## CHAPTER 9

## Accounting for Receivables

## ASSIGNMENT CLASSIFICATION TABLE

| Study Objectives |  | Questions | Brief Exercises | Exercises | A Problems | B Problems |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| 1. | Identify the different types of receivables. | 1,2 | 1 |  |  |  |
|  | Explain how companies recognize accounts receivable. | 3 | 2 | 1, 2, 14 | $\begin{aligned} & 1 \mathrm{~A}, 3 \mathrm{~A}, 4 \mathrm{~A}, \\ & 6 \mathrm{~A}, 7 \mathrm{~A} \end{aligned}$ | $\begin{aligned} & 1 \mathrm{~B}, 3 \mathrm{~B}, 4 \mathrm{~B} \\ & 6 \mathrm{~B}, 7 \mathrm{~B} \end{aligned}$ |
|  | Distinguish between the methods and bases companies use to value accounts receivable. | $\begin{aligned} & 4,5,6 \\ & 7,8 \end{aligned}$ | $\begin{aligned} & 3,4,5 \\ & 6,7 \end{aligned}$ | 3, 4, 5, 6 | $\begin{aligned} & 1 \mathrm{~A}, 2 \mathrm{~A}, 3 \mathrm{~A}, \\ & 4 \mathrm{~A}, 5 \mathrm{~A} \end{aligned}$ | $\begin{aligned} & 1 \mathrm{~B}, 2 \mathrm{~B}, 3 \mathrm{~B}, \\ & 4 \mathrm{~B}, 5 \mathrm{~B} \end{aligned}$ |
| 4. | Describe the entries to record the disposition of accounts receivable. | $9,10,11$ | 8 | 7, 8, 9, 14 | 6A, 7A | 6B, 7B |
|  | Compute the maturity date of and interest on notes receivable. | $\begin{aligned} & 12,13,14 \\ & 15,16 \end{aligned}$ | 9, 10 | $\begin{aligned} & 10,11,12 \\ & 13 \end{aligned}$ | 6A, 7A | 6B, 7B |
|  | Explain how companies recognize notes receivable. |  | 11 | 10, 11, 12 | 7A | 7B |
|  | Describe how companies value notes receivable. |  |  |  | 7A | 7B |
|  | Describe the entries to record the disposition of notes receivable. | 17 |  | 12, 13 | 6A, 7A | 6B, 7B |
|  | Explain the statement presentation and analysis of receivables. | 18, 19 | 3, 12 | 14, 15 | 1A, 6A | 1B, 6B |

## ASSIGNMENT CHARACTERISTICS TABLE

| Problem Number | Description | Difficulty Level | Time Allotted (min.) |
| :---: | :---: | :---: | :---: |
| 1A | Prepare journal entries related to bad debts expense. | Simple | 15-20 |
| 2 A | Compute bad debts amounts. | Moderate | 20-25 |
| 3A | Journalize entries to record transactions related to bad debts. | Moderate | 20-30 |
| 4A | Journalize transactions related to bad debts. | Moderate | 20-30 |
| 5A | Journalize entries to record transactions related to bad debts. | Moderate | 20-30 |
| 6A | Prepare entries for various notes receivable transactions. | Moderate | 40-50 |
| 7A | Prepare entries for various receivable transactions. | Complex | 50-60 |
| 1B | Prepare journal entries related to bad debts expense. | Simple | 15-20 |
| 2B | Compute bad debts amounts. | Moderate | 20-25 |
| 3B | Journalize entries to record transactions related to bad debts. | Moderate | 20-30 |
| 4B | Journalize transactions related to bad debts. | Moderate | 20-30 |
| 5B | Journalize entries to record transactions related to bad debts. | Moderate | 20-30 |
| 6B | Prepare entries for various notes receivable transactions. | Moderate | 40-50 |
| 7B | Prepare entries for various receivable transactions. | Complex | 50-60 |

## BLOOM'S TAXONOMY TABLE

Correlation Chart between Bloom's Taxonomy, Study Objectives and End-of-Chapter Exercises and Problems

| Study Objective | Knowledge | Comprehension | Application | Analysis | Synthesis | Evaluation |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
| 1. Identify the different types of receivables. | Q9-2 | Q9-1 BE9-1 |  |  |  |  |
| 2. Explain how companies recognize accounts receivable. |  |  | Q9-3 E9-2 <br> BE9-2 P9-7A <br> E9-1 P9-7B | E9-14 P9-4A P9-3B <br> P9-1A P9-6A P9-4B <br> P9-3A P9-1B P9-6B |  |  |
| 3. Distinguish between the methods and bases used to value accounts receivable. | Q9-8 | $\begin{array}{\|l\|l\|} \text { Q9-4 } \\ \text { Q9-5 } \\ \text { Q9-6 } \end{array}$ | $\begin{aligned} & \mathrm{BE9-4} \\ & \mathrm{BE}-5 \\ & \mathrm{BE} 9-6 \\ & \mathrm{E9-5} \\ & \mathrm{E9-6} \end{aligned}$ | Q9-7 P9-1A P9-1B <br> BE9-3 P9-2A P9-2B <br> BE9-7 P9-3A P9-3B <br> E9-3 P9-4A P9-4B <br> $E 9-4$ $P 9-5 A$ $P 9-5 B$ |  |  |
| 4. Describe the entries to record the disposition of accounts receivable. | Q9-9 | Q9-10 | Q9-11 E9-9 <br> BE9-8 P9-7A <br> E9-7 P9-7B <br> E9-8  | $\begin{array}{\|l} \mathrm{E} 9-14 \\ \text { P9-6A } \\ \text { P9-6B } \end{array}$ |  |  |
| 5. Compute the maturity date of and interest on notes receivable. | Q9-13 | $\begin{aligned} & \text { Q9-12 } \\ & \text { Q9-16 } \end{aligned}$ | Q9-14 E9-12 <br> Q9-15 E9-13 <br> BE9-9 P9-7A <br> BE9-10 P9-7B | $\begin{aligned} & \text { E9-10 } \\ & \text { E9-11 } \\ & \text { P9-6A } \\ & \text { P9-6B } \end{aligned}$ |  |  |
| 6. Explain how companies recognize notes receivable. |  |  | BE9-11 P9-7B <br> P9-7A E9-12 | $\begin{aligned} & \text { E9-10 } \\ & \text { E9-11 } \end{aligned}$ |  |  |
| 7. Describe how companies value notes receivable. |  |  | $\begin{array}{\|l\|l\|} \text { P9-7A } \\ \text { P9-7B } \end{array}$ |  |  |  |
| 8. Describe the entries to record the disposition of notes receivable. |  | Q9-17 | E9-12 P9-7A <br> E9-13 P9-7B | $\begin{array}{\|l} \text { P9-6A } \\ \text { P9-6B } \end{array}$ |  |  |
| 9. Explain the statement presentation and analysis of receivables. | Q9-18 |  | Q9-19 BE9-12 E9-15 | BE9-3 P9-6A <br> E9-14 P9-1B <br> P9-1A P9-6B |  |  |
| Broadening Your Perspective |  |  | Exploring the Web | Decision Making Across the Organization Comparative Analysis |  | All About You Financial Reporting Comparative Analysis Ethics Case Communication |

