# CHAPTER 9
## ACCOUNTING FOR RECEIVABLES

### SUMMARY OF QUESTIONS BY STUDY OBJECTIVES AND BLOOM'S TAXONOMY

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| **Multiple Choice Questions** | | | | | | | | | | | |
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| 47. | 2 | K | 72. | 3 | K | 97. | 3 | AP | 122. | 5 | K | sg147. | 2 | K |
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| 54. | 2 | C | 79. | 3 | C | 104. | 4 | AP | 129. | 6 | K | sg154. | 5 | K |
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| **Brief Exercises** | | | | | | | | | | | |
| 159. | 2 | AN | 162. | 3 | AN | 165. | 5.6 | AN | 168. | 8 | AN |
| 160. | 3 | AN | 163. | 4 | AP | 166. | 5.8 | AP | 169. | 8 | AN |
| 161. | 3 | AN | 164. | 5 | AP | 167. | 6 | AP | 170. | 9 | AN |

*This question also appears in the Study Guide.*

*This question also appears in a self-test at the student companion website.*
### SUMMARY OF QUESTIONS BY STUDY OBJECTIVES AND BLOOM’S TAXONOMY

#### Exercises

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### SUMMARY OF STUDY OBJECTIVES BY QUESTION TYPE

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Note: TF = True-False  BE = Brief Exercise  C = Completion  MC = Multiple Choice  Ex = Exercise

The chapter also contains one set of ten Matching questions and six Short-Answer Essay questions.

CHAPTER STUDY OBJECTIVES

1. **Identify the different types of receivables.** Receivables are frequently classified as (1) accounts, (2) notes, and (3) other. Accounts receivable are amounts customers owe on account. Notes receivable are claims for which lenders issue formal instruments of credit as proof of debt. Other receivables include nontrade receivables such as interest receivable, loans to company officers, advances to employees, and income taxes refundable.

2. **Explain how companies recognize accounts receivable in the accounts.** Companies record accounts receivable at invoice price. They are reduced by sales returns and allowances. Cash discounts reduce the amount received on accounts receivable. When interest is charged on a past due receivable, the company adds this interest to the accounts receivable balance and recognizes it as interest revenue.

3. **Distinguish between the methods and bases companies use to value accounts receivable.** There are two methods of accounting for uncollectible accounts: the allowance method and the direct write-off method. Companies use either the percentage-of-sales or the percentage-of-receivables basis may be used to estimate uncollectible accounts using the allowance method. The percentage of sales basis emphasizes the matching principle. The percentage-of-receivables basis emphasizes the cash realizable value of the accounts receivable. An aging schedule is often used with this basis.

4. **Describe the entries to record the disposition of accounts receivable.** When a company collects an account receivable, it credits Accounts Receivable. When a company sells (factors) an account receivable, a service charge expense reduces the amount collected.

5. **Compute the maturity date of and interest on notes receivable.** For a note stated in months, the maturity date is found by counting the months from the date of issue. For a note stated in days, the number of days is counted, omitting the issue date and counting the due date. The formula for computing interest is Face value \( \times \) Interest rate \( \times \) Time.
6. **Explain how companies recognize notes receivable in the accounts.** Companies record notes receivable at face value. In some cases, it is necessary to accrue interest prior to maturity. In this case, companies debit Interest Receivable and credit Interest Revenue.

7. **Describe how companies value notes receivable.** As with accounts receivable, companies report notes receivable at their cash (net) realizable value. The notes receivable allowance account is the Allowance for Doubtful Accounts. The computation and estimations involved in valuing notes receivable at cash realizable value, and in recording the proper amount of bad debts expense and related allowance are similar to those for accounts receivable.

8. **Describe the entries to record the disposition of notes receivable.** Notes can be held to maturity. At that time, the face value plus accrued interest is due, and the note is removed from the accounts. In many cases, the holder of the note speeds up the conversion by selling the receivable to another party (a factor). In some situations, the maker of the note dishonors the note (defaults), in which case the company writes off the note.

9. **Explain the statement presentation and analysis of receivables.** Companies should identify in the balance sheet or in the notes to the financial statements each major type of receivable. Short-term receivables are considered current assets. Companies report the gross amount of receivables and the allowance for doubtful accounts. They report bad debts and service charge expenses in the multiple-step income statement as operating (selling) expenses; interest revenue appears under other revenues and gains in the nonoperating activities section of the statement. Managers and investors evaluate accounts receivable for liquidity by computing a turnover ratio and an average collection period.

**TRUE-FALSE STATEMENTS**

1. Trade receivables occur when two companies trade or exchange notes receivables.

2. Other receivables include nontrade receivables such as loans to company officers.

3. Both accounts receivable and notes receivable represent claims that are expected to be collected in cash.

4. Receivables are valued and reported in the balance sheet at their gross amount less any sales returns and allowances and less any cash discounts.

5. The three primary accounting problems with accounts receivable are: (1) recognizing, (2) depreciating, and (3) disposing.

6. Accounts receivable are the result of cash and credit sales.

7. If a retailer assesses a finance charge on the amount owed by a customer, Accounts Receivable is debited for the amount of the interest.

8. If a company uses the allowance method to account for uncollectible accounts, the entry to write off an uncollectible account only involves balance sheet accounts.

9. The percentage of receivables basis of estimating expected uncollectible accounts emphasizes income statement relationships.
10. Under the direct write-off method, no attempt is made to match bad debts expense to sales revenues in the same accounting period.

11. Allowance for Doubtful Accounts is debited under the direct write-off method when an account is determined to be uncollectible.

12. Allowance for Doubtful Accounts is a contra asset account.

13. Cash realizable value is determined by subtracting Allowance for Doubtful Accounts from Net Sales.

14. Generally accepted accounting principles require that the direct write-off method be used for financial reporting purposes if it is also used for tax purposes.

15. Under the allowance method, Bad Debts Expense is debited when an account is deemed uncollectible and must be written off.

16. Under the allowance method, the cash realizable value of receivables is the same both before and after an account has been written off.

17. The percentage of sales basis for estimating uncollectible accounts always results in more Bad Debts Expense being recognized than the percentage of receivables basis.

18. An aging schedule is prepared only for old accounts receivables that have been past due for more than one year.

19. An aging of accounts receivable schedule is based on the premise that the longer the period an account remains unpaid, the greater the probability that it will eventually be collected.

20. Sales resulting from the use of VISA and MasterCard are considered credit sales by the retailer.

21. A factor purchases receivables from businesses for a fee and collects the remittances directly from customers.

22. A major advantage of national credit cards to retailers is that there is no charge to the retailer by the credit card companies for their services.

23. Receivables may be sold because they may be the only reasonable source of cash.

24. If a retailer accepts a national credit card such as VISA, the retailer must maintain detailed records of customer accounts.

25. A note receivable is a written promise by the maker to the payee to pay a specified amount of money at a definite time.

26. The maturity date of a 1-month note receivable dated June 30 is July 30.

27. The two key parties to a note are the maker and the payee.

28. When the due date of a note is stated in months, the time factor in computing interest is the number of months divided by 360 days.
29. The accounts receivable turnover ratio is computed by dividing total sales by the average net receivables during the year.

30. Both the gross amount of receivables and the allowance for doubtful accounts should be reported in the financial statements.

Additional True-False Questions

31. Notes receivable represent claims for which formal instruments of credit are issued as evidence of debt.

32. The two methods of accounting for uncollectible accounts are (a) percentage of sales and (b) percentage of receivables.

33. The account Allowance for Doubtful Accounts is closed out at the end of the year.

34. In order to accelerate the receipt of cash from receivables, owners may sell the receivables to another company for cash.

35. When counting the exact number of days to determine the maturity date of a note, the date of issue is included but the due date is omitted.

36. A note is dishonored when it is not fully paid at maturity.

37. Short-term receivables are reported in the current assets section before temporary investments.

Answers to True-False Statements

|------|------|------|------|------|------|------|------|------|------|------|------|------|------|

MULTIPLE CHOICE QUESTIONS

38. Claims for which formal instruments of credit are issued as proof of the debt are
   a. accounts receivable.
   b. interest receivable.
   c. notes receivable.
   d. other receivables.

39. Interest is usually associated with
   a. accounts receivable.
   b. notes receivable.
   c. doubtful accounts.
   d. bad debts.
40. The receivable that is usually evidenced by a formal instrument of credit is a(n)
   a. trade receivable.
   b. note receivable.
   c. accounts receivable.
   d. income tax receivable.

41. Which of the following receivables would not be classified as an "other receivable"?
   a. Advance to an employee
   b. Refundable income tax
   c. Notes receivable
   d. Interest receivable

42. Notes or accounts receivables that result from sales transactions are often called
   a. sales receivables.
   b. non-trade receivables.
   c. trade receivables.
   d. merchandise receivables.

43. The term "receivables" refers to
   a. amounts due from individuals or companies.
   b. merchandise to be collected from individuals or companies.
   c. cash to be paid to creditors.
   d. cash to be paid to debtors.

44. A cash discount is usually granted to all of the following except
   a. retail customers.
   b. retailers.
   c. wholesalers.
   d. All of these are granted discounts.

45. Which one of the following is not a primary problem associated with accounts receivable?
   a. Depreciating accounts receivable
   b. Recognizing accounts receivable
   c. Valuing accounts receivable
   d. Disposing of accounts receivable

46. Trade accounts receivable are valued and reported on the balance sheet
   a. in the investment section.
   b. at gross amounts less sales returns and allowances.
   c. at net realizable value.
   d. only if they are not past due.

47. Three accounting issues associated with accounts receivable are
   a. depreciating, returns, and valuing.
   b. depreciating, valuing, and collecting.
   c. recognizing, valuing, and disposing.
   d. accrual, bad debts, and disposing.
48. Which of the following would require a compound journal entry?
   a. To record merchandise returned that was previously purchased on account.
   b. To record sales on account.
   c. To record purchases of inventory when a discount is offered for prompt payment.
   d. To record collection of accounts receivable when a cash discount is taken.

49. Which of the following would be considered as an unlikely occurrence?
   a. Manufacturer offers a cash discount to a wholesaler.
   b. Wholesaler offers a cash discount to a retailer.
   c. Retailer offers a cash discount to a customer.
   d. All of these are standard practices.

Use the following information for questions 50–51.

A customer charges a treadmill at Hank's Sport Shop. The price is $2,000 and the financing charge is 9% per annum if the bill is not paid in 30 days. The customer fails to pay the bill within 30 days and a finance charge is added to the customer's account.

