

Woodlawn case part 3



There are several necessary journal entries that have been made to adjust the unadjusted trial balance. For Allowance for doubtful accounts: 1. In 2009, \$ 58, 621. 84 was directly written off to bad debt expense reflecting the amounts owed by customers who had gone bankrupt during the year. The journal entry would have been recorded as Dr Bad debt expense 58, 621. 84 Cr Account receivable 58, 621. 84 To record the uncollectable amount due to customer bankruptcy.

The conditions of using the direct write-off method is either for companies in their first year of operations, or for whom uncollectible accounts are immaterial. Woodlawn does not fit either case. Therefore, it is wrong for Woodlawn to use the direct write-off method. The following journal entry is what should have been recorded, Dr Allowance for doubtful account 58, 621. 84 Cr Account receivable 58, 621. 84 To record the uncollectible amount due to customer bankruptcy. Therefore, the following adjusted entry is made to correct the write-off of \$58, 621. 4. Dr. Allowance for doubtful account 58, 621. 84 Cr. Bad debt expense 58, 621. 84 To record the correction of error made in write-off. 2. Historically, bad debt has averaged out to approximately 1. 5% of revenues. Therefore, we estimate that bad debt in 2009 would be 1. 5% of revenue. The journal entry is the following, Dr. Bad debt expense 20, 279. 28* Cr. Allowance for doubtful account 20, 279. 28 To record the estimated uncollectible amount. *(Calculation: 1. 5%*\$1, 351, 951. 83= 20, 279. 28) 3. As Tim mentioned that Woodlawn has received \$93, 256. 1 that's over 90 days past due since August 31, 2010. There is no journal entry needed to be done, since it had past the fiscal year end. 4. Woodlawn has not received \$69, 942. 13 from Erie Limited that's past due

over 90 days. But since Erie always paid its bills, there is no need to write-off Erie Limited to AFDA. No adjusted entry needed. 5. Calculation of total amount of Allowance for doubtful accounts (AFDA). Assumption for calculating AFDA: we estimate the percentage for AFDA in 2010 to be 11%. This estimation is based on:

1. Based on the information Michael provided, the worse of the recession is over and current economic conditions have improved since last month.
2. Customers are paying slower than previous years due to bad economic conditions. Therefore the percentage of AFDA should fall in a range among percentages of 2008-2009, which is 4.9%-13.1%.

We estimate 11% to be a better choice. The total amount of AFDA ending balance is $11\% \times \$374,692.53 = \$41,216.18$. In order to calculate the AFDA amount needed to adjust, we need the AFDA opening balance which is \$35,000 from trial balance, the correction of error made in write-off \$58,621.4. $\$58,621.84 - \$35,000 = \$23,621.84$. $\$41,216.18 - \$23,621.84 = \$17,594.34$. The adjusted entry is made based on the previous information, Dr Bad debt expense 64,838.02 Cr Allowance for doubtful accounts 64,838.02 To record the adjustment made for Allowance for doubtful accounts at the fiscal year end. For Insurance: Calculation of the adjustment of prepaid expenses at the year end: Prepaid insurance for the beginning of September 1, 2009: \$9,300 Insurance from Fife Insurance: Policy Period: 2010/05/20-2011/05/20 Amount: \$12,885.48 For the period beginning at Sept, 1 2009, to year end at August 31, 2010 is 103 days in total, Total Insurance expense = $\$12,885.48 \times \frac{103}{365} = \$3,636.18$ Balance

required at year end = $\$12,885.48 - \$3,636.18 = \$9,249.30$ Prepaid expense adjustments = $\$9,300 - \$9,249.30 = \$50.70$ The adjusted entry is made based on the previous calculation, Dr Insurance expense \$50.70 Cr Prepaid insurance \$50.70 To record the adjustment of prepaid insurance.