## ANSWERS TO QUESTIONS

1. Accounts receivable are amounts owed by customers on account. They result from the sale of goods and services in the normal course of business operations (i.e., in trade). Notes receivable represent claims that are evidenced by formal instruments of credit.
2. Other receivables include nontrade receivables such as interest receivable, loans to company officers, advances to employees, and income taxes refundable.
3. Accounts Receivable 40
Interest Revenue 40
4. The essential features of the allowance method of accounting for bad debts are:
(1) Uncollectible accounts receivable are estimated and matched against revenue in the same accounting period in which the revenue occurred.
(2) Estimated uncollectibles are debited to Bad Debts Expense and credited to Allowance for Doubtful Accounts through an adjusting entry at the end of each period.
(3) Actual uncollectibles are debited to Allowance for Doubtful Accounts and credited to Accounts Receivable at the time the specific account is written off.
5. Jerry Gatewood should realize that the decrease in cash realizable value occurs when estimated uncollectibles are recognized in an adjusting entry. The write-off of an uncollectible account reduces both accounts receivable and the allowance for doubtful accounts by the same amount. Thus, cash realizable value does not change.
6. The two bases of estimating uncollectibles are: (1) percentage-of-sales and (2) percentage-ofreceivables. The percentage-of-sales basis establishes a percentage relationship between the amount of credit sales and expected losses from uncollectible accounts. This method emphasizes the matching of expenses with revenues. Under the percentage-of-receivables basis, the balance in the allowance for doubtful accounts is derived from an analysis of individual customer accounts. This method emphasizes cash realizable value.
7. The adjusting entry under the percentage-of-sales basis is:

Bad Debts Expense .................................................................................... 4,100
Allowance for Doubtful Accounts
4,100
The adjusting entry under the percentage-of-receivables basis is:
Bad Debts Expense
2,300
Allowance for Doubtful Accounts (\$5,800 - \$3,500)
8. Under the direct write-off method, bad debt losses are not estimated and no allowance account is used. When an account is determined to be uncollectible, the loss is debited to Bad Debts Expense. The direct write-off method makes no attempt to match bad debts expense to sales revenues or to show the cash realizable value of the receivables in the balance sheet.
9. From its own credit cards, the DeVito Company may realize financing charges from customers who do not pay the balance due within a specified grace period. National credit cards offer the following advantages:
(1) The credit card issuer makes the credit investigation of the customer.
(2) The issuer maintains individual customer accounts.
(3) The issuer undertakes the collection process and absorbs any losses from uncollectible accounts.
(4) The retailer receives cash more quickly from the credit card issuer than it would from individual customers.
10. The reasons companies are selling their receivables are:
(1) Receivables may be sold because they may be the only reasonable source of cash.
(2) Billing and collection are often time-consuming and costly. It is often easier for a retailer to sell the receivables to another party with expertise in billing and collection matters.
11. Cash. $\qquad$ 582,000
Service Charge Expense (3\% X \$600,000) .................................................. 18,000 Accounts Receivable $\qquad$
12. A promissory note gives the holder a stronger legal claim than one on an accounts receivable. As a result, it is easier to sell to another party. Promissory notes are negotiable instruments, which means they can be transferred to another party by endorsement. The holder of a promissory note also can earn interest.
13. The maturity date of a promissory note may be stated in one of three ways: (1) on demand, (2) on a stated date, and (3) at the end of a stated period of time.
14. The maturity dates are: (a) March 13 of the next year, (b) August 4, (c) July 20, and (d) August 30.
15. The missing amounts are: (a) $\$ 20,000$, (b) $\$ 9,000$, (c) $8 \%$, and (d) four months.
16. If a financial institution uses 360 days rather than 365 days, it will receive more interest revenue. The reason is that the denominator is smaller, which makes the fraction larger and, therefore, the interest revenue larger.
17. When Cain Company dishonors a note, it may: (1) issue a new note for the maturity value of the dishonored note, or (2) refuse to make any settlement, or (3) it might make partial payment and issue a new note for the unpaid balance.
18. Each of the major types of receivables should be identified in the balance sheet or in the notes to the financial statements. Both the gross amount of receivables and the allowance for doubtful accounts should be reported. If collectible within a year or the operating cycle, whichever is longer, these receivables are reported as current assets immediately below short-term investments.
19. Net credit sales for the period are $8.14 \times \$ 400,000=\$ 3,256,000$.

## SOLUTIONS TO BRIEF EXERCISES

## BRIEF EXERCISE 9-1

(a) Accounts receivable.
(b) Notes receivable.
(c) Other receivables.

## BRIEF EXERCISE 9-2

(a) Accounts Receivable................................................ 15,200

Sales $\qquad$
(b) Sales Returns and Allowances .............................. 3,800

Accounts Receivable $\qquad$
(c) Cash (\$11,400-\$228)

11,172
Sales Discounts (\$11,400 X 2\%)
228
Accounts Receivable (\$15,200-\$3,800).