50. What is the amount of the finance charge?
   a. $60
   b. $15
   c. $180
   d. $6

51. The accounts affected by the journal entry made by Hank's Sport Shop to record the finance charge are
   a. Accounts Receivable
     Cash
   b. Cash
     Finance Receivable
   c. Accounts Receivable
     Interest Payable
   d. Accounts Receivable
     Interest Revenue

52. Which of the following practices by a credit card company results in lower interest charges to the cardholder?
   a. The card company states interest as a monthly percentage rather than an annual percentage.
   b. The card company allows a grace period before interest is accrued.
   c. The card company allows cardholders to skip payments on their cards.
   d. The card company calculates finance charges from the date of purchase to the date the amount is paid.

53. If a department store fails to make the entry to accrue the finance charges due from customers,
   a. accounts receivable will be overstated.
   b. interest revenue will be understated.
   c. interest expense will be overstated.
   d. interest expense will be understated.
54. Under the allowance method, writing off an uncollectible account
   a. affects only balance sheet accounts.
   b. affects both balance sheet and income statement accounts.
   c. affects only income statement accounts.
   d. is not acceptable practice.

55. The net amount expected to be received in cash from receivables is termed the
   a. cash realizable value.
   b. cash-good value.
   c. gross cash value.
   d. cash-equivalent value.

56. If a company fails to record estimated bad debts expense,
   a. cash realizable value is understated.
   b. expenses are understated.
   c. revenues are understated.
   d. receivables are understated.

57. Janway sells softball equipment. On November 14, they shipped $1,000 worth of softball
    uniforms to Chris Middle School, terms 2/10, n/30. On November 21, they received an
    order from Douglas High School for $600 worth of custom printed bats to be produced in
    December. On November 30, Chris Middle School returned $100 of defective
    merchandise. Janway has received no payments from either school as of month end.
    What amount will be recognized as net accounts receivable on the Balance Sheet as of
    November 30?
   a. $1,600
   b. $1,500
   c. $1,000
   d. $900

58. Larson Company on July 15 sells merchandise on account to Stuart Co. for $1,000, terms
    2/10, n/30. On July 20 Stuart Co. returns merchandise worth $400 to Larson Company.
    On July 24 payment is received from Stuart Co. for the balance due. What is the amount
    of cash received?
   a. $600
   b. $588
   c. $580
   d. $1,000

59. The existing balance in Allowance for Doubtful Accounts is considered in computing bad
    debts expense in the
   a. direct write-off method.
   b. percentage of receivables basis.
   c. percentage of sales basis.
   d. percentage of receivables and percentage of sales basis.

60. When the allowance method is used to account for uncollectible accounts, Bad Debts
    Expense is debited when
   a. a sale is made.
   b. an account becomes bad and is written off.
   c. management estimates the amount of uncollectibles.
   d. a customer's account becomes past-due.
61. When an account becomes uncollectible and must be written off,
a. Allowance for Doubtful Accounts should be credited.
b. Accounts Receivable should be credited.
c. Bad Debts Expense should be credited.
d. Sales should be debited.

62. The collection of an account that had been previously written off under the allowance method of accounting for uncollectibles
a. will increase income in the period it is collected.
b. will decrease income in the period it is collected.
c. requires a correcting entry for the period in which the account was written off.
d. does not affect income in the period it is collected.

63. The percentage of sales basis of estimating expected uncollectibles
a. emphasizes the matching of expenses with revenues.
b. emphasizes balance sheet relationships.
c. emphasizes cash realizable value.
d. is not generally accepted as a basis for estimating bad debts.

64. An aging of a company’s accounts receivable indicates that $9,000 are estimated to be uncollectible. If Allowance for Doubtful Accounts has a $1,100 credit balance, the adjustment to record bad debts for the period will require a
a. debit to Bad Debts Expense for $9,000.
b. debit to Allowance for Doubtful Accounts for $7,900.
c. debit to Bad Debts Expense for $7,900.
d. credit to Allowance for Doubtful Accounts for $9,000.

65. A debit balance in the Allowance for Doubtful Accounts
a. is the normal balance for that account.
b. indicates that actual bad debt write-offs have exceeded previous provisions for bad debts.
c. indicates that actual bad debt write-offs have been less than what was estimated.
d. cannot occur if the percentage of sales method of estimating bad debts is used.

66. Under the direct write-off method of accounting for uncollectible accounts, Bad Debts Expense is debited
a. when a credit sale is past due.
b. at the end of each accounting period.
c. whenever a pre-determined amount of credit sales have been made.
d. when an account is determined to be uncollectible.

67. An alternative name for Bad Debts Expense is
a. Deadbeat Expense.
b. Uncollectible Accounts Expense.
c. Collection Expense.
d. Credit Loss Expense.

68. A reasonable amount of uncollectible accounts is evidence
a. that the credit policy is too strict.
b. that the credit policy is too lenient.
c. of a sound credit policy.
d. of poor judgments on the part of the credit manager.
69. Bad Debts Expense is considered
   a. an avoidable cost in doing business on a credit basis.
   b. an internal control weakness.
   c. a necessary risk of doing business on a credit basis.
   d. avoidable unless there is a recession.

70. The best managed companies will have
   a. no uncollectible accounts.
   b. a very strict credit policy.
   c. a very lenient credit policy.
   d. some accounts that will prove to be uncollectible.

71. Two methods of accounting for uncollectible accounts are the
   a. allowance method and the accrual method.
   b. allowance method and the net realizable method.
   c. direct write-off method and the accrual method.
   d. direct write-off method and the allowance method.

72. The allowance method of accounting for uncollectible accounts is required if
   a. the company makes any credit sales.
   b. bad debts are significant in amount.
   c. the company is a retailer.
   d. the company charges interest on accounts receivable.

73. Bad Debts Expense is reported on the income statement as
   a. part of cost of goods sold.
   b. reducing gross profit.
   c. an operating expense.
   d. a contra-revenue account.

74. When the allowance method of accounting for uncollectible accounts is used, Bad Debts
   Expense is recorded
   a. in the year after the credit sale is made.
   b. in the same year as the credit sale.
   c. as each credit sale is made.
   d. when an account is written off as uncollectible.

75. The method of accounting for uncollectible accounts that results in a better matching of
   expenses with revenues is the
   a. aging accounts receivable method.
   b. direct write-off method.
   c. percentage of receivables method.
   d. percentage of sales method.

76. To record estimated uncollectible accounts using the allowance method, the adjusting
   entry would be a
   a. debit to Accounts Receivable and a credit to Allowance for Doubtful Accounts.
   b. debit to Bad Debts Expense and a credit to Allowance for Doubtful Accounts.
   c. debit to Allowance for Doubtful Accounts and a credit to Accounts Receivable.
   d. debit to Loss on Credit Sales and a credit to Accounts Receivable.
77. Under the allowance method of accounting for uncollectible accounts,
   a. the cash realizable value of accounts receivable is greater before an account is written
      off than after it is written off.
   b. Bad Debts Expense is debited when a specific account is written off as uncollectible.
   c. the cash realizable value of accounts receivable in the balance sheet is the same
      before and after an account is written off.
   d. Allowance for Doubtful Accounts is closed each year to Income Summary.

78. Allowance for Doubtful Accounts on the balance sheet
   a. is offset against total current assets.
   b. increases the cash realizable value of accounts receivable.
   c. appears under the heading "Other Assets."
   d. is offset against accounts receivable.

79. When an account is written off using the allowance method, the
   a. cash realizable value of total accounts receivable will increase.
   b. total accounts receivable will decrease.
   c. allowance account will increase.
   d. total accounts receivable will stay the same.

80. If an account is collected after having been previously written off,
   a. the allowance account should be debited.
   b. only the control account needs to be credited.
   c. both income statement and balance sheet accounts will be affected.
   d. there will be both a debit and a credit to accounts receivable.

81. When an account is written off using the allowance method, accounts receivable
   a. is unchanged and the allowance account increases.
   b. increases and the allowance account increases.
   c. decreases and the allowance account decreases.
   d. decreases and the allowance account increases.

82. Two bases for estimating uncollectible accounts are:
   a. percentage of assets and percentage of sales.
   b. percentage of receivables and percentage of total revenue.
   c. percentage of current assets and percentage of sales.
   d. percentage of receivables and percentage of sales.

83. The percentage of receivables basis for estimating uncollectible accounts emphasizes
   a. cash realizable value.
   b. the relationship between accounts receivable and bad debts expense.
   c. income statement relationships.
   d. the relationship between sales and accounts receivable.

84. Long Company uses the percentage of sales method for recording bad debts expense.
    For the year, cash sales are $500,000 and credit sales are $2,000,000. Management
    estimates that 1% is the sales percentage to use. What adjusting entry will Long Company
    make to record the bad debts expense?
85. The balance of Allowance for Doubtful Accounts prior to making the adjusting entry to record estimated uncollectible accounts
   a. is relevant when using the percentage of receivables basis.
   b. is relevant when using the percentage of sales basis.
   c. is relevant to both bases of adjusting for uncollectible accounts.
   d. will never show a debit balance at this stage in the accounting cycle.

86. The direct write-off method of accounting for bad debts
   a. uses an allowance account.
   b. uses a contra-asset account.
   c. does not require estimates of bad debt losses.
   d. is the preferred method under generally accepted accounting principles.

87. Under the direct write-off method of accounting for uncollectible accounts
   a. the allowance account is increased for the actual amount of bad debt at the time of write-off.
   b. a specific account receivable is decreased for the actual amount of bad debt at the time of write-off.
   c. balance sheet relationships are emphasized.
   d. bad debts expense is always recorded in the period in which the revenue was recorded.

88. An aging of a company's accounts receivable indicates that $4,000 are estimated to be uncollectible. If Allowance for Doubtful Accounts has a $1,200 credit balance, the adjustment to record bad debts for the period will require a
   a. debit to Bad Debts Expense for $4,000.
   b. debit to Allowance for Doubtful Accounts for $2,800.
   c. debit to Bad Debts Expense for $2,800.
   d. credit to Allowance for Doubtful Accounts for $4,000.

89. An aging of a company's accounts receivable indicates that $3,000 are estimated to be uncollectible. If Allowance for Doubtful Accounts has a $1,200 debit balance, the adjustment to record bad debts for the period will require a
   a. debit to Bad Debts Expense for $3,000.
   b. debit to Bad Debts Expense for $4,200.
   c. debit to Bad Debts Expense for $1,800.
   d. credit to Allowance for Doubtful Accounts for $4,000.

