint Stillmore operates a private investigating agency called Stillmore Investigations. Some clients pay in advance for services; others are billed after services have been performed. Advanced payments are credited to an account entitled Unearned Retainer Fees. Adjusting entries are performed on a *monthly* basis. An *unadjusted* trial balance dated December 31, 2005, follows. (Bear in mind that adjusting entries have already been made for the first 11 months of 2005, but *not* for December.)

STILLMORE INVESTIGATIONS
Unadjusted Trial Balance
December 31, 2005

| | | |
|--|-----------|-----------|
| Cash | \$ 40,585 | |
| Accounts receivable | 2,000 | |
| Office supplies | 205 | |
| Prepaid rent | 1,200 | |
| Unexpired insurance | 270 | |
| Office equipment | 54,000 | |
| Accumulated depreciation: office equipment | | \$ 35,250 |
| Accounts payable | | 1,400 |
| Interest payable | | 360 |
| Income taxes payable | | 1,750 |
| Note payable | | 9,000 |
| Unearned retainer fees | | 3,500 |
| Capital stock | | 30,000 |
| Retained earnings | | 8,000 |
| Dividends | 1,000 | |
| Client fees earned | | 60,000 |
| Office supplies expense | 605 | |
| Depreciation expense: office equipment | 8,250 | |
| Rent expense | 5,775 | |
| Insurance expense | 1,010 | |
| Salaries expense | 27,100 | |
| Interest expense | 360 | |
| Income taxes expense | 6,900 | |
| Totals | \$149,260 | \$149,260 |

Other Data

1. Accrued but unrecorded client fees earned at December 31 amount to \$1,500.
2. Records show that \$2,500 of cash receipts originally recorded as Unearned Retainer Fees had been earned as of December 31.
3. Office supplies on hand at December 31 amount to \$110.
4. The company purchased all of its office equipment when it first began business. At that time, the equipment's estimated useful life was six years (or 72 months).
5. On October 1, 2005, the company renewed its rental agreement paying \$1,800 cash for six months' rent in advance.
6. On March 1 of the current year, the company paid \$1,080 cash to renew its 12-month insurance policy.
7. Accrued but unrecorded salaries at December 31 amount to \$1,900.
8. On June 1, 2005, the company borrowed money from the bank by signing a \$9,000, 8 percent, 12-month note payable. The entire note, plus 12 months accrued interest, is due on May 31, 2006.
9. The company's CPA estimates that income taxes expense for the *entire year* is \$7,500.

Instructions

- a. For each of the above numbered paragraphs, prepare the necessary adjusting entry (including an explanation).
- b. Prepare the company's adjusted trial balance dated December 31, 2005.
- c. Using figures from the adjusted trial balance prepared in **b**, compute net income for the year ended December 31, 2005.
- d. How much was the company's average monthly rent expense in January through September of 2005? Explain your answer.

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- e. How much was the company's average monthly insurance expense in January and February of 2005? Explain your answer.
- f. If the company purchased all of its office equipment when it first began operations, for how many months has it been in business? Explain your answer.
- g. Indicate the effect of each adjusting entry prepared in part a on the major elements of the company's income statement and balance sheet. Organize your answer in tabular form using the column headings shown. Use the symbols **I** for increase, **D** for decrease, and **NE** for no effect. The answer for the adjusting entry number **1** is provided as an example.

| Adjusting Entry | Income Statement | | | Balance Sheet | | |
|--------------------|------------------|----------|---------------|---------------|-------------|-------------------|
| | Revenue | Expenses | Net Income | Assets | Liabilities | Owners' Equity |
| 1 | I | NE | I | I | NE | I |