BRIEF EXERCISE 9-3
(a) Bad Debts Expense

35,000
Allowance for Doubtful Accounts
35,000
(b) Current assets
$\qquad$
Accounts receivable \$600,000
Less: Allowance for doubtful Accounts

35,000
565,000
Merchandise inventory .................................... 130,000
Prepaid expenses $\qquad$
Total current assets
7,500
\$792,500
(a) Allowance for Doubtful Accounts ..... 5,400
Accounts Receivable-Ristau ..... 5,400
(b)Accounts receivable
Allowance for doubfulaccountsCash realizable value(1) Before Write-Off\$700,00054,000\$646,000
(2) After Write-Off\$694,60048,600\$646,000
BRIEF EXERCISE 9-5
Accounts Receivable-Ristau ..... 5,400
Allowance for Doubtful Accounts ..... 5,400
Cash ..... 5,400
Accounts Receivable-Ristau ..... 5,400
BRIEF EXERCISE 9-6
Bad Debts Expense [(\$800,000 - \$45,000) X 2\%] ..... 15,100Allowance for Doubtful Accounts15,100
BRIEF EXERCISE 9-7
(a) Bad Debts Expense [(\$450,000 X 1\%) - \$1,500] ..... 3,000
Allowance for Doubtful Accounts

$\qquad$ ..... 3,000
(b) Bad Debts Expense [(\$450,000 X 1\%) + \$800] = 5,300
BRIEF EXERCISE 9-8
(a) Cash (\$150-\$6) ..... 144
Service Charge Expense (\$150 X 4\%) ..... 6
Sales
$\qquad$150
(b) Cash (\$60,000-\$1,800) ..... 58,200
Service Charge Expense (\$60,000 X 3\%). ..... 1,800
Accounts Receivable ..... 60,000

Interest Maturity Date
(a) $\$ 800$
(b) $\$ 875$
(c) $\$ 200$

August 9
October 12
July 11

## BRIEF EXERCISE 9-10

|  | Maturity Date |  | Annual Interest Rate |  |
| :--- | :--- | :---: | :---: | :---: |
|  |  | Total Interest |  |  |
| (a) May 31 | $9 \%$ |  | $\$ 9,000$ |  |
| (b) August 1 |  | $8 \%$ |  | $\$ 600$ |
| (c) September 7 |  | $10 \%$ |  | $\$ 6,000$ |

## BRIEF EXERCISE 9-11

Jan. 10 Accounts Receivable ..... 13,600Sales
$\qquad$13,600
Feb. 9 Notes Receivable ..... 13,600
Accounts Receivable ..... 13,600

## BRIEF EXERCISE 9-12

Accounts Receivable Turnover Ratio:
$\frac{\$ 20 B}{(\$ 2.7 B+\$ 2.8 B) \div 2}=\frac{\$ 20 B}{\$ 2.75 B}=7.3$ times

Average Collection Period for Accounts Receivable:
$\frac{365 \text { days }}{7.3 \text { times }}=50$ days

## SOLUTIONS TO EXERCISES

## EXERCISE 9-1

March 1 Accounts Receivable-CC Company ..... 3,000
Sales.............................................................. ..... 3,000
3 Sales Returns and Allowances ..... 500 Accounts Receivable-CC Company ..... 500
9 Cash ..... 2,450
Sales Discounts ..... 50
Accounts Receivable-CC Company ..... 2,500
15 Accounts Receivable ..... 400Sales400
31 Accounts Receivable ..... 6Interest Revenue
$\qquad$6
EXERCISE 9-2
(a) Jan. 6 Accounts Receivable-Cortez ..... 9,000
Sales

$\qquad$ ..... 9,000
16 Cash (\$9,000-\$180) ..... 8,820
Sales Discounts (2\% X \$9,000) ..... 180
Accounts Receivable-Cortez ..... 9,000
(b) Jan. 10 Accounts Receivable-Dawes ..... 9,000
Sales ..... 9,000
Feb. 12 Cash ..... 5,000
Accounts Receivable-Dawes ..... 5,000
Mar. 10 Accounts Receivable—Dawes ..... 80Interest Revenue80[2\% X (\$9,000 - \$5,000)]

## (a)

 Dec. 3Bad Debts Expense
1,400
Accounts Receivable-Fell 1,400
(b) (1) Dec. 31 Bad Debts Expense $\qquad$ 8,100
[(\$840,000-\$30,000) X 1\%] Allowance for Doubtful Accounts $\qquad$ 8,100
(2) Dec. 31 Bad Debts Expense ............................. 9,900 Allowance for Doubtful Accounts $\qquad$ 9,900
[(\$120,000 X 10\%) - \$2,100]
(c) (1) Dec. 31 Bad Debts Expense $\qquad$ 6,075
[(\$840,000 - \$30,000) X .75\%] Allowance for Doubtful Accounts 6,075
(2) Dec. 31 Bad Debts Expense $\qquad$ 7,400 Allowance for Doubtful Accounts 7,400
[(\$120,000 X 6\%) + \$200]

## EXERCISE 9-4


(b) Mar. 31 Bad Debts Expense 6,930
Allowance for Doubtful Accounts
6,930 (\$8,130-\$1,200)
Allowance for Doubtful Accounts ..... 13,000Accounts Receivable
$\qquad$
Accounts Receivable ..... 1,800
Allowance for Doubtful Accounts

1,800
1,800
Cash.
Accounts ReceivableBad Debts Expense15,200
Allowance for Doubtful Accounts
[\$19,000 - (\$15,000 - \$13,000 + \$1,800)]
EXERCISE 9-6
December 31, 2008
Bad Debts Expense (2\% X \$400,000) ..... 8,000
Allowance for Doubtful Accounts
$\qquad$May 11, 2009
Allowance for Doubtful Accounts ..... 1,100
Accounts Receivable-Frye
$\qquad$(4\% X \$3,500)
SalesJune 12, 2009
Accounts Receivable-Frye1,100
Allowance for Doubtful Accounts
$\qquad$
Cash ..... 1,100Accounts Receivable-Frye
$\qquad$
EXERCISE 9-7
(a) Mar. 3 Cash (\$680,000-\$20,400) ..... 659,600
Service Charge Expense20,400(3\% X \$680,000)Accounts Receivable
$\qquad$
(b) May 10 Cash (\$3,500-\$140) ..... 3,360
Service Charge Expense ..... 140