90. Using the percentage of receivables method for recording bad debts expense, estimated uncollectible accounts are $25,000. If the balance of the Allowance for Doubtful Accounts is $8,000 debit before adjustment, what is the amount of bad debts expense for that period?
91. Using the percentage of receivables method for recording bad debts expense, estimated uncollectible accounts are $10,000. If the balance of the Allowance for Doubtful Accounts is $2,000 credit before adjustment, what is the amount of bad debts expense for that period?
   a. $10,000
   b. $8,000
   c. $12,000
   d. $2,000

92. Using the percentage of receivables method for recording bad debts expense, estimated uncollectible accounts are $10,000. If the balance of the Allowance for Doubtful Accounts is $2,000 debit before adjustment, what is the balance after adjustment?
   a. $10,000
   b. $12,000
   c. $8,000
   d. $2,000

93. Using the allowance method, the uncollectible accounts for the year is estimated to be $28,000. If the balance for the Allowance for Doubtful Accounts is a $7,000 credit before adjustment, what is the amount of bad debts expense for the period?
   a. $7,000
   b. $21,000
   c. $28,000
   d. $35,000

94. Using the allowance method, the uncollectible accounts for the year is estimated to be $28,000. If the balance for the Allowance for Doubtful Accounts is a $7,000 debit before adjustment, what is the amount of bad debts expense for the period?
   a. $7,000
   b. $21,000
   c. $28,000
   d. $35,000

95. In reviewing the accounts receivable, the cash realizable value is $16,000 before the write-off of a $1,500 account. What is the cash realizable value after the write-off?
   a. $16,000
   b. $1,500
   c. $17,500
   d. $14,500

96. In 2008, the Fitzu Co. had net credit sales of $750,000. On January 1, 2008, Allowance for Doubtful Accounts had a credit balance of $16,000. During 2008, $30,000 of uncollectible accounts receivable were written off. Past experience indicates that the allowance should be 10% of the balance in receivables (percentage of receivable basis). If the accounts receivable balance at December 31 was $200,000, what is the required adjustment to the Allowance for Doubtful Accounts at December 31, 2008?
97. A company has net credit sales of $900,000 for the year and it estimates that uncollectible accounts will be 2% of sales. If Allowance for Doubtful Accounts has a credit balance of $1,000 prior to adjustment, its balance after adjustment will be a credit of
a. $18,000.
b. $19,000.
c. $17,980.
d. $17,000.

98. In 2008, Carpenter Company had net credit sales of 1,125,000. On January 1, 2008, Allowance for Doubtful Accounts had a credit balance of $27,000. During 2008, $45,000 of uncollectible accounts receivable were written off. Past experience indicates that the allowance should be 10% of the balance in receivables (percentage of receivables basis). If the accounts receivable balance at December 31 was $300,000, what is the required adjustment to the Allowance for Doubtful Accounts at December 31, 2008?

a. $30,000
b. $112,500
c. $48,000
d. $45,000

99. The change in the cash realizable value from the balance at 12/31/07 to 12/31/08 was a
a. $50,000 increase.
b. $59,000 increase.
c. $42,000 increase.
d. $51,000 increase.

100. Bad debts expense for 2008 is
a. $17,000.
b. $9,000.
c. $54,000
d. $1,000.

101. During 2008, Carbondale Inc. had sales on account of $132,000, cash sales of $54,000, and collections on account of $84,000. In addition, they collected $1,450 which had been written off as uncollectible in 2007. As a result of these transactions, the change in the accounts receivable balance indicates a
a. $100,550 increase.
b. $48,000 increase.
c. $46,550 increase.
d. $102,000 increase.

102. Brother Bear Corporation’s unadjusted trial balance includes the following balances (assume normal balances):

- Accounts Receivable $746,000
- Allowance for Doubtful Accounts 14,200

Bad debts are estimated to be 6% of outstanding receivables. What amount of bad debts expense will the company record?

a. $44,760  
b. $30,560  
c. $29,708  
d. $45,612

103. Manning Retailers accepted $75,000 of Citibank Visa credit card charges for merchandise sold on July 1. Citibank charges 4% for its credit card use. The entry to record this transaction by Manning Retailers will include a credit to Sales of $75,000 and a debit(s) to:

a. Cash $72,000 and Service Charge Expense $3,000.
b. Accounts Receivable $72,000 and Service Charge Expense $3,000.
c. Cash $72,000 and Interest Expense $3,000.
d. Accounts Receivable $75,000.

104. ABC Company accepted a national credit card for a $3,000 purchase. The cost of the goods sold is $2,400. The credit card company charges a 3% fee. What is the impact of this transaction on net operating income?

a. Increase by $582  
b. Increase by $600  
c. Increase by $510  
d. Increase by $2,910

105. Major advantages of credit cards to the retailer include all of the following except the 

a. issuer does the credit investigation of customers.  
b. issuer undertakes the collection process.  
c. retailer receives more cash from the credit card issuer.  
d. All of these are advantages.

106. The sale of receivables by a business

a. indicates that the business is in financial difficulty.  
b. is generally the major revenue item on its income statement.  
c. is an indication that the business is owned by a factor.  
d. can be a quick way to generate cash for operating needs.

107. If a retailer regularly sells its receivables to a factor, the service charge of the factor should be classified as a(n)

a. selling expense.  
b. interest expense.  
c. other expense.  
d. contra asset.
108. If a company sells its accounts receivables to a factor,
a. the seller pays a commission to the factor.
b. the factor pays a commission to the seller.
c. there is a gain on the sale of the receivables.
d. the seller defers recognition of sales revenue until the account is collected.

109. Retailers generally consider sales from the use of national credit card sales as a
a. credit sale.
b. collection of an accounts receivable.
c. cash sale.
d. collection of a note receivable.

110. Receivables might be sold to
a. lengthen the cash-to-cash operating cycle.
b. take advantage of deep discounts on the cash realizable value of receivables.
c. generate cash quickly.
d. finance companies at an amount greater than cash realizable value.

111. A company regularly sells its receivables to a factor who assesses a 2% service charge on the amount of receivables purchased. Which of the following statements is true for the seller of the receivables?
a. The loss section of the income statement will increase each time receivables are sold.
b. The credit to Accounts Receivable is less than the debit to Cash when the accounts are sold.
c. Selling expenses will increase each time accounts are sold.
d. The other expense section of the income statement will increase each time accounts are sold.

112. Winsor Furniture factors $800,000 of receivables to Fast Factors, Inc. Fast Factors assesses a 2% service charge on the amount of receivables sold. Winsor Furniture factors its receivables regularly with Fast Factors. What journal entry does Winsor make when factoring these receivables?

a. Cash 784,000
   Loss on Sale of Receivables 16,000
   Accounts Receivable 800,000

b. Cash 784,000
   Accounts Receivable 784,000

b. Cash 784,000
   Accounts Receivable 784,000
   Gain on Sale of Receivables 16,000

d. Cash 784,000
   Service Charge Expense 16,000
   Accounts Receivable 800,000

113. When customers make purchases with a national credit card, the retailer
a. is responsible for maintaining customer accounts.
b. is not involved in the collection process.
c. absorbs any losses from uncollectible accounts.
d. receives cash equal to the full price of the merchandise sold from the credit card company.
114. The retailer considers VISA and MasterCard sales as
   a. cash sales.
   b. promissory sales.
   c. credit sales.
   d. contingent sales.

115. The basic issues in accounting for notes receivable include each of the following except
   a. analyzing notes receivable.
   b. disposing of notes receivable.
   c. recognizing notes receivable.
   d. valuing notes receivable.

116. A 60-day note receivable dated June 13 has a maturity date of
   b. August 12.
   c. August 11.
   d. August 10.

117. The maturity value of a $90,000, 10%, 60-day note receivable dated July 3 is
   a. $90,000.
   b. $99,000.
   c. $105,000.
   d. $91,500.

118. A 90-day note dated June 14 has a maturity date of
   a. September 14.
   b. September 12.
   c. September 13.
   d. September 15.

119. A 30-day note dated May 18 has a maturity date of
   a. June 18.
   b. June 17.
   c. June 19.
   d. June 16.

120. A promissory note
   a. is not a formal credit instrument.
   b. may be used to settle an accounts receivable.
   c. has the party to whom the money is due as the maker.
   d. cannot be factored to another party.

121. Which of the following is not true regarding a promissory note?
   a. Promissory notes may not be transferred to another party by endorsement.
   b. Promissory notes may be sold to another party.
   c. Promissory notes give a stronger legal claim to the holder than accounts receivable.
   d. Promissory notes may be bearer notes and not specifically identify the payee by name.
122. The two key parties to a promissory note are the
a. maker and a bank.
b. debtor and the payee.
c. maker and the payee.
d. sender and the receiver.

123. When calculating interest on a promissory note with the maturity date stated in terms of
days, the
a. maker pays more interest if 365 days are used instead of 360.
b. maker pays the same interest regardless if 365 or 360 days are used.
c. payee receives more interest if 360 days are used instead of 365.
d. payee receives less interest if 360 days are used instead of 365.

124. The maturity value of a $4,000, 9%, 60-day note receivable dated February 10th is
a. $4,060.
b. $4,030.
c. $4,000.
d. $4,360.

125. The interest on a $5,000, 10%, 1-year note receivable is
a. $5,000.
b. $500.
c. $5,050.
d. $5,500.

126. The maturity value of a $30,000, 8%, 3-month note receivable is
a. $30,600.
b. $30,240.
c. $32,400.
d. $30,200.

127. The interest on a $4,000, 6%, 60-day note receivable is
a. $240.
b. $40.
c. $80.
d. $120.

128. The interest on a $2,000, 6%, 90-day note receivable is
a. $120.
b. $60.
c. $30.
d. $90.

129. Notes receivable are recognized in the accounts at
a. cash (net) realizable value.
b. face value.
c. gross realizable value.
d. maturity value.
130. A note receivable is a negotiable instrument which
   a. eliminates the need for a bad debts allowance.
   b. can be transferred to another party by endorsement.
   c. takes the place of checks in a business firm.
   d. can only be collected by a bank.

131. A company that receives an interest bearing note receivable will
   a. debit Notes Receivable for the maturity value of the note.
   b. credit Notes Receivable for the maturity value of the note.
   c. debit Notes Receivable for the face value of the note.
   d. credit Notes Receivable for the face value of the note.

132. The face value of a note refers to the amount
   a. that can be received if sold to a factor.
   b. borrowed plus interest received at maturity from the maker.
   c. that is identified on the formal instrument of credit.
   d. remaining after a service charge has been deducted.

