

# ACT2111 Tutorial – Chap.8

ACT2111 Teaching team

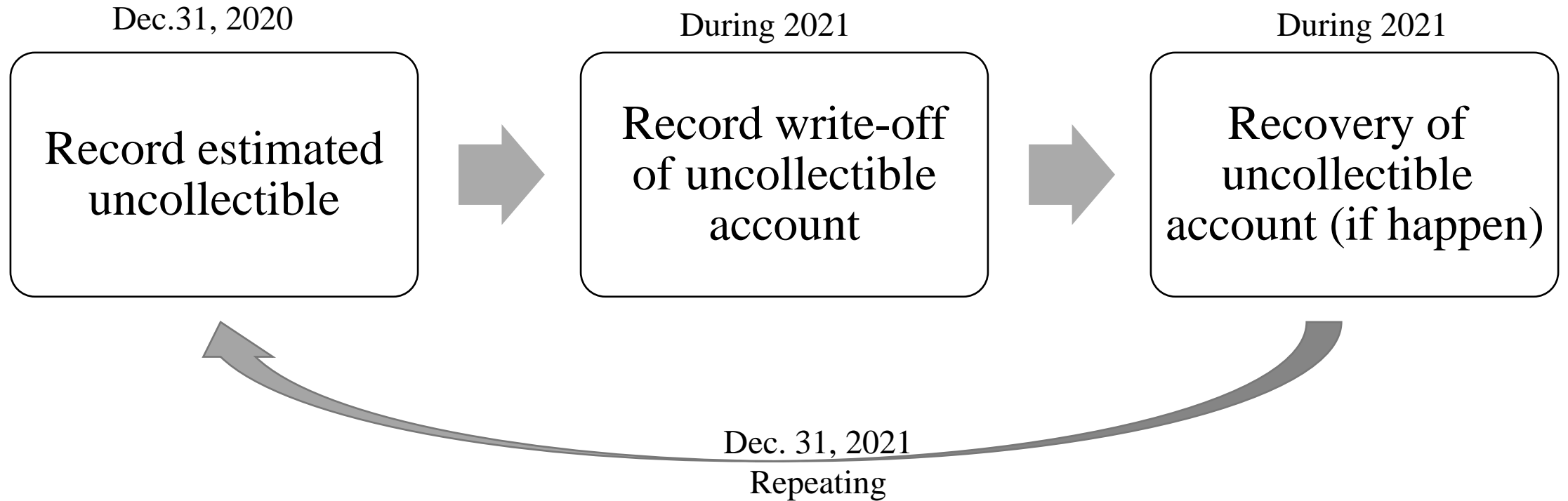
- Account receivable
  - Allowance method
- Note receivable
  - Disposing of note receivable
- Tutorial practice problems
  - E8-4, E8-6, E8-12

# Account receivable

- **Accounts receivable** are amounts customers owe on account.
  - They result from the sale of goods and services
  - Companies generally expect to collect accounts receivable within 30 to 60 days
  - They are usually the most significant type of claim held by a company
  - Receivables are important because they represent one of a company's most liquid assets

# Accounting for uncollectible accounts

## Allowance method



# Accounting for uncollectible accounts - Allowance method

Record estimated uncollectible

## How to estimate uncollectible?

### 1. Percentage-of-receivable method

Estimated uncollectible = amount of uncollectible at the year end  
\* percentage of expected uncollectible

### 2. Aging the account receivable

Different estimate percentage uncollectible for different numbers of days past due.

Accounts Receivable Aging Schedule						
Customer	Total	Not yet due	Number of Days Past Due			
			1-30	31-60	61-90	Over 90
T.E. Adert	¥ 600		¥ 300		¥ 200	¥ 100
R.C. Bortz	300	¥ 300				
B.A. Carl	450		200	¥ 250		
O.L. Diker	700	500			200	
T.O. Ebbet	600			300		300
Others	36,950	26,200	5,200	2,450	1,600	1,500
	¥39,600	¥27,000	¥5,700	¥3,000	¥2,000	¥1,900
Estimated % uncollectible		2%	4%	10%	20%	40%
Total estimated uncollectible	¥2,228	¥540	¥228	¥300	¥400	¥760