June 12, 2009

Service Charge Expense
Accounts Receivable1,100680,0003,500

13,000

1,800

15,200
15,200
8,0001,1001,100
(a) Apr. 2 Accounts Receivable-Nancy Hansel ..... 1,500
Sales

$\qquad$ ..... 1,500
May 3 Cash ..... 700
Accounts Receivable-Nancy Hansel ..... 700
June 1 Accounts Receivable-Nancy Hansel ..... 8
Interest Revenue. ..... 8
[(\$1,500 - \$700) X 1\%]
(b) July 4 Cash ..... 194
Service Charge Expense ..... 6(3\% X \$200)Sales200
EXERCISE 9-9
(a) Jan. 15 Accounts Receivable ..... 18,000Saless .........................................................18,000
20 Cash (\$4,300-\$86) ..... 4,214
Service Charge Expense ..... 86(\$4,300 X 2\%)
Sales ..... 4,300
Feb. 10 Cash ..... 10,000
Accounts Receivable ..... 10,000
15 Accounts Receivable (\$8,000 X 1\%). ..... 80 Interest Revenue ..... 80
(b) Interest Revenue is reported under other revenues and gains. Service Charge Expense is a selling expense.
(a) ..... 2008
Nov. 1 Notes Receivable ..... 15,000Cash15,000
Dec. 11 Notes Receivable ..... 6,750
Sales

$\qquad$
16 Notes Receivable

$\qquad$ ..... 4,000Accounts Receivable-Reber
$\qquad$
31 Interest Receivable ..... 295
Interest Revenue*
. ...............................

*Calculation of interest revenue:

*Calculation of interest revenue:

*Calculation of interest revenue:

*Calculation of interest revenue:

Givens's note: $\quad \$ 15,000 \times 10 \%$ X $2 / 12=\$ 250$

Givens's note: $\quad \$ 15,000 \times 10 \%$ X $2 / 12=\$ 250$

Givens's note: $\quad \$ 15,000 \times 10 \%$ X $2 / 12=\$ 250$

Givens's note: $\quad \$ 15,000 \times 10 \%$ X $2 / 12=\$ 250$

Countryman's note:

Countryman's note:

Countryman's note:

Countryman's note:  6,750 X 8\% X 20/360 =  6,750 X 8\% X 20/360 =  6,750 X 8\% X 20/360 =  6,750 X 8\% X 20/360 = .....  ..... 30 .....  ..... 30 .....  ..... 30 .....  ..... 30
Reber's note:
Reber's note:
Reber's note:
Reber's note: 4,000 X 9\% X 15/360 = 4,000 X 9\% X 15/360 = 4,000 X 9\% X 15/360 = 4,000 X 9\% X 15/360 = ..... 15 ..... 15 ..... 15 ..... 15
Total accrued interest
Total accrued interest
Total accrued interest
Total accrued interest ..... \$295 ..... \$295 ..... \$295 ..... \$295 ..... 16,500
250 ..... 1,250

$\qquad$ ..... 15,000
EXERCISE 9-11
2008
May 1 Notes Receivable ..... 7,500
Accounts Receivable-Julia Gonzalez ....................................................295
(b)
2009
2009
Nov. 1 Cash
Nov. 1 Cash
Interest Receivable.
Interest Revenue*
Interest Revenue*
Notes Receivable
Notes Receivable
*(\$15,000 X 10\% X 10/12)7,500
Dec. 31 Interest Receivable ..... 500
Interest Revenue500
(\$7,500 X 10\% X 8/12)
31 Interest Revenue ..... 500Income Summary500
2009
May 1 Cash ..... 8,250
Notes Receivable ..... 7,500
Interest Receivable ..... 500
Interest Revenue ..... 250
(\$7,500 X 10\% X 4/12)
EXERCISE 9-12
4/1/08 Notes Receivable ..... 20,000
Accounts Receivable-Wilson ..... 20,000
7/1/08 Notes Receivable ..... 25,000
Cash ..... 25,000
12/31/08 Interest Receivable ..... 1,800
Interest Revenue ..... 1,800
(\$20,000 X 12\% X 9/12)
Interest Receivable ..... 1,250
Interest Revenue ..... 1,250(\$25,000 X 10\% X 6/12)
4/1/09 Cash. ..... 22,400Notes Receivable20,000
Interest Receivable ..... 1,800
Interest Revenue ..... 600(\$20,000 X 12\% X 3/12 = \$600)
Accounts Receivable ..... 26,875
Notes Receivable25,000
Interest Receivable ..... 1,250
Interest Revenue ..... 625

## EXERCISE 9-13

(a) May 2 Notes Receivable .............................................. 7,600 Cash 7,600

| (b) | Nov. 2 | Accounts Receivable-Everhart Inc. $\qquad$ | 7,942 | $\begin{array}{r} 7,600 \\ 342 \end{array}$ |
| :---: | :---: | :---: | :---: | :---: |
|  |  | Notes Receivable. |  |  |
|  |  | Interest Revenue .................................. |  |  |
|  |  | (\$7,600 X 9\% X 1/2) |  |  |
|  |  | (To record the dishonor of |  |  |
|  |  | Everhart Inc. note with expectation of collection) |  |  |
| (c) | Nov. 2 | Allowance for Doubtful Accounts .............. | 7,600 | 7,600 |
|  |  | Notes Receivable ................................ |  |  |
|  |  | (To record the dishonor of |  |  |
|  |  | Everhart Inc. note with no |  |  |
|  |  | expectation of collection) |  |  |

EXERCISE 9-14
(a) Sales $\qquad$
Cost of Goods Sold
Beginning Inventory................................................. \$36,000
Add: Purchases (net).............................................. 60,000
Goods Available for Sale ........................................ 96,000
Less: Ending Inventory .......................................... 33,000
Cost of Goods Sold
63,000
Gross Profit