133. Risen Company receives a $5,000, 3-month, 8% promissory note from Dodd Company in
    settlement of an open accounts receivable. What entry will Risen Company make upon
    receiving the note?

   a. Notes Receivable............................................................ 5,100
      Accounts Receivable—Dodd Company......................... 5,100
   b. Notes Receivable............................................................ 5,100
      Accounts Receivable—Dodd Company......................... 5,000
      Interest Revenue .................................................. 100
   c. Notes Receivable............................................................ 5,000
      Interest Receivable ................................................ 100
      Accounts Receivable—Dodd Company......................... 5,000
      Interest Revenue .................................................. 100
   d. Notes Receivable............................................................ 5,000
      Accounts Receivable—Dodd Company......................... 5,000

134. When a note is accepted to settle an open account, Notes Receivable is debited for the
    note’s
   a. net realizable value.
   b. maturity value.
   c. face value.
   d. face value plus interest.

135. Short-term notes receivable are reported at
   a. cash (net) realizable value.
   b. face value.
   c. gross realizable value.
   d. maturity value.
136. Short-term notes receivables
   a. have a related allowance account called Allowance for Doubtful Notes Receivable.
   b. are reported at their gross realizable value.
   c. use the same estimations and computations as accounts receivable to determine cash
      realizable value.
   d. present the same valuation problems as long-term notes receivables.

137. When a note receivable is dishonored,
   a. interest revenue is never recorded.
   b. bad debts expense is recorded.
   c. the maturity value of the note is written off.
   d. Accounts Receivable is debited if eventual collection is expected.

138. Herbert Company lends Newton Company $30,000 on April 1, accepting a four-month,
     9% interest note. Herbert Company prepares financial statements on April 30. What
     adjusting entry should be made before the financial statements can be prepared?
     a. Note Receivable ............................................................ 30,000
        Cash .....................................................................  30,000
     b. Interest Receivable ........................................................ 225
        Interest Revenue ..................................................  225
     c. Cash .............................................................................. 225
        Interest Revenue ..................................................  225
     d. Interest Receivable ........................................................ 900
        Interest Revenue ..................................................  900

139. When a note receivable is honored, Cash is debited for the note's
     a. net realizable value.
     b. maturity value.
     c. gross realizable value.
     d. face value.

140. The average collection period for receivables is computed by dividing 365 days by
     a. net credit sales.
     b. average accounts receivable.
     c. ending accounts receivable.
     d. accounts receivable turnover ratio.

141. The average collection period is computed by dividing
     a. net credit sales by average gross accounts receivable.
     b. net credit sales by ending gross accounts receivable.
     c. the accounts receivable turnover ratio by 365 days.
     d. 365 days by the accounts receivable turnover ratio.

Use the following information for questions 142–143.

The financial statements of Bolton Manufacturing Company report net sales of $500,000 and
accounts receivable of $50,000 and $30,000 at the beginning and end of the year, respectively.
142. What is the receivables turnover ratio for Bolton?
   a. 7 times
   b. 10 times
   c. 16.7 times
   d. 12.5 times

143. What is the average collection period for accounts receivable in days?
   a. 52.1
   b. 29.2
   c. 21.9
   d. 36.5

Use the following information for questions 144–145.

The financial statements of Colter Manufacturing Company report net sales of $400,000 and accounts receivable of $80,000 and $40,000 at the beginning and end of the year, respectively.

144. What is the receivables turnover ratio for Colter?
   a. 6.7 times
   b. 10 times
   c. 5 times
   d. 8 times

145. What is the average collection period for accounts receivable in days?
   a. 40 times
   b. 80 times
   c. 54.7 times
   d. 50 times

Additional Multiple Choice Questions

146. Which of the following are also called trade receivables?
   a. Accounts receivable
   b. Other receivables
   c. Advances to employees
   d. Income taxes refundable

147. On February 1, 2008, Cogwell Company sells merchandise on account to Livingston Company for $5,000. The entry to record this transaction by Cogwell Company is
   a. Sales ................................................................. 5,000
      Accounts Payable ............................................... 5,000
   b. Cash ................................................................. 5,000
      Sales ................................................................. 5,000
   c. Accounts Receivable ............................................. 5,000
      Sales ................................................................. 5,000
   d. Notes Receivable .................................................. 5,000
      Accounts Receivable ............................................. 5,000
148. Writing off an uncollectible account under the allowance method requires a debit to
   a. Accounts Receivable.
   b. Allowance for Doubtful Accounts.
   c. Bad Debts Expense.
   d. Uncollectible Accounts Expense.

149. When the allowance method of recognizing bad debts expense is used, the entry to
   recognize that expense
   a. increases net income.
   b. decreases current assets.
   c. has no effect on current assets.
   d. has no effect on net income.

150. The direct write-off method
   a. is acceptable for financial reporting purposes.
   b. debits Allowance for Doubtful Accounts to record write-offs of accounts.
   c. shows only actual losses from uncollectible accounts receivable.
   d. estimates bad debt losses.

151. Voight Company's account balances at December 31 for Accounts Receivable and
   Allowance for Doubtful Accounts were $2,100,000 and $105,000 (Cr.), respectively. An
   aging of accounts receivable indicated that $192,000 are expected to become
   uncollectible. The amount of the adjusting entry for bad debts at December 31 is
   a. $192,000.
   b. $87,000.
   c. $297,000.
   d. $105,000.

152. In recording the sale of accounts receivable, the commission charged by a factor is
   recorded as
   a. Bad Debts Expense.
   b. Commission Expense.
   c. Loss on Sale of Receivables.
   d. Service Charge Expense.

153. Gudenas Co., makes a credit card sale to a customer for $600. The credit card sale has a
   grace period of 30 days and then an interest charge of 18% per year or 1.5% per month is
   added to the balance. If the unpaid balance on the above sale is $360 at the end of the
   grace period, the interest charge is
   a. $9.00.
   b. $6.00.
   c. $3.60.
   d. $5.40.

154. The interest rate specified on any note is for a
   a. day.
   b. month.
   c. week.
   d. year.
155. On February 1, Maris Company received a $9,000, 10%, four-month note receivable. The cash to be received by Maris Company when the note becomes due is
a. $300.
b. $9,000.
c. $9,300.
d. $9,900.

156. The entry to record the dishonor of a note receivable assuming the payee expects eventual collection includes a debit to
a. Notes Receivable.
b. Cash.
c. Allowance for Doubtful Accounts.
d. Accounts Receivable.

157. Which of the following statements concerning receivables is incorrect?
a. Notes receivable are often listed last under receivables.
b. The contingent liability from selling notes receivable should be disclosed.
c. Both the gross amount of receivables and the allowance for doubtful accounts should be reported.
d. Interest revenue and gain on sale of notes receivable are shown under other revenues and gains.

158. The accounts receivable turnover ratio is computed by dividing
a. total sales by average net accounts receivable.
b. net credit sales by average net accounts receivable.
c. total sales by ending net accounts receivable.
d. net credit sales by ending net accounts receivable.

Answers to Multiple Choice Questions

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<th>Item</th>
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<th>Ans.</th>
<th>Item</th>
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<td>c</td>
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<td>c</td>
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<td>c</td>
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<td>c</td>
<td>127.</td>
<td>b</td>
<td>145.</td>
<td>c</td>
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</table>
BRIEF EXERCISES

BE 159

Record the following transactions for Verbatim Company.

1. On August 4, Verbatim sold merchandise on account to Reedy Company for $450, terms 2/10, n/30.
2. On August 7, Verbatim granted Reedy a sales allowance and reduced the cost of the merchandise by $50 because some of the goods were slightly damaged.
3. On August 12, Reedy paid the account in full.

Solution 159  (6 min.)

1. Accounts Receivable ............................................................. 450
   Sales Revenue ................................................................. 450

2. Sales Returns and Allowances ............................................... 50
   Accounts Receivable ......................................................... 50

3. Sales Discounts ............................................................... 8
   Cash ............................................................................. 392
   Accounts Receivable ......................................................... 400

BE 160

At December 31, 2008, Attwood Company reported Accounts Receivable of $34,000 and Allowance for Doubtful Accounts of $3,500. On January 7, 2009, Brady Enterprises declares bankruptcy and it is determined that the receivable of $1,200 from Brady is not collectible.

1. What is the cash realizable value of Accounts Receivable at December 31, 2008?
2. What entry would Attwood make to write off the Brady account?
3. What is the cash realizable value of Accounts Receivable after the Brady account is written off?

Solution 160  (5 min.)

1. Cash realizable value = $34,000 – $3,500 = $30,500

2. Allowance for Doubtful Accounts ............................................. 1,200
   Accounts Receivable—Brady ............................................... 1,200

3. Cash realizable value = ($34,000 – $1,200) – ($3,500 – $1,200) = $30,500
BE 161
Portillo Company's ledger at the end of the current year shows Accounts Receivable of $150,000.

Instructions
a. If Allowance for Doubtful Accounts has a credit balance of $3,000 in the trial balance and bad debts are expected to be 10% of accounts receivable, journalize the adjusting entry for the end of the period.

b. If Allowance for Doubtful Accounts has a debit balance of $3,000 in the trial balance and bad debts are expected to be 10% of accounts receivable, journalize the adjusting entry for the end of the period.

Solution 161  (5 min.)
(a) Bad Debts Expense ................................................................. 12,000
    Allowance for Doubtful Accounts ($15,000 – $3,000) .......... 12,000
    (To adjust the allowance account to total estimated uncollectible, $150,000 × .10 = $15,000)
(b) Bad Debts Expense ................................................................. 18,000
    Allowance for Doubtful Accounts ($15,000 + $3,000) ....... 18,000

BE 162
Noell Co. sells Christmas angels. Noell determines that at the end of December, it has the following aging schedule of Accounts Receivable:

<table>
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<tr>
<th>Customer</th>
<th>Total</th>
<th>Not Yet Due</th>
<th>Number of Days Past Due</th>
</tr>
</thead>
<tbody>
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<td></td>
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<td>1–30</td>
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<tr>
<td>DV Farmer</td>
<td>$500</td>
<td>$300</td>
<td>$200</td>
</tr>
<tr>
<td>JJ Joysen</td>
<td>300</td>
<td>100</td>
<td></td>
</tr>
<tr>
<td>NJ Bell</td>
<td>150</td>
<td></td>
<td>50</td>
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<tr>
<td>JC Net</td>
<td>200</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td></td>
<td>?</td>
<td>300</td>
</tr>
<tr>
<td>% uncollectible</td>
<td>1%</td>
<td>5%</td>
<td>10%</td>
</tr>
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</table>

Compute the net receivables based on the above information at the end of December. (There was no beginning balance in the Allowance for Doubtful Accounts).
### Solution 162 (5 min.)