# Accounting for uncollectible accounts - Allowance method

Record estimated uncollectible

## How to get bad debt expense?

Beginning Allowance – Actual Write-off + **Bad Debt Expense** = Ending Allowance

Remaining Allowance Before Adjustment

Year-end Adjustment

Allowance for the next year

Estimated uncollectible

Allowance for doubtful accounts	
Write-off	Beginning balance
	Recovery
	Ending balance before adjustment

Allowance for doubtful accounts	
Write-off	Beginning balance
	Recovery
	<b>Bad debts</b>
	Ending balance

Estimation

Estimated uncollectible

Dr. Bad debt expense

Cr. Allowance for doubtful accounts

# Accounting for uncollectible accounts - Allowance method

Record write-off  
of uncollectible  
account

Record actual write-off

(when we think collection is impossible)

Dr. Allowance for doubtful accounts    xxx

Cr. Account receivable    xxx

\*Remark:

- Since write-off of the account reduces both Accounts Receivable and Allowance for Doubtful Accounts by the same amount, cash realizable value of accounts receivable remains unchanged

# Accounting for uncollectible accounts - Allowance method

Recovery of  
uncollectible  
account (if happen)

Recovery of uncollectible account

Dr. Account receivable    xxx

Cr. Allowance for doubtful accounts    xxx

Reverse the  
write-off entry

Dr. Cash    xxx

Cr. Account receivable    xxx

Record the  
collection of  
receivable



# Note receivable

- Companies may grant credit in exchange for a promissory note. A promissory note is a written promise to pay a specified amount of money on demand or at a definite time
  - To the payee, the promissory note is a note receivable
  - To the maker, the promissory note is a note payable
- Notes receivable is similar to account receivable, but a more formal credit arrangement evidenced by a written note.
- Interests are granted in the note receivable

$$\begin{array}{ccccccc} \text{Face Value} & & \text{Annual} & & \text{Time in} & & \\ \text{of Note} & \times & \text{Interest} & \times & \text{Terms of} & = & \text{Interest} \\ & & \text{Rate} & & \text{One Year} & & \end{array}$$

# Note receivables

## Disposing of note receivable

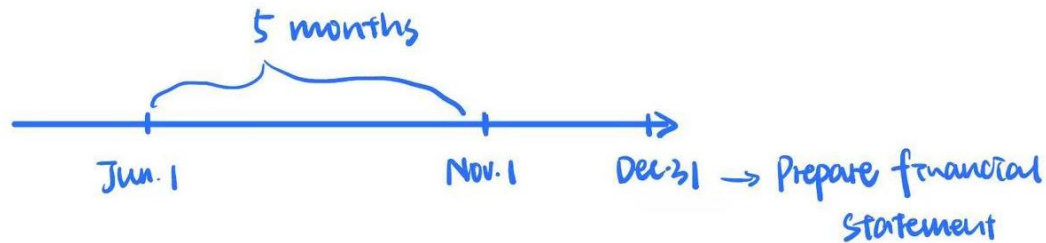
1. Honor of note receivable: Maker pays it in full at its maturity date

### *Example:*

Assume that Wolder Co. lends Higley Co. €10,000 on June 1, accepting a five-month, 9% interest note. Wolder Co. prepare financial statement on December 31.

In this situation, interest is €375 ( $€10,000 \times 9\% \times 5/12$ ).

The amount due, the maturity value, is €10,375 ( $€10,000 + €375$ )

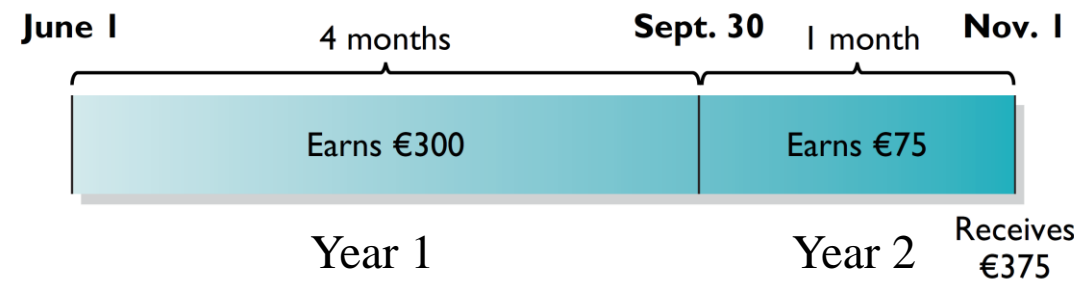


Nov. 1	Cash	10,375	
	Notes Receivable		10,000
	Interest Revenue ( $€10,000 \times 9\% \times \frac{5}{12}$ )		375
	(To record collection of Higley note and interest)		

Scenario 1:  
the maturity  
of note  
receivable is  
within the  
reporting  
period

# Note receivables

*Example:* With previous problem, let's assume Wolder Co. prepares financial statement on September 30.