Total Sales $=\$ 83,000(\$ 20,000+\$ 63,000)$
Cash Sales $=\$ 18,000$
Credit Sales $=\underline{\$ 65,000}$
(b) Accounts Receivable at December 31 is $\mathbf{\$ 1 0 , 0 0 0}$, as shown below:

| Accounts Receivable |  |  |  |
| :--- | ---: | :--- | ---: |
| Beg. Bal. | $\$ 24,000$ | Write-offs | 1,000 |
| Credit sales | 65,000 | Collections | 78,000 |
| End bal. | 10,000 |  |  |

## EXERCISE 9-15

(a) Beginning accounts receivable ............................................. \$ 100,000

Net credit sales........................................................................ 1,000,000
Cash collections $(900,000)$
Accounts written off
Ending accounts receivable $(30,000)$
$\$ 170,000$
(b) $\$ 1,000,000 /[(\$ 100,000+\$ 170,000) / 2]=\underline{7.41}$
(c) $365 / 7.41=49.3$ days

## SOLUTIONS TO PROBLEMS

## PROBLEM 9-1A

(a) 1. Accounts Receivable ..... 3,200,000Sales
$\qquad$
2. Sales Returns and Allowances

$\qquad$ ..... 50,000Accounts Receivable
$\qquad$50,000
3. Cash ..... 2,810,000
Accounts Receivable ..... 2,810,000
4. Allowance for Doubtful Accounts

$\qquad$
90,000 Accounts Receivable

$\qquad$ ..... 90,000
5. Accounts Receivable

$\qquad$ ..... 24,000
Allowance for Doubtful Accounts

$\qquad$ ..... 24,000
Cash ..... 24,000Accounts Receivable24,000
(b)

| Accounts Receivable |  |  |  |
| :--- | ---: | ---: | ---: |
| Bal. | 960,000 | $(2)$ | 50,000 |
| (1) | $3,200,000$ | $(3)$ | $2,810,000$ |
| (5) | 24,000 | $(4)$ | 90,000 |
|  |  | $(5)$ | 24,000 |
| Bal. | $1,210,000$ |  |  |


| Allowance for Doubtful Accounts |  |  |
| :--- | ---: | :--- | ---: |
| (4) 90,000 | Bal. | 80,000 |
|  | $(5)$ | 24,000 |
|  |  |  |
|  | Bal. | 14,000 |

## PROBLEM 9-1A (Continued)

(c) Balance before adjustment [see (b)]......................................... \$ 14,000 Balance needed............................................................................. 115,000
Adjustment required..................................................................... \$101,000
The journal entry would therefore be as follows:
Bad Debts Expense............................................. 101,000 Allowance for Doubtful Accounts 101,000
(d) $\frac{\$ 3,200,000-\$ 50,000}{(\$ 880,000+\$ 1,095,000) \div 2}=\frac{\$ 3,150,000}{\$ 987,500}=3.19$ times

## PROBLEM 9-2A

(a) $\$ 33,000$.
(b) $\$ 44,000(\$ 2,200,000 \times 2 \%)$.
(c) $\$ 46,500$ [(\$825,000 X 6\%) - \$3,000].
(d) $\$ 52,500[(\$ 825,000 \times 6 \%)+\$ 3,000]$.
(e) The weakness of the direct write-off method is two-fold. First, it does not match expenses with revenues. Second, the accounts receivable are not stated at cash realizable value at the balance sheet date.

## PROBLEM 9-3A

(a) Dec
(a) \& (b)

Bad Debts Expense

| Date | Explanation | Ref. | Debit | Credit |
| :--- | :--- | :---: | :---: | :---: |
| 2008 |  |  |  |  |
| Dec. 31 | Adjusting |  | 30,610 |  |

Allowance for Doubtful Accounts

| Date | Explanation | Ref. | Debit | Credit | Balance |
| :--- | :--- | :--- | :--- | :--- | :--- |
| 2008 |  |  |  |  |  |
| Dec. | 31 | Balance |  |  | 30,610 |
|  | 31 | Adjusting |  |  | 42,000 |
| 2009 |  |  | 1,000 |  |  |
| Mar. | 31 |  |  | 1,000 | 41,610 |
| May | 31 |  |  |  | 42,610 |

## (b)

Mar. 31 Allowance for Doubtful Accounts ............. 1,000
Accounts Receivable
(2)

May 31 Accounts Receivable
1,000
Allowance for Doubtful Accounts 1,000

31 Cash................................................................. 1,000
Accounts Receivable
1,000
(c)

2009
Dec. 31 Bad Debts Expense
Allowance for Doubtful Accounts
29,400 (\$28,600 + \$800)

## PROBLEM 9-4A

(a) Total estimated bad debts

|  |  | Number of Days Outstanding |  |  |  |  |  |
| :--- | :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Total | $0-30$ | $31-60$ | $61-90$ | $91-120$ | Over 120 |  |
| Accounts | $\$ 375,000$ | $\$ 220,000$ | $\$ 90,000$ | $\$ 40,000$ | $\$ 10,000$ | $\$ 15,000$ |  |
| receivable | $\$$ | $1 \%$ | $4 \%$ | $5 \%$ | $8 \%$ | $10 \%$ |  |
| $\%$ uncollectible |  |  |  |  |  |  |  |
| Estimated | $\$ 10,100$ | $\$ 2,200$ | $\$ 3,600$ | $\$ 2,000$ | $\$$ | 800 |  | $\mathbf{\$ 1 , 5 0 0}$| Bad debts |
| :--- |

(b) Bad Debts Expense ......................................................... 18,100

Allowance for Doubtful Accounts
18,100
(\$10,100 + \$8,000)
(c) Allowance for Doubtful Accounts

5,000
Accounts Receivable $\qquad$ 5,000
(d) Accounts Receivable ..................................................... 5,000

Allowance for Doubtful Accounts $\qquad$
Cash
5,000
Accounts Receivable
(e) If Wall Inc. used 3\% of total accounts receivable rather than aging the individual accounts the bad debt expense adjustment would be \$19,250 [(\$375,000 X 3\%) + \$8,000]. The rest of the entries would be the same as they were when aging the accounts receivable.