<table>
<thead>
<tr>
<th>Customer</th>
<th>Total</th>
<th>Not Yet Due</th>
<th>Number of Days Past Due</th>
</tr>
</thead>
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<tr>
<td></td>
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<td>1–30</td>
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<td>DV Farmer</td>
<td>$ 500</td>
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<td>JJ Joysen</td>
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<td>NJ Bell</td>
<td>150</td>
<td></td>
<td>50</td>
</tr>
<tr>
<td>JC Net</td>
<td>200</td>
<td>200</td>
<td></td>
</tr>
<tr>
<td></td>
<td>$1,150</td>
<td>300</td>
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<table>
<thead>
<tr>
<th>% uncollectible</th>
<th>1%</th>
<th>5%</th>
<th>10%</th>
<th>20%</th>
<th>50%</th>
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<tr>
<td>Total Estimated Uncollectible Amounts</td>
<td>$133</td>
<td>$3</td>
<td>$15</td>
<td>$25</td>
<td>$40</td>
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</table>

Net Receivables = ($1,150 – $133 = $1,017)

### BE 163

Mickey Company has the following accounts in its general ledger at July 31: Accounts Receivable $40,000 and Allowance for Doubtful Accounts $2,500. During August, the following transactions occurred.

Oct. 15 Sold $20,000 of accounts receivable to Good Factors, Inc. who assesses a 3% finance charge.

25 Made sales of $900 on VISA credit cards. The credit card service charge is 2%.

**Instructions**

Journalize the transactions.

### Solution 163 (5 min.)

Oct. 15

- **Cash** .......................................................... 19,400
- **Service Charge Expense ($20,000 × 3%)** ...................... 600
- **Accounts Receivable** ............................................ 20,000

25

- **Cash** .......................................................... 882
- **Service Charge Expense ($900 × 2%)** ........................ 18
- **Sales** .......................................................... 900
BE 164
Determine the interest on the following notes:

(a) $2,000 at 6% for 90 days.
(b) $900 at 9% for 5 months.
(c) $3,000 at 8% for 60 days
(d) $1,600 at 7% for 6 months

Solution 164  (5 min.)
(a) $30.00  ($2,000 × .06 × 90/360)
(b) $33.75  ($900 × .09 × 5/12)
(c) $40.00  ($3,000 × .08 × 60/360)
(d) $56.00  ($1,600 × .07 × 6/12)

BE 165
Brama Distributors has the following transactions related to notes receivable during the last two months of the year.

Dec.  1 Loaned $12,000 cash to E. Hoffer on a 1-year, 6% note.
16  Sold goods to J. Smith, receiving a $2,400, 60-day, 7% note.
31  Accrued interest revenue on all notes receivable.

Instructions
Journalize the transactions for Brama Distributors.

Solution 165  (6 min.)
Dec  1 Notes Receivable—E. Hoffer...............................................  12,000
Cash ...........................................................................   12,000
(To record loan made to E. Hoffer)

Dec 16 Notes Receivable—J. Smith................................................  2,400
Sales...........................................................................   2,400
(To record sale to J. Smith)

Dec. 31 Interest Receivable..............................................................  67
Interest Revenue* .......................................................   67
(To record accrued interest)

*Calculation of interest revenue
Hoffer note:  $12,000 × 6% × 30/360 =  $60
Smith note:  2,400 × 7% × 15/360 =  7
Total accrued interest $67
Accounting for Receivables

BE 166
Compute the maturity value for each of the following notes receivable.

1. A $5,000, 6%, 3-month note dated July 20.
   Maturity value $____________.

2. A $12,000, 9%, 150-day note dated August 5.
   Maturity value $____________.

Solution 166 (5 min.)
1. Maturity value: $5,075
   $5,000 × 6% × 3/12 = $75 + $5,000 = $5,075

2. Maturity value: $11,198
   $12,000 × 9% × 150/360 = $450 + $12,000 = $12,450

BE 167
On February 7, Able Company sold goods on account to Charlene Enterprises for $3,200, terms 2/10, n/30. On March 9, Charlene gave Able a 60-day, 12% promissory note in settlement of the account. Record the sale and the acceptance of the promissory note on the books of Able Company.

Solution 167 (4 min.)
February 7   Accounts Receivable................................. 3,200
            Sales Revenue ........................................... 3,200

March 9    Notes Receivable .................................................. 3,200
            Accounts Receivable ........................................ 3,200

BE 168
On March 9, Charlene gave Able Company a 60-day, 12% promissory note for $3,200. Charlene honors the note on May 9. Record the collection of the note and interest by Able assuming that no interest has been accrued.

Solution 168 (3 min.)
May 9    Cash........................................................................ 3,264
        Interest Revenue ............................................... 64
        Note Receivable .................................................. 3,200
BE 169

On March 9, Charlene gave Able Company a 60-day, 12% promissory note for $3,200. Charlene dishonors the note on May 9. Record the entry that Able would make when the note is dishonored, assuming that no interest has been accrued.

Solution 169  (3 min.)

May 9   Accounts Receivable—Charlene...........................................  3,264
              Interest Revenue ...........................................................   64
              Note Receivable ............................................................   3,200

BE 170

The following data exists for Curran Company.

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<td>Accounts Receivable</td>
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<td>$ 70,000</td>
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<tr>
<td>Net Sales</td>
<td>500,000</td>
<td>410,000</td>
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</table>

Calculate the receivables turnover ratio and the average collection period for accounts receivable in days for 2008.

Solution 170  (5 min.)

Receivables turnover ratio = \( \frac{\$500,000}{\left(\frac{\$80,000 + \$70,000}{2}\right)} \) = 6.7 times

Average collection period = \( \frac{365 \text{ days}}{6.7} \) = 54.5 days

**EXERCISES**

Ex. 171

Presented below are various receivable transactions entered into by Brewer Tool Company. Indicate whether the receivables are reported as accounts receivable, notes receivable, or other receivables on the balance sheet.

a. Loaned a company officer $4,000.

b. Accepted a $2,000 promissory note from a customer as payment on account.

c. Determined that a $10,000 income tax refund is due from the IRS.

d. Sold goods to a customer on account for $5,000.

e. Recorded $500 accrued interest on a note receivable due next year.

f. Made an American Express credit card sale for $3,000.

g. Advanced $1,000 to a trusted employee.
Solution 171  (10 min.)
a. Other Receivables  
b. Note Receivable  
c. Other Receivables  
d. Accounts Receivable  
e. Other Receivables  
f. Accounts Receivable  
g. Other Receivables

Ex. 172

Prepare journal entries to record the following transactions entered into by Elway Company:

2008
June 1  Received a $20,000, 12%, 1-year note from Sue Gold as full payment on her account.

Nov. 1  Sold merchandise on account to Peyson, Inc. for $10,000, terms 2/10, n/30.

Nov. 5  Peyson, Inc. returned merchandise worth $500.

Nov. 9  Received payment in full from Peyson, Inc.

Dec. 31  Accrued interest on Gold's note.

2009
June 1  Sue Gold honored her promissory note by sending the face amount plus interest. No interest has been accrued in 2009.

Solution 172  (15 min.)

2008
June 1  Notes Receivable ................................................................. 20,000  
        Accounts Receivable—S. Gold ...................................  20,000  

Nov. 1  Accounts Receivable—Peyson, Inc. ............................ 10,000  
        Sales ............................................................................  10,000  

Nov. 5  Sales Returns and Allowances............................................. 500  
        Accounts Receivable—Peyson, Inc.............................  500  

Nov. 9  Cash ..................................................................................... 9,310  
        Sales Discounts ($9,500 × .02)................................. 190  
        Accounts Receivable—Peyson, Inc.............................  9,500  

Dec. 31  Interest Receivable................................................................. 1,400  
        Interest Revenue ..........................................................  1,400  
($20,000 × 12% × 7 ÷ 12 = $1,400)
Solution 172 (cont.)

2009
June 1 Cash ................................................................. 22,400
Notes Receivable .................................................. 20,000
Interest Receivable ........................................ 1,400
Interest Revenue ............................................... 1,000
($20,000 \times 12\% \times \frac{5}{12} = $1,000)

Ex. 173

Record the following transactions for Wheeler Company.
1. On April 12, sold $12,000 of merchandise to Finney Inc., terms 2/10, n/30.
2. On April 15, Finney returned $2,000 of merchandise.
3. On April 22, Finney paid for the merchandise.

Solution 173 (7 min.)

1. Accounts Receivable .................................................. 12,000
   Sales ................................................................. 12,000
2. Sales Returns and Allowances ...................................... 2,000
   Accounts Receivable ......................................... 2,000
3. Cash ($10,000 – $200) ............................................... 9,800
   Sales Discounts ($10,000 \times 2\%) ............................. 200
   Accounts Receivable ($12,000 – $2,000) ................ 10,000

Ex. 174

The Dent Sign Company uses the allowance method in accounting for uncollectible accounts. Past experience indicates that 1% of net credit sales will eventually be uncollectible. Selected account balances at December 31, 2007, and December 31, 2008, appear below:

<table>
<thead>
<tr>
<th></th>
<th>12/31/07</th>
<th>12/31/08</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net Credit Sales</td>
<td>$400,000</td>
<td>$500,000</td>
</tr>
<tr>
<td>Accounts Receivable</td>
<td>75,000</td>
<td>100,000</td>
</tr>
<tr>
<td>Allowance for Doubtful Accounts</td>
<td>5,000</td>
<td>?</td>
</tr>
</tbody>
</table>

Instructions
(a) Record the following events in 2008.
   Aug. 10 Determined that the account of Ann Koch for $1,000 is uncollectible.
   Sept. 12 Determined that the account of Joe Yates for $4,000 is uncollectible.
   Oct. 10 Received a check for $550 as payment on account from Ann Koch, whose account had previously been written off as uncollectible. She indicated the remainder of her account would be paid in November.
   Nov. 15 Received a check for $450 from Ann Koch as payment on her account.
(b) Prepare the adjusting journal entry to record the bad debt provision for the year ended December 31, 2008.
(c) What is the balance of Allowance for Doubtful Accounts at December 31, 2008?
Solution 174  (20 min.)

(a) Aug. 10  Allowance for Doubtful Accounts.................................  1,000
           Accounts Receivable—Ann Koch...............................  1,000
             (To write off Ann Koch account)

Sept. 12 Allowance for Doubtful Accounts.................................  4,000
           Accounts Receivable—Joe Yates...............................  4,000
             (To write off Joe Yates account)

Oct. 10   Accounts Receivable—Ann Koch................................  1,000
           Allowance for Doubtful Accounts........................  1,000
             (To reinstate Ann Koch account previously
              written off)

           Cash............................................................................  550
           Accounts Receivable—Ann Koch...............................  550
             (To record collection on account)

Nov. 15  Cash............................................................................  450
           Accounts Receivable—Ann Koch...............................  450
             (To record collection on account)

(b) Dec. 31  Bad Debts Expense ($500,000 × 1%) .........................  5,000
           Allowance for Doubtful Accounts........................  5,000
             (To record estimate of uncollectible accounts)

(c) Balance of Allowance for Doubtful Accounts at December 31, 2008, is $6,000 ($5,000 – $1,000 – $4,000 + $1,000 + $5,000).