Scenario 2: the maturity of note receivable is cut off by the reporting date

Sept. 30	Interest Receivable ( $€10,000 \times 9\% \times \frac{4}{12}$ )	300	
	Interest Revenue (To accrue 4 months' interest on Higley note)		300
Nov. 1	Cash [ $€10,000 + (€10,000 \times 9\% \times \frac{5}{12})$ ]	10,375	
	Notes Receivable		10,000
	Interest Receivable		300
	Interest Revenue ( $€10,000 \times 9\% \times \frac{1}{12}$ )		75
	(To record collection of Higley note and interest)		

# Note receivables

Disposing of note receivable

## 2. Dishonor of note receivable

Case 1: The note holder usually transfers the **Notes Receivable** account to an **Accounts Receivable** account

Nov. 1	Accounts Receivable	10,375	
	Notes Receivable		10,000
	Interest Revenue		375
	(To record the dishonor of Higley note)		

Case 2: If instead on November 1 there is no hope of collection, the note holder would write off the face value of the note

Nov. 1	Allowance for Doubtful Accounts	10,000	
	Notes Receivable		10,000

**E8.4** At the beginning of the current period, Coe Ltd. had balances in Accounts Receivable of £200,000 and in Allowance for Doubtful Accounts of £9,000 (credit). During the period, it had net credit sales of £800,000 and collections of £763,000. It wrote off as uncollectible accounts receivable of £7,300. However, a £3,100 account previously written off as uncollectible was recovered before the end of the current period. Uncollectible accounts are estimated to total £25,000 at the end of the period. (Omit cost of goods sold entries.)

*Journalize receivables transactions.*

- **Instructions**

- **a.** Prepare the entries to record sales and collections during the period.
- **b.** Prepare the entry to record the write-off of uncollectible accounts during the period.
- **c.** Prepare the entries to record the recovery of the uncollectible account during the period.
- **d.** Prepare the entry to record bad debt expense for the period.
- **e.** Determine the ending balances in Accounts Receivable and Allowance for Doubtful Accounts.
- **f.** What is the net realizable value of the receivables at the end of the period?

**E8.6 (LO 2)** Min Yachts has accounts receivable of ₩95,400 at March 31, 2020 (amounts in thousands). Credit terms are 2/10, n/30. At March 31, 2020, there is a ₩2,100 credit balance in Allowance for Doubtful Accounts prior to adjustment. The company uses the percentage - of - receivables basis for estimating uncollectible accounts. The company's estimates of bad debts are as shown below.

*Determine bad debt expense, and prepare the adjusting entry.*

	Balance, March 31		
Age of Accounts	2020	2019	Estimated Percentage Uncollectible
Current	₩65,000	₩75,000	2%
1–30 days past due	12,900	8,000	5
31–90 days past due	10,100	2,400	30
Over 90 days past due	7,400	1,100	50
	₩95,400	₩86,500	

### Instructions

- Determine the total estimated uncollectibles as of March 31, 2020.
- Prepare the adjusting entry at March 31, 2020, to record bad debt expense.
- Discuss the implications of the changes in the aging schedule from 2019 to 2020.

**E8.12 (LO 3)** Chang Supply has the following transactions related to notes receivable during the last 2 months of 2020. The company does not make entries to accrue interest except at December 31.

*Journalize entries for notes receivable transactions.*

Nov. 1	Loaned HK\$300,000 cash to Manny Shin on a 12 month, 10% note.
Dec. 11	Sold goods to Malcolm Inc., receiving a HK\$67,500, 90 - day, 8% note.
16	Received a HK\$400,000, 180 <u>day</u> , 9% note in exchange for Joe Ferneti's outstanding accounts receivable.
31	Accrued interest revenue on all <u>notes</u> receivable.

### Instructions

- Journalize the transactions for Chang Supply. (Ignore cost of goods sold.)
- Record the collection of the Shin note at its maturity in 2021.