Aging the individual accounts rather than applying a percentage to the total accounts receivable should produce a more accurate allowance account and bad debts expense.

## PROBLEM 9-5A

(a) The allowance method. Since the balance in the allowance for doubtful accounts is given, they must be using this method because the account would not exist if they were using the direct write-off method.

## (b)

(1) Dec. 31 Bad Debts Expense
(\$11,750-\$2,000)
Allowance for Doubtful Accounts 9,750
(2) Dec. $31 \quad \begin{gathered}\text { Bad Debts Expense ............................. } \\ \text { (\$950,000 X 1\%) }\end{gathered}$ 9,500

Allowance for Doubtful Accounts

9,500
(c) (1) Dec. 31 Bad Debts Expense (\$11,750 + \$2,000)
Allowance for Doubtful
Accounts $\qquad$ 13,750
(2) Dec. 31 Bad Debts Expense

9,500
Allowance for Doubtful Accounts $\qquad$ 9,500
(d) Allowance for Doubtful Accounts

3,000
Accounts Receivable
3,000
Note: The entry is the same whether the amount of bad debts expense at the end of 2008 was estimated using the percentage of receivables or the percentage of sales method.
(e) Bad Debts Expense

3,000
Accounts Receivable.
(f) Allowance for Doubtful Accounts is a contra-asset account. It is subtracted from the gross amount of accounts receivable so that accounts receivable is reported at its cash realizable value.

## PROBLEM 9-6A

(a) Oct. 7 Accounts Receivable ..... 6,900
Sales

$\qquad$
12 Cash (\$900-\$27) ..... 873
Service Charge Expense ..... 27
(\$900 X 3\%)
Sales900
15 Accounts Receivable ..... 460
Interest Revenue ..... 460
15 Cash ..... 8,107
Notes Receivable ..... 8,000
Interest Receivable ..... 80
(\$8,000 X 8\% X 45/360)
Interest Revenue ..... 27(\$8,000 X 8\% X 15/360)
24 Accounts Receivable-Hughey ..... 9,150
Notes Receivable9,000
Interest Receivable ..... 90
(\$9,000 X 10\% X 36/360)
Interest Revenue60(\$9,000 X 10\% X 24/360)
31 Interest Receivable. ..... 120(\$16,000 X 9\% X 1/12)Interest Revenue120
(b)
Notes Receivable

| Date | Explanation | Ref. | Debit | Credit | Balance |  |
| :--- | ---: | :--- | :---: | :---: | :---: | ---: |
| Oct. | 1 | Balance | $\checkmark$ |  |  | 33,000 |
|  | 15 |  |  |  | 8,000 | 25,000 |
|  | 24 |  |  |  | 9,000 | 16,000 |


| Accounts Receivable |  |  |  |  |  |  |
| :--- | ---: | ---: | ---: | ---: | ---: | :---: |
| Date | Explanation | Ref. | Debit | Credit | Balance |  |
| Oct. | 7 |  | 6,900 |  | 6,900 |  |
|  | 15 |  | 460 |  | 7,360 |  |
|  | 24 |  |  | 9,150 |  |  |
|  |  |  |  |  |  |  |

Interest Receivable

| Date | Explanation | Ref. | Debit | Credit | Balance |  |
| :--- | :--- | :--- | :---: | :---: | ---: | ---: |
| Oct. | 1 | Balance | $\checkmark$ |  |  | 170 |
|  | 15 |  |  |  | 80 | 90 |
|  | 24 |  |  |  | 90 | 0 |
|  | 31 |  |  | 120 |  | 120 |

(c) Current assets

Notes receivable ...................................................................... \$16,000
Accounts receivable................................................................ 16,510
Interest receivable 120
Total receivables............................................................. \$32,630

## PROBLEM 9-7A

Jan. 5 Accounts Receivable-Dedonder Company ..... 20,000
Sales

$\qquad$ ..... 20,000
20 Notes Receivable. ..... 20,000Accounts Receivable-DedonderCompany20,000
Feb. 18 Notes Receivable ..... 8,000
Sales ..... 8,000
Apr. 20 Cash (\$20,000 + \$450) ..... 20,450
Notes Receivable ..... 20,000
Interest Revenue. ..... 450
(\$20,000 X 9\% X 3/12)
30 Cash (\$25,000 + \$1,000) ..... 26,000
Notes Receivable ..... 25,000
Interest Revenue. ..... 1,000
(\$25,000 X 12\% X 4/12)
May 25 Notes Receivable. ..... 4,000
Accounts Receivable-Jenks Inc. ..... 4,000
Aug. 18 Cash (\$8,000 + \$360) ..... 8,360Notes Receivable8,000
Interest Revenue ..... 360
(\$8,000 X 9\% X 6/12)
25 Accounts Receivable-Jenks Inc. ..... 4,070 (\$4,000 + \$70)
Notes Receivable ..... 4,000
Interest Revenue. ..... 70
(\$4,000 X 7\% X 3/12)
Sept. 1 Notes Receivable ..... 12,000
Sales ..... 12,000

## PROBLEM 9-1B

(a) 1. Accounts Receivable......................................... 2,570,000
Sales
2,570,000
2. Sales Returns and Allowances ...................... 40,000
Accounts Receivable.
40,000
3. Cash
2,300,000
Accounts Receivable.
2,300,000
4. Allowance for Doubtful Accounts
65,000
Accounts Receivable.
65,000
5. Accounts Receivable
25,000
Allowance for Doubtful Accounts.
25,000
Cash
Accounts Receivable.
25,000
25,000
(b)

Accounts Receivable

| Bal. | $1,000,000$ | $(2)$ | 40,000 |
| :--- | ---: | ---: | ---: |
| (1) | $2,570,000$ | $(3)$ | $2,300,000$ |
| $(5)$ | 25,000 | $(4)$ | 65,000 |
|  |  | $(5)$ | 25,000 |
| Bal. | $1,165,000$ |  |  |