Ex. 175

Kiley Company had a $700 credit balance in Allowance for Doubtful Accounts at December 31, 2008, before the current year's provision for uncollectible accounts. An aging of the accounts receivable revealed the following:

<table>
<thead>
<tr>
<th>Estimated Percentage</th>
<th>Uncollectible</th>
</tr>
</thead>
<tbody>
<tr>
<td>Current Accounts</td>
<td>$120,000</td>
</tr>
<tr>
<td>1–30 days past due</td>
<td>1%</td>
</tr>
<tr>
<td>31–60 days past due</td>
<td>3%</td>
</tr>
<tr>
<td>61–90 days past due</td>
<td>6%</td>
</tr>
<tr>
<td>Over 90 days past</td>
<td>12%</td>
</tr>
<tr>
<td>Total Accounts Receivable</td>
<td>$155,000</td>
</tr>
<tr>
<td></td>
<td>30%</td>
</tr>
</tbody>
</table>

Instructions

(a) Prepare the adjusting entry on December 31, 2008, to recognize bad debts expense.

(b) Assume the same facts as above except that the Allowance for Doubtful Accounts account had a $500 debit balance before the current year's provision for uncollectible accounts. Prepare the adjusting entry for the current year's provision for uncollectible accounts.

(c) Assume that the company has a policy of providing for bad debts at the rate of 1% of sales, that sales for 2008 were $550,000, and that Allowance for Doubtful Accounts had a $650 credit balance before adjustment. Prepare the adjusting entry for the current year's provision for bad debts.
Solution 175  (20 min.)

(a) Bad Debts Expense .......................................................... 4,460  
    Allowance for Doubtful Accounts ($5,160 – $700) .............. 4,460  
    (To adjust the allowance account to total estimated uncollectible)

(b) Bad Debts Expense .......................................................... 5,660  
    Allowance for Doubtful Accounts ($5,160 + $500) .............. 5,660  
    (To adjust the allowance account to total estimated uncollectible)

(c) Bad Debts Expense ($550,000 × 1%) .................................. 5,500  
    Allowance for Doubtful Accounts ................................. 5,500  
    (To record estimated bad debts for year)

Ex. 176

Compute bad debts expense based on the following information:

(a) Taylor Company estimates that 1% of net credit sales will become uncollectible. Sales are $600,000, sales returns and allowances are $30,000, and the allowance for doubtful accounts has a $6,000 credit balance.

(b) Taylor Company estimates that 3% of accounts receivable will become uncollectible. Accounts receivable are $100,000 at the end of the year, and the allowance for doubtful accounts has a $500 debit balance.

Solution 176  (4 min.)

(a) Bad debts expense = $5,700 [($600,000 – $30,000) × .01]  
(b) Bad debts expense = $3,500 [($100,000 × .03) + $500]

Ex. 177

The December 31, 2007 balance sheet of Quaye Company had Accounts Receivable of $500,000 and a credit balance in Allowance for Doubtful Accounts of $33,000. During 2008, the following transactions occurred: sales on account $1,400,000; sales returns and allowances, $50,000; collections from customers, $1,150,000; accounts written off $35,000; previously written off accounts of $5,000 were collected.

Instructions

(a) Journalize the 2008 transactions.

(b) If the company uses the percentage of sales basis to estimate bad debts expense and anticipates 2% of net sales to be uncollectible, what is the adjusting entry at December 31, 2008?

(c) If the company uses the percentage of receivables basis to estimate bad debts expense and determines that uncollectible accounts are expected to be 4% of accounts receivable, what is the adjusting entry at December 31, 2008?

(d) Which basis would produce a higher net income for 2008 and by how much?
Solution 177  
(20–30 min.)

(a) Accounts Receivable ........................................... 1,400,000  
Sales ................................................................. 1,400,000  
(To record credit sales)

Sales Returns and Allowances .............................. 50,000  
Accounts Receivable ........................................ 50,000  
(To record credits to customers)

Cash ............................................................... 1,150,000  
Accounts Receivable ..................................... 1,150,000  
(To record collection of receivables)

Allowance for Doubtful Accounts .......................... 35,000  
Accounts Receivable ........................................ 35,000  
(To write off specific accounts)

Accounts Receivable ......................................... 5,000  
Allowance for Doubtful Accounts ...................... 5,000  
(To reverse write-off of account)

Cash ............................................................... 5,000  
Accounts Receivable ........................................ 5,000  
(To record collection of account)

(b) Percentage of sales basis:

Sales ................................................................. $1,400,000  
Less: Sales Returns and Allowances .................... 50,000  
Net Sales ......................................................... 1,350,000  
Bad debt percentage .......................................... .02  
Bad debt provision ............................................ $ 27,000  

Dec. 31  Bad Debts Expense .................................. 27,000  
Allowance for Doubtful Accounts ...................... 27,000

(c) Percentage of receivables basis:

<table>
<thead>
<tr>
<th>ACCOUNTS RECEIVABLE</th>
<th>ALLOWANCE FOR DOUBTFUL ACCOUNTS</th>
</tr>
</thead>
<tbody>
<tr>
<td>500,000</td>
<td>35,000</td>
</tr>
<tr>
<td>1,400,000</td>
<td>33,000</td>
</tr>
<tr>
<td>5,000</td>
<td>5,000</td>
</tr>
<tr>
<td>5,000</td>
<td>Bal. 3,000</td>
</tr>
<tr>
<td>Bal. 665,000</td>
<td></td>
</tr>
</tbody>
</table>

Required balance ($665,000 × .04) ......................... $26,600  
Balance before adjustment .................................. 3,000  
Adjustment required .......................................... $23,600  

Dec. 31  Bad Debts Expense .................................. 23,600  
Allowance for Doubtful Accounts ...................... 23,600
Solution 177 (cont.)

(d) Percentage of sales basis .............................................................. $27,000
   Percentage of receivables basis .................................................. 23,600
   Net income higher with percentage of receivables basis by .......... $  3,400

Ex. 178

Lloyd Products is undecided about which base to use in estimating uncollectible accounts. On December 31, 2008, the balance in Accounts Receivable was $680,000 and net credit sales amounted to $3,500,000 during 2008. An aging analysis of the accounts receivable indicated that $36,000 in accounts are expected to be uncollectible. Past experience has shown that about 1% of net credit sales eventually are uncollectible.

Instructions

Prepare the adjusting entries to record estimated bad debts expense using the (1) percentage of sales basis and (2) the percentage of receivables basis under each of the following independent assumptions:

(a) Allowance for Doubtful Accounts has a credit balance of $3,200 before adjustment.
(b) Allowance for Doubtful Accounts has a debit balance of $730 before adjustment.

Solution 178 (15 min.)

(1) Percentage of sales basis:

The following adjusting entry would be the same regardless of the balance in the Allowance for Doubtful Accounts.

   Bad Debts Expense ($3,500,000 × .01) .......................................... 35,000
   Allowance for Doubtful Accounts ............................................... 35,000

(2) Percentage of receivables basis:

(a) Bad Debts Expense ($36,000 – $3,200) ........................................ 32,800
   Allowance for Doubtful Accounts ............................................... 32,800

(b) Bad Debts Expense ($36,000 + $730) ........................................... 36,730
   Allowance for Doubtful Accounts ............................................... 36,730

Ex. 179

The income statement approach to estimating uncollectible accounts expense is used by Dodson Company. On February 28, the firm had accounts receivable in the amount of $437,000 and Allowance for Doubtful Accounts had a credit balance of $2,140 before adjustment. Net credit sales for February amounted to $3,000,000. The credit manager estimated that uncollectible accounts expense would amount to 1% of net credit sales made during February. On March 10, an accounts receivable from Marie Green for $6,100 was determined to be uncollectible and written off. However, on March 31, Green received an inheritance and immediately paid her past due account in full.
Ex. 179  (cont.)

Instructions
(a) Prepare the journal entries made by Dodson Company on the following dates:
1. February 28
2. March 10
3. March 31

(b) Assume no other transactions occurred that affected the allowance account during March.
Determine the balance of Allowance for Doubtful Accounts at March 31.

Solution 179  (15 min.)
(a) 1. Feb. 28 Bad Debts Expense ($3,000,000 × .01) ................... 30,000
    Allowance for Doubtful Accounts ................................. 30,000
    (To record the bad debts expense for
    February)

2. Mar. 10 Allowance for Doubtful Accounts ............................. 6,100
    Accounts Receivable—M. Green ................................. 6,100
    (To write off M. Green account deemed
    uncollectible)

3. Mar. 31 Accounts Receivable—M. Green ............................. 6,100
    Allowance for Doubtful Accounts ................................. 6,100
    (To reinstate an account previously
    written off)

    Mar. 31 Cash ............................................................... 6,100
    Accounts Receivable—M. Green ................................. 6,100
    (To record payment on account in full)

(b) $2,140 + $30,000 – $6,100 + $6,100 = $32,140.

Ex. 180
Elder Company uses the allowance method for estimating uncollectible accounts. Prepare journal
entries to record the following transactions:

January 5 Sold merchandise to Mary Cerner for $1,000, terms n/15.

April 15 Received $200 from Mary Cerner on account.

August 21 Wrote off as uncollectible the balance of the Mary Cerner account when she
declared bankruptcy.

October 5 Unexpectedly received a check for $250 from Mary Cerner.
Solution 180  (10 min.)

January 5  Accounts Receivable ......................................................... 1,000
Sales ............................................................................................... 1,000

April 15  Cash .......................................................................................... 200
Accounts Receivable—M. Cerner .................................................. 200

August 21  Allowance for Doubtful Accounts .................................... 800
Accounts Receivable—M. Cerner .................................................. 800

October 5  Accounts Receivable—M. Cerner ......................................... 250
Allowance for Doubtful Accounts ........................................... 250
Cash ................................................................................................. 250
Accounts Receivable—M. Cerner .................................................. 250

Ex. 181

Stone Furniture Store has credit sales of $400,000 in 2008 and a debit balance of $600 in the Allowance for Doubtful Accounts at year end. As of December 31, 2008, $130,000 of accounts receivable remain uncollected. The credit manager prepared an aging schedule of accounts receivable and estimates that $3,000 will prove to be uncollectible.

On March 4, 2009, the credit manager authorizes a write-off of the $1,000 balance owed by A. Lowell.

