Credit sale -AR turnover Avg A/R 365 AR tumover = DSO compare Pro: Increase Seller's receivable which is - Cons: Increase wage cost weighted more Bad debt cost Delayed reciept of cash when inventory going to be old, but thing would happen, so => cost of good sold how to match bed debt and A/R same period sales has expense has to calculate bad debt expense: Percentage of credit sale orging of A/R [footnote] Public offering, footnotes disclose everything A/R Sale Revenue when estimate the Bad debt BD (tE,-SE) B/S Cash ADA (+XA,-A) ADA CA) A/R Less: ADA

A/R(-A)

inventory

A/R net

Allowance method

- 1. Record the estimated bad debts in the period credit sales occur, using an end-of-period adjustment, and
- 2. Remove ("write off") specific customer balances when they are known to be uncollectible.

Compare to benchmark A/R two over A/R two over $= \frac{365}{NR} two over$ $= \frac{365}{Net sole} = \frac{365 \times Avg \text{ net }AR}{Net soles}$ write off specific customers ADA A/Rwrite off — decrease R/E

E8-9 Recording and Determining the Effects of Write-Offs, Recoveries, and Bad Debt Expense Estimates on the Balance Sheet and Income Statement

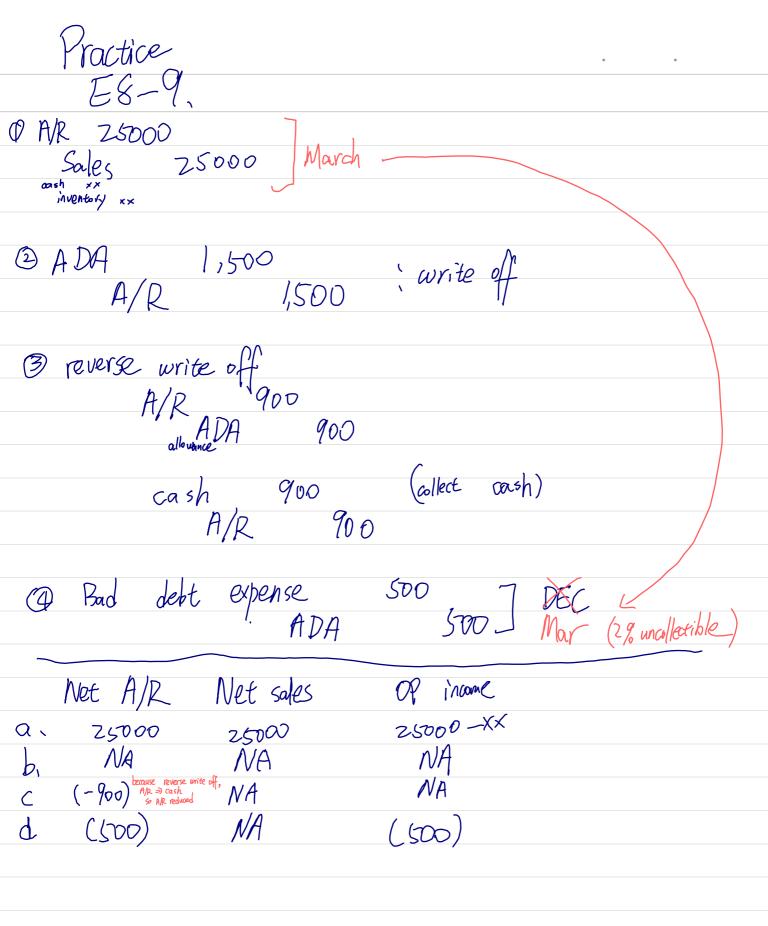
Fraud Investigators Inc. operates a fraud detection service.

Required:

- 1. Prepare journal entries for each transaction below.
 - a. On March 31, 10 customers were billed for detection services totaling \$25,000.
 - **b.** On October 31, a customer balance of \$1,500 from a prior year was determined to be uncollectible and was written off.
 - c. On December 15, a customer paid an old balance of \$900, which had been written off in a prior year.
 - **d.** On December 31, \$500 of bad debts were estimated and recorded for the year.

2. Complete the following table, indicating the amount and effect (+ for increase, – for decrease, and NE for no effect) of each transaction.

Transaction	Net Receivables	Net Sales	Income from Operations
a.			
b.			
C.			
d.			



LO 8-2, 8-3 S8-4 Ethical Decision Making: A Real-Life Example

MCI You work for a company named MCI and you have been assigned the job of adjusting the com-

tomer account balances for December.

44,000

WorldCom

Total

40.000

28,000

35,000

162,000

485,000

750,000

0

0

0

63,000

Customer

AfriTel

CT&T

Hi-Rim

Level 8

NewTel

Others

Telemedia

GlobeCom

Accounts Receivable Aged Listing—December 31 0-30 days 31-60 days 61-90 days 91-120 days >120 days 20.000 10.000 5.000 5.000 0 0 0 0 0 18.000 8.000 1.000 1,000 0 35,000 0 0 0 0

29,000

13,000

13,000

pany's Allowance for Doubtful Accounts balance. You obtained the following aged listing of cus-

0 0	0	0	0
188,000 28,000 11,000 1,00	28,000	188,000	257,000
260,000 70,000 30,000 50,00	70,000	260,000	340,000