Allowance for Doubtful Accounts

| (4) 65,000 | Bal. | 60,000 |
| :--- | :--- | :--- | :--- |
|  |  |  |
|  |  | 25,000 |
|  | Bal. | 20,000 |

(c) Balance before adjustment [see (b)]
\$20,000
Balance needed
90,000
Adjustment required
$\$ \mathbf{\$ 7 0 , 0 0 0}$
The journal entry would therefore be as follows:

> Bad Debts Expense................................................................000 Allowance for Doubtful Accounts
(d) $\frac{\$ 2,570,000-\$ 40,000}{(\$ 1,075,000+\$ 940,000) \div 2}=\frac{\$ 2,530,000}{\$ 1,007,500}=2.51$ times

## PROBLEM 9-2B

(a) $\$ 26,000$.
(b) $\$ 30,800(\$ 1,540,000 \times 2 \%)$.
(c) $\$ 22,000$ [(\$520,000 X 5\%) - \$4,000].
(d) $\$ 28,000[(\$ 520,000 \times 5 \%)+\$ 2,000]$.
(e) There are two major weaknesses with the direct write-off method. First, it does not match expenses with the associated revenues. Second, the accounts receivable are not stated at cash realizable value at the balance sheet date.

## PROBLEM 9-3B



## PROBLEM 9-4B

(a) Total estimated bad debts

|  |  | Number of Days Outstanding |  |  |  |  |
| :---: | :---: | :---: | :---: | :---: | :---: | :---: |
|  | Total | 0-30 | 31-60 | 61-90 | 91-120 | Over 120 |
| Accounts receivable | \$260,000 | \$100,000 | \$60,000 | \$50,000 | \$30,000 | \$20,000 |
| \% uncollectible |  | 1\% | 5\% | 7.5\% | 10\% | 15\% |
| Estimated Bad debts | \$ 13,750 | \$ 1,000 | \$ 3,000 | \$ 3,750 | \$ 3,000 | \$ 3,000 |

(b) Bad Debts Expense

Allowance for Doubtful Accounts
[\$13,750 - \$10,000]
(c) Allowance for Doubtful Accounts

2,000
Accounts Receivable
(d) Accounts Receivable ..................................................... 1,000

Allowance for Doubtful Accounts $\qquad$
Cash
1,000
Accounts Receivable 1,000
(e) When an allowance account is used, an adjusting journal entry is made at the end of each accounting period. This entry satisfies the matching principle by recording the bad debts expense in the period in which the sales occur.

## PROBLEM 9-5B

(a) (1) Dec. 31
Bad Debts Expense
16,050
(\$17,550-\$1,500)
Allowance for Doubtful Accounts $\qquad$ 16,050
(2) Dec. 31 Bad Debts Expense
17,000
(\$850,000 X 2\%)
Allowance for Doubtful
Accounts $\qquad$ 17,000
(b) (1) Dec. 31 Bad Debts Expense............................... 19,050
(\$17,550 + \$1,500)
Allowance for Doubtful
Accounts .................................. 19,050
(2) Dec. 31 Bad Debts Expense ............................... 17,000
Allowance for Doubtful
Accounts $\qquad$ 17,000


Note: The entry is the same whether the amount of bad debts expense at the end of 2008 was estimated using the percentage of receivables or the percentage of sales method.
(d) Bad Debts Expense 4,500
Accounts Receivable 4,500
(e) The advantages of the allowance method over the direct write-off method are:
(1) It attempts to match bad debts expense related to uncollectible accounts receivable with sales revenues on the income statement.
(2) It attempts to show the cash realizable value of the accounts receivable on the balance sheet.

## PROBLEM 9-6B

(a) July 5 Accounts Receivable

$\qquad$ ..... 6,200
Sales

$\qquad$ ..... 6,200
14 Cash (\$700-\$21). ..... 679
Service Charge Expense ..... 21(\$700 X 3\%)Sales700
14 Accounts Receivable ..... 440
Interest Revenue ..... 440
15 Cash ..... 6,100
Notes Receivable ..... 6,000
Interest Receivable ..... 75
(\$6,000 X 10\% X 45/360)
Interest Revenue ..... 25(\$6,000 X 10\% X 15/360)
25 Accounts Receivable ..... 25,375
Notes Receivable ..... 25,000
Interest Receivable ..... 225
(\$25,000 X 9\% X 36/360)Interest Revenue150(\$25,000 X 9\% X 24/360)
31 Interest Receivable ..... 100
(\$15,000 X 8\% X 1/12)
Interest Revenue100
(b)
Notes Receivable

| Date |  | Explanation | Ref. | Debit | Credit | Balance |
| :--- | ---: | :--- | :---: | :---: | :---: | ---: |
| July | 1 | Balance | $\checkmark$ |  |  | 46,000 |
|  | 15 |  |  |  | 6,000 | 40,000 |
|  | 25 |  |  |  | 25,000 | 15,000 |

Accounts Receivable

| Date | Explanation | Ref. | Debit | Credit | Balance |
| :--- | ---: | ---: | ---: | ---: | ---: |
| July | 5 |  | 6,200 |  | 6,200 |
|  | 14 |  | 440 |  | 6,640 |
|  | 25 |  |  | 25,375 |  |
|  |  |  |  |  |  |

Interest Receivable

| Date |  | Explanation | Ref. | Debit | Credit | Balance |
| :--- | ---: | :--- | :---: | :---: | ---: | ---: |
| July | 1 | Balance | $\checkmark$ |  |  | 300 |
|  | 15 |  |  |  | 75 | 225 |
|  | 25 |  |  | 100 |  | 0 |
|  | 31 | Adjusting |  |  |  | 100 |

(c) Current assets

Notes receivable ..................................................................... \$15,000
Accounts receivable 32,015
Interest receivable
100
Total receivables
\$47,115