Instructions
(a) Prepare the adjusting entry to record the estimated uncollectible accounts expense in 2008.
(b) Show the balance sheet presentation of accounts receivable on December 31, 2008.
(c) On March 4, before the write-off, assume the balance of Accounts Receivable account is $160,000 and the balance of Allowance for Doubtful Accounts is a credit of $2,000. Make the appropriate entry to record the write-off of the Lowell account. Also show the balance sheet presentation of accounts receivable before and after the write-off.

Solution 181  (20 min.)

(a) Bad Debts Expense ($3,000 + $600) ................................................... 3,600
Allowance for Doubtful Accounts .................................................. 3,600

(b) Accounts Receivable ...................................................................... $130,000
Less: Allowance for Doubtful Accounts ........................................... 3,000 $127,000

(c) Allowance for Doubtful Accounts .................................................. 1,000
Accounts Receivable—A. Lowell .................................................. 1,000

<table>
<thead>
<tr>
<th>Before Write-off</th>
<th>After Write-off</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accounts Receivable</td>
<td>$160,000</td>
</tr>
<tr>
<td>Less: Allowance for Doubtful Accounts</td>
<td>$2,000</td>
</tr>
<tr>
<td>Cash Realizable Value</td>
<td>$158,000</td>
</tr>
</tbody>
</table>
Ex. 182
An inexperienced accountant made the following entries. In each case, the explanation to the entry is correct.

Dec. 17 Cash........................................................................................ 2,940
Sales Discounts............................................................................... 60
Accounts Receivable..................................................................... 3,000
(To record collection of 12/4 sales, terms 2/10, n/30)

20 Cash........................................................................................ 18,360
Notes Receivable .......................................................... 18,000
Interest Revenue ........................................................... 360
(Collection of $18,000, 8%, 90 day note dated Sept. 21.
Interest had been accrued through Nov. 30.)

27 Cash........................................................................................ 1,000
Bad Debts Expense.............................................................. 1,000
(To correct erroneous collection entry)

31 Bad Debts Expense.............................................................. 600
Allowance for Doubtful Accounts................................. 600
(To recognize estimated bad debts based on 1% of
net sales of $600,000)

Instructions
Prepare the correcting entries.

Solution 182 (15 min.)

Dec. 17 Accounts Receivable............................................................ 60
Sales Discounts............................................................................... 60
(To correct accounts for granting sales discount when discount period had lapsed)

20 Interest Revenue.................................................................. 280
Interest Receivable...................................................... 280
[To recognize collection of interest accrued through
November 30 ($18,000 × 8% × 70/360 = $280)]

27 Bad Debts Expense.............................................................. 1,000
Allowance for Doubtful Accounts......................................... 1,000
(To correct erroneous collection entry)

31 Bad Debts Expense.............................................................. 5,400
Allowance for Doubtful Accounts................................. 5,400
[To adjust balance in Bad Debts Expense to
$6,000 (1% × $600,000)]
Ex. 183
Prepare the necessary journal entry for the following transaction.
Carlson Company sold $200,000 of its accounts receivables to a factor. The factor charges a 3% fee.

Solution 183 (3 min.)
Cash ($200,000 – $6,000) ................................................................. 194,000
Service Charge Expense ($200,000 × 3%) ....................................... 6,000
Accounts Receivable .......................................................... 200,000

Ex. 184
Morton Company has the following accounts receivable in its general ledger at July 31: Accounts Receivable $32,000. During August, the following transactions occurred.

Aug. 1 Added 1% finance charges to $12,000 of credit card balances for not paying within the 30 day grace period.

15 Sold $20,000 of accounts receivable to Rush Factors Inc. who charge a 2% commission.

28 Collected $7,000 from Morton credit card customers including $350 of finance charges previously billed.

Instructions
(a) Journalize the transactions.
(b) Indicate the statement presentation of finance and service charges.

Solution 184 (12 min.)
(a) Aug. 1 Accounts Receivable .................................................. 120
     Interest Revenue .................................................. 120
     (To recognize finance charges—1% × $12,000)

15 Cash .......................................................... 19,600
     Service Charge Expense ($20,000 × 2%) .................. 400
     Accounts Receivable ........................................ 20,000
     (To record sale of receivables to Rush Factors)

28 Cash .......................................................... 7,000
     Accounts Receivable ........................................ 7,000
     (To record collection of Morton receivables)

(b) Service Charge Expense is a selling expense. Interest Revenue is classified under Other Revenues and Gains.
Ex. 185
Listed below are two independent situations involving the disposition of receivables.

1. Dylan Company sells $300,000 of its receivables to Speedy Factors, Inc. Speedy Factors assesses a finance charge of 2% of the amount of receivables sold.

Instructions
Prepare the journal entry to record the sale of the receivables on Dylan Company's books.

2. A restaurant is the site for a large company party. The bill totals $3,000 and is charged by the patron on a Visa credit card.

Instructions
Assume a 3% service fee is charged by Visa. Record the entry for the transaction on the restaurant's books.

Solution 185  (7 min.)
1. Cash................................................................. 294,000
   Service Charge Expense ($300,000 × .02).......................... 6,000
   Accounts Receivable..................................................... 300,000

2. Cash................................................................. 2,910
   Service Charge Expense ($3,000 × .03).......................... 90
   Sales ........................................................................ 3,000

Ex. 186
Compute the maturity date and the maturity value associated with each of the following notes receivables.

1. A $15,000, 6%, 3-month note dated April 20.
   Maturity date ___________, Maturity value $____________.

2. A $25,000, 8%, 72-day note dated June 10.
   Maturity date ___________, Maturity value $____________.

3. An $8,000, 9%, 30-day note dated September 20.
   Maturity date ___________, Maturity value $____________.

Solution 186  (10 min.)
1. Maturity date: July 20
   Maturity value: $15,225
   $15,000 × 6% × 3/12 = $225 + $15,000 = $15,225
Solution 186 (cont.)

2. Maturity date: Term of note 72 days
   June (30–10) 20
   July 31 51
   Maturity date, August 21

   Maturity value: $25,400
   \[ \$25,000 \times 8\% \times \frac{72}{360} = \$400 + \$25,000 = \$25,400 \]

3. Maturity date: Term of note 30 days
   September (30–20) 10
   Maturity date, October 20

   Maturity value: $8,060
   \[ \$8,000 \times 9\% \times \frac{30}{360} = \$60 + \$8,000 = \$8,060 \]

Ex. 187

Compute the maturity date and interest for the following notes.

<table>
<thead>
<tr>
<th>Dates of Notes</th>
<th>Terms</th>
<th>Principal</th>
<th>Interest Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) April 17</td>
<td>60 days</td>
<td>$60,000</td>
<td>6%</td>
</tr>
<tr>
<td>(b) August 11</td>
<td>3 months</td>
<td>80,000</td>
<td>8%</td>
</tr>
</tbody>
</table>

Solution 187 (3 min.)

<table>
<thead>
<tr>
<th>Maturity Date</th>
<th>Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) June 16</td>
<td>$600 ($60,000 \times .06 \times 60/360)</td>
</tr>
<tr>
<td>(b) November 11</td>
<td>$1,600 ($80,000 \times .08 \times 3/12)</td>
</tr>
</tbody>
</table>

Ex. 188

Compute the missing amount for each of the following notes:

<table>
<thead>
<tr>
<th>Principal</th>
<th>Annual Interest Rate</th>
<th>Time</th>
<th>Total Interest</th>
</tr>
</thead>
<tbody>
<tr>
<td>(a) $40,000</td>
<td>10%</td>
<td>2.5 years</td>
<td>?</td>
</tr>
<tr>
<td>(b) $120,000</td>
<td>?</td>
<td>9 months</td>
<td>$7,200</td>
</tr>
<tr>
<td>(c) ?</td>
<td>10%</td>
<td>90 days</td>
<td>$1,500</td>
</tr>
<tr>
<td>(d) $40,000</td>
<td>9%</td>
<td>?</td>
<td>$1,200</td>
</tr>
</tbody>
</table>
Solution 188  (10 min.)

(a) $10,000  ($40,000 × .10 × 2.5 years) = $10,000
(b) 8%  ($120,000 × ? × 9 ÷ 12 = $7,200; ? = 8%)
(c) $60,000  (? × .10 × 90 ÷ 360 = $1,500; ? = $60,000)
(d) 4 months  ($40,000 × .09 × ? = $1,200; ? = 4 ÷ 12)

Ex. 189
Prepare the necessary journal entries for the following transactions for Presley Co.

May 25  Presley Co. received a $25,000, 2-month, 6% note from Durler Company in settlement of an account receivable.

June 25  Presley Co. received payment on the Durler note.

Solution 189  (5 min.)

May 25  Notes Receivable .............................................................. 25,000
       Accounts Receivable ................................................ 25,000

       (To record acceptance of Ann Howe note as payment on account)

June 25  Cash ................................................................. 25,250
       Notes Receivable ................................................ 25,000
       Interest Revenue ($25,000 × .06 × 2/12) .................. 250

Ex. 190
Record the following transactions in general journal form for Klein Company.

July 1  Received a $10,000, 8%, 3-month note, dated July 1, from Ann Howe in payment of her open account.

Oct. 1  Received notification from Ann Howe that she was unable to honor her note at this time. It is expected that Howe will pay at a later date.

Nov. 15  Received full payment from Ann Howe for her note receivable previously dishonored.

Solution 190  (15 min.)

July 1  Notes Receivable .............................................................. 10,000
       Accounts Receivable—Ann Howe .............................. 10,000
       (To record acceptance of Ann Howe note as payment on account)

Oct. 1  Accounts Receivable—Ann Howe .............................. 10,200
       Notes Receivable ............................................... 10,000
       Interest Revenue ($10,000 × 8% × 1/4) ...................... 200
       (To record dishonored note, $10,000, plus interest)
Solution 190  (cont.)
Nov.  15  Cash ..........................................................  10,200
        Accounts Receivable—Ann Howe ..................  10,200
        (To record payment on account)

Ex. 191
Rowe Boat Company often requires customers to sign promissory notes for major credit
purchases. Journalize the following transactions for Rowe Boat Company.

Feb.  12  Accepted a $25,000, 6%, 60-day note from Jim Stone for a 24-foot motorboat built to
         his specifications.

April 14  Received notification from Jim Stone that he was unable to honor his promissory note
         but that he expects to pay the amount owed in May.

May  26  Received a check from Jim Stone for the total amount owed.

June 10  Received notification by the bank that Jim Stone’s check was being returned "NSF"
         and that Mr. Stone had declared personal bankruptcy.