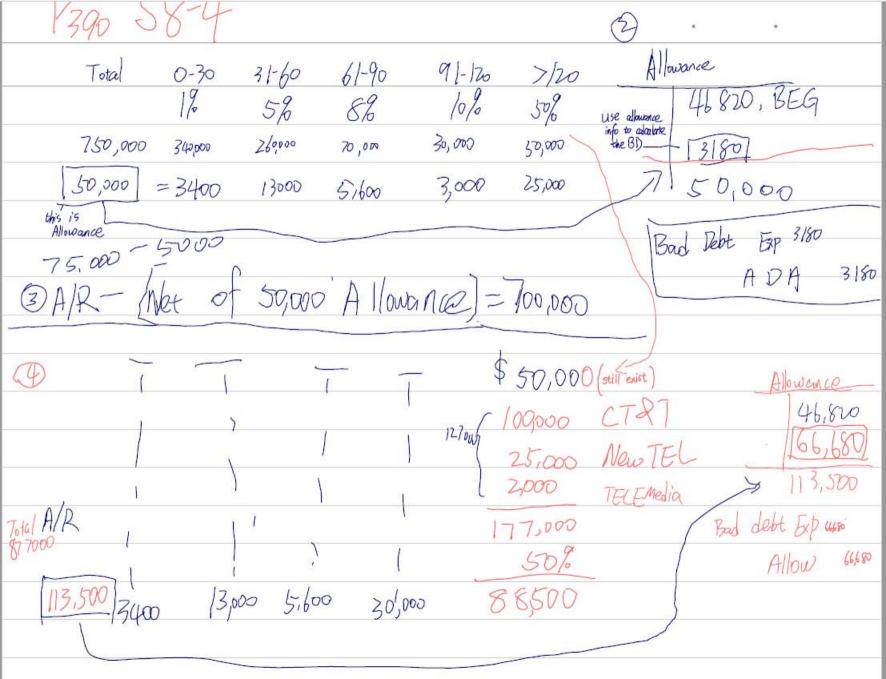
November, when the account had a credit balance of \$46,820.

To check the reasonableness of the calculated balance, you obtain the aged listings for prior months (shown below). As you scan the listings, you notice an interesting pattern. Several account balances, which had grown quite large by the end of November, had disappeared in the final month of the year. You ask the accounts receivable manager, Walter Pavlo, what happened. He said the customers "obtained some financing . . . I guess out of nowhere" and they must have used it to pay off their account balances.

Total Accounts Receivable as of							
	Q1	Q2	Q3	Q4			
Customer	(March 31)	(June 30)	(September 30)	(October 31)	(November 30)	(December 31)	
AfriTel	19,000	19,000	21,000	16,000	20,000	40,000	
CT&T	0	30,000	100,000	100,000	100,000	0	
GlobeCom	29,000	28,000	31,000	27,000	28,000	28,000	
Hi-Rim	0	0	25,000	35,000	35,000	35,000	
Level 8	229,000	229,000	198,000	174,000	190,000	162,000	
NewTel	0	0	25,000	25,000	25,000	0	
Telemedia	0	0	2,000	2,000	2,000	0	
Others	524,000	489,000	375,000	503,000	463,000	485,000	
TOTAL	801,000	795,000	777,000	882,000	863,000	750,000	

Required:

- 1. Calculate the balance that should be reported in Allowance for Doubtful Accounts as of December 31.
- 2. Prepare the adjusting journal entry that is required on December 31.
- 3. Show how Accounts Receivable would be reported on the balance sheet at December 31.
- 4. If the balances for CT&T, NewTel, and Telemedia at the end of November continued to exist at the end of December (in the over-120-days category), what balance would you have estimated for the Allowance for Doubtful Accounts on December 31? Would this have changed MCI's net income in the current year? Explain.



S8-6 Critical Thinking: Analyzing the Impact of Credit Policies

Problem Solved Company has been operating for five years as a software consulting firm. During this period, it has experienced rapid growth in Sales Revenue and in Accounts Receivable. To solve its growing receivables problem, the company hired you as its first corporate controller. You have put into place more stringent credit-granting and collection procedures that you expect will reduce receivables by approximately one-third by year-end. You have gathered the following data related to the changes (in thousands):

	(in thousands)		
	Beginning of Year	End of Year (projected)	
Accounts Receivable	\$1,000,608	\$660,495	
Allowance for Doubtful Accounts	36,800	10,225	
Accounts Receivable, Net	\$ 963,808	\$650,270	
	Prior Year	Current Year (projected)	
Net Sales (assume all on credit)	\$7,515,444	\$7,015,069	

Compute, to one decimal place, the accounts receivable turnover ratio based on three different assumptions: a. The stringent credit policies reduce Accounts Receivable, Net, and decrease Net Sales as

Required:

prior year.

projected in the table.
b. The stringent credit policies reduce Accounts Receivable, Net, as projected in the table but do not decrease Net Sales from the prior year.
c. The stringent credit policies are not implemented, resulting in no change from the

beginning of the year Accounts Receivable balance and no change in Net Sales from the

a) A/R turnover = AVGAR - 70/5069 - 28.7 (650,270+963808)/2 8.7 = 42 days $\frac{75/5444}{(650,270+963808)/2} = 9.3x \frac{3.65}{9.3} = 39 \text{ Days}$ b) FLAT Sales

 $(650,270+963808)/2 \qquad (7.3) \qquad$