Solution 191  (15 min.)
Feb.  12  Notes Receivable........................................  25,000
         Sales ..........................................................  25,000

April 14  Accounts Receivable—J. Stone ..................  25,250
         Notes Receivable .......................................  25,000
         Interest Revenue ($25,000 × 6% × 1/6)..............  250

May  26  Cash ..........................................................  25,250
         Accounts Receivable—J. Stone ..................  25,250

June 10  Accounts Receivable—J. Stone ..................  25,250
         Cash ..........................................................  25,250
         Allowance for Doubtful Accounts ...............  25,250
         Accounts Receivable—J. Stone ..................  25,250

Ex. 192
The following information is available for Wenger Company.

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Beginning accounts receivable</td>
<td>$  80,000</td>
</tr>
<tr>
<td>Ending accounts receivable</td>
<td>120,000</td>
</tr>
<tr>
<td>Net sales</td>
<td>1,000,000</td>
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Instructions
Compute the receivables turnover ratio and the average collection period.
Solution 192  (5 min.)

Receivables turnover = 10 times $1,000,000 ÷ [($80,000 + $120,000) ÷ 2]

Average collection period = 36.5 days \( (365 \div 10) \)
COMPLETION STATEMENTS

193. Accounts receivable, which are also referred to as __________ receivables, are amounts owed by customers on account.

194. The three primary accounting problems associated with accounts receivable are (1) ____________, (2) ____________, and (3) ____________ of accounts receivable.

195. In order to encourage prompt payment of a trade receivable, companies often offer a ____________ to customers.

196. When credit sales are made, ____________ Expense is considered a normal and necessary risk of doing business on a credit basis.

197. The two methods of accounting for uncollectible accounts are the ____________ method and the ____________ method.

198. Allowance for Doubtful Accounts is a ____________ account which is ____________ from Accounts Receivable on the balance sheet.

199. When the allowance method is used to account for uncollectible accounts, the ____________ is credited when an account is determined to be uncollectible.

200. The ____________ basis of estimating uncollectibles provides a better ____________ of bad debt expense with sales revenue and therefore emphasizes income statement relationships.

201. The ____________ basis of estimating uncollectibles normally results in the best approximation of ____________ value and therefore emphasizes balance sheet relationships.

202. Sales resulting from the use of VISA and MasterCard are considered ____________ by the retailer.

203. A finance company or bank that purchases receivables from businesses is known as a ____________.

204. A 75-day note receivable dated June 10 would mature on ____________.

205. Collection of a note receivable will result in a credit to ____________ for the face value of the note and a credit to ____________.

206. A note which is not paid on the maturity date is said to be ____________.

Answers to Completion Statements

193. trade 200. percentage of sales, matching
194. recognizing, valuing, disposing 201. percentage of receivables, cash realizable
195. cash discounts 202. cash sales
196. Bad Debts 203. factor
197. allowance, direct write-off 204. August 24
198. contra asset, deducted 205. Notes Receivable, Interest Revenue
199. Accounts Receivable 206. dishonored
MATCHING

207. Match the items below by entering the appropriate code letter in the space provided.

A. Aging of receivables
B. Direct write-off method
C. Promissory note
D. Trade receivables
E. Percentage of sales basis
F. Percentage of receivables basis
G. Factoring
H. Dishonored note
I. Average collection period
J. Credit card sales

___ 1. A written promise to pay a specified amount on demand or at a definite time.
___ 2. Sales that involve the customer, the retailer, and the credit card issuer.
___ 3. Emphasizes the matching of costs and revenues in the same period.
___ 4. Amounts owed by customers from the sale of goods and services.
___ 5. A note which is not paid in full at maturity.
___ 6. Analysis of customer account balances by length of time they have been unpaid.
___ 7. Emphasizes expected cash realizable value of accounts receivable.
___ 8. Generally not acceptable for financial reporting purposes.
___ 9. The amount of time that a receivable is outstanding.
___ 10. Sale of accounts receivable to a factor.

Answers to Matching

1. C 6. A
2. J 7. F
3. E 8. B
5. H 10. G
SHORT-ANSWER ESSAY QUESTIONS

S-A E 208

Management can choose between two bases in calculating the estimated uncollectible accounts under the allowance method. One basis emphasizes an income statement viewpoint whereas the other emphasizes a balance sheet viewpoint. Identify the two bases and contrast the two approaches. How do the different points of view affect the amount recognized as Bad Debts Expense during the accounting period?

Solution 208

The two bases available to calculate the estimated uncollectibles under the accrual based allowance method are: (a) percentage of sales basis and (b) percentage of receivables basis. The percentage of sales basis emphasizes the income statement while the percentage of receivables basis emphasizes the balance sheet. Under the percentage of sales basis the bad debts expense for the period is calculated directly as a percentage of net credit sales without regard to any balance in the allowance account. Under the percentage of receivables basis, the emphasis is on establishing the proper amount to carry as a balance in the allowance account; bad debts expense is indirectly determined to be the amount necessary to create the proper balance in the allowance account.

S-A E 209

Customer purchases using credit cards are a significant source of revenue for many retailers. From the standpoint of a retailer, briefly discuss some advantages and disadvantages of a retail store having its own credit card as opposed to accepting one of the national credit cards (e.g., VISA, MasterCard).

Solution 209

The advantages of a retail store using its own credit card are the avoidance of a 2 to 6 percent charge by the national credit card and the ability to issue credit to the customers of its choice. In addition, with its own credit card operation the retailer earns the interest on the unpaid balances.

The disadvantages of a retail store using its own credit card are the risk of nonpayment (bad debts), the delay in receiving cash from the sales (cash is collected immediately from the national credit card company), and the costs of record keeping and managing (approving credit and collection) its own credit operation.

S-A E 210

Your friend Mark has opened an office supply store. He will extend open credit to local businesses and is concerned about potential bad debts. What can Mark do to reduce potential bad debts?
Solution 210

1. Establish a reasonable policy for extending credit. The company needs to consider the risks of having either a ‘too tight’ or ‘too loose’ credit policy. Potential credit customers should be screened appropriately.

2. The company should decide upon the required payment period and communicate it to customers and employees. This period should be in line with the ones established by competitors. Also, employees should enforce the collection period but yet exercise judgment in unusual circumstances.

3. The company should evaluate the relationship among sales, accounts receivable, and cash collections to monitor trends and watch for potential problems.

4. The company should prepare an accounts receivable aging schedule on a regular basis. The collection department should follow up on past due accounts in a timely and professional manner. There should be a clear company policy regarding collection efforts and when to write off accounts.

S-A E 211

Banks that issue credit cards generally charge retailers a fee of 2 to 4% of the amount of sale. List reasons why companies are willing to pay these fees.

Solution 211

1. The use of bank credit cards increases sales. Many people want to use credit cards to make purchases. If a company does not offer this service, customers will buy from a competitor that does offer the services.

2. Bad debts are absorbed by the credit card company.

3. The company receives its cash (less the fees) immediately.

4. The company does not have to hire employees to approve credit and make collections for these sales.

S-A E 212 (Ethics)

Linder Books, a small book publishing company, wrote off the debt of The Learning Center, and the Academy of Basic Education, both small private schools, after it determined that the schools were facing serious financial difficulty. No notice of the action was sent to the schools; Linder Books simply stopped sending bills. Nearly a year later, The Learning Center was given a large endowment and a government grant. The resulting publicity brought the school to the attention of Linder Books, which immediately reinstated the account, and sent a new bill to the school, including interest for the entire time the debt was outstanding. No further action was taken regarding the Academy of Basic Education, which was still operational.

Required:
Did Linder Books act ethically in reinstating the debt of one client, and not the other? Explain.
Solution 212

Yes, it is ethical to reinstate the debt of The Learning Center, especially since there was no evidence given that The Learning Center attempted to negotiate a reduction or elimination of the debt, or even that it was aware that the debt had been written off by Linder Books. Linder Books' discovery that one bad debt may be collectible places the company under no obligation to attempt to collect any or all of its other bad debts, so it need not have reinstated the other account receivable.

The addition of interest to the debt is another question. Whether the interest would be collectible depends upon the laws of the state, and whether the addition of interest was specified as a possibility when the debt was incurred. It is questionable whether Linder Books can collect also because they apparently did not include interest in earlier bills sent to these clients, and because they stopped sending bills for some period of time.

Note that this solution is different from the case in which a debt is written off because of a bankruptcy. Had The Learning Center become bankrupt, Linder Books could not have legally reinstated the debt, even if The Learning Center became solvent at some time in the future.

S-A E 213 (Communication)

Grenwood Company received a letter from Jane Gambel, a customer. Jane had purchased $425 worth of clothing from Grenwood on credit. She has made two payments of $50 each. She has missed the last two payments, and has received a collection letter from Grenwood. Her total debt presently, with interest and late fees, is $351.13.

Jane sent a letter to Grenwood in which she asked for her debt to be forgiven. She said she had heard that companies make allowances for accounts they are doubtful about collecting, and that Grenwood certainly should have been doubtful about her—that as a college student she had changed her major three times. She also said that she could not enjoy a high quality of life when making such high payments, but that she didn't want to be embarrassed by bill collectors, either. She especially didn't want her parents to find out that she had not paid her debts. Having Grenwood write off her account seemed to her the best solution in the circumstances. She added that the clothes she bought at Grenwood were among the best she had ever owned, and that she "told everybody" that Grenwood was definitely the best place to get clothes.

Required:
You are the accounting manager for Grenwood. Write a short letter to Jane explaining why her debt cannot be written off.
Ms. Jane Gambel  
123 College View Apartments, #717  
Lakeland University  
Lakeland, Michigan 60771  

Dear Ms. Gambel:  

Thank you for your recent letter explaining your delay in paying your account. We appreciated hearing about your satisfaction with Grenwood clothing, and we're glad you tell your friends about us.  

As you know, your account is becoming seriously past due. Presently, the total charges, including late payment penalties and interest (detailed on the attached billing form) is $351.13.  

Your account cannot be simply "forgiven" as you request in your letter. Our "Allowance for Doubtful Accounts" does not mean that we have certain customers whose debts we are willing to cancel readily. When Grenwood extends credit to anyone, it is our expression of confidence in that person's ability and willingness to pay. In other words, we aren't "doubtful" about any of our customers. The Allowance account is simply our recognition that a few customers, though very willing to pay, may become unable to do so because of circumstances beyond their control. If we detect some problem that may indicate a present or future unwillingness to pay, we do not extend credit. To do so would not be fair to Grenwood or to the customer.  

We were sure about your ability and willingness to pay when we granted you credit. We were very pleased to receive your first two payments right on time. Won't you reconsider, and send your next payment today? If you need to renegotiate the size of the payments, you may contact Betty in the Credit Department to discuss the matter.  

I look forward to receiving your payment.  

Sincerely,  

Mary Gates  
Accounting Manager