## PROBLEM 9-7B

Jan. 5 Accounts Receivable-Klostermann Company ..... 6,300
Sales ..... 6,300
Feb. 2 Notes Receivable ..... 6,300
Accounts Receivable-Klostermann Company ..... 6,300
12 Notes Receivable ..... 7,800
Sales ..... 7,800
26 Accounts Receivable-Louk Co. ..... 4,000
Sales4,000
Apr. 5 Notes Receivable. ..... 4,000
Accounts Receivable-Louk Co. ..... 4,000
12 Cash (\$7,800 + \$130) ..... 7,930
Notes Receivable ..... 7,800
Interest Revenue. ..... 130
(\$7,800 X 10\% X 2/12)
June 2 Cash (\$6,300 + \$210) ..... 6,510
Notes Receivable ..... 6,300
Interest Revenue ..... 210
(\$6,300 X 10\% X 4/12)
July 5 Accounts Receivable-Louk Co. ..... 4,080
(\$4,000 + \$80)
Notes Receivable4,000
Interest Revenue ..... 80
(\$4,000 X 8\% X 3/12)
15 Notes Receivable ..... 7,000
Sales7,000
Oct. 15 Allowance for Doubtful Accounts ..... 7,000Notes Receivable7,000

## SEK COMPANY <br> Accounts Receivable Aging Schedule <br> May 31, 2008

|  | $\begin{gathered} \text { Proportion } \\ \text { of } \\ \text { Total } \\ \hline \end{gathered}$ | Amount in Category | Probability of NonCollection | Estimated Uncollectible Amount |
| :---: | :---: | :---: | :---: | :---: |
| Not yet due | . 620 | \$ 868,000 | . 02 | \$17,360 |
| Less than 30 days past due | . 200 | 280,000 | . 04 | 11,200 |
| 30 to 60 days past due | . 090 | 126,000 | . 06 | 7,560 |
| 61 to 120 days past due | . 050 | 70,000 | . 09 | 6,300 |
| 121 to 180 days past due | . 025 | 35,000 | . 25 | 8,750 |
| Over 180 days past due | . 015 | 21,000 | . 70 | 14,700 |
|  | 1.000 | \$1,400,000 |  | \$65,870 |

(b)

## SEK COMPANY Analysis of Allowance for Doubtful Accounts May 31, 2008

June 1, 2007 balance ..... \$ 29,500
Bad debts expense accrual (\$2,900,000 X .045) ..... 130,500
Balance before write-offs of bad accounts ..... 160,000
Write-offs of bad accounts ..... 102,000
Balance before year-end adjustment ..... 58,000
Estimated uncollectible amount ..... 65,870
Additional allowance needed ..... $\$ 7,870$
Bad Debts Expense. ..... 7,870 Allowance for Doubtful Accounts ............................ $\mathbf{7 , 8 7 0}$

## (c) 1. Steps to Improve the Accounts Receivable Situation

Establish more selective creditgranting policies, such as more restrictive credit requirements or more thorough credit investigations.

Establish a more rigorous collection policy either through external collection agencies or by its own personnel.

Charge interest on overdue accounts. Insist on cash on delivery (COD) or cash on order (coo) for new customers or poor credit risks.
2. Risks and Costs Involved

This policy could result in lost sales and increased costs of credit evaluation. The company may be all but forced to adhere to the prevailing credit-granting policies of the office equipment and supplies industry.

This policy may offend current customers and thus risk future sales. Increased collection costs could result from this policy.

This policy could result in lost sales and increased administrative costs.
(a) (1) Accounts receivable turnover ratio

PepsiCo
\$32,562
(\$2,999* + \$3,261) $\div 2$

$$
\text { *See note } 14
$$

$$
\frac{\$ 32,562}{\$ 3,130}=10.4 \text { times }
$$

(2) Average collection period

$$
\frac{365}{10.4}=35.1 \text { days } \quad \frac{365}{10.2}=35.8 \text { days }
$$

(b) Both companies have reasonable accounts receivable turnovers and collection periods of slightly greater than 30 days. This collection period probably approximates their credit terms that they provide to customers.

## (a) Benefits of Factoring Receivables

Factoring is a flexible financial solution that can help your business be more competitive while improving your cash flow, credit rating, and supplier discounts. Unlike traditional bank financing, factoring relies on the financial strength and credit worthiness of your customers, not you. You can use factoring services as much as you want or as little as you want. There are no obligations, no minimums, and no maximums. Here are the most common reasons businesses use factoring services:

Offer better terms to win more business. With factoring you can attract more business by offering better terms on your invoices. Most companies negotiate on price to win business in a competitive market, but with factoring you can negotiate with terms instead of price. To your customers, better terms can be more attractive than better prices. When using attractive terms to win business, you can build the cost of factoring into your costs of goods and services.

Example: A new customer may choose to do business with your company because you can offer NET 30 or NET 45 terms while your competitor (who isn't factoring) requires payment up front but has a $3 \%$ better price. If you factor the subsequent invoice at a discount of $3 \%$, you have leveraged factoring services to win the business at no extra cost and improved your cash flow at the same time.

Improve cash flow without additional debt. Eliminate long billing cycles. Receive cash for your outstanding invoices in 24 hours or less. No new debt is created. Factoring is not a loan. This allows you to preserve your financial leverage to take on new debt.

Customer Credit Services. Reduce bad debt expense, streamline credit approvals for new customers, improve decision-making on new business, and reduce administrative costs.

Accounts Receivable Management. Reduce administrative costs, improve customer relationships, improve receivable turns, improve accounting, and redirect critical resources to marketing and production.

Flexibility. Factor as much as you want or as little as you want. You decide. No obligations. No binding contracts. There are no minimums and no maximums in the amount you can factor. Funding is based on the strength of your customers.
(b) Factoring fees are based on a per Diem Rate. The factor will assess the risk of the particular situation and determine a discount rate. This usually ranges from $3 \%$ to $9 \%$ of the gross invoices sold, and is the fee for the duties the factor assumes and the cost of using their money. The sooner a receivable is paid, the lower the discount rate.
(c) Upon approval, the factor will advance the manufacturer 70\%-90\% of the total value of their invoices. This percentage is called the Advance Rate, and the cash is often delivered within $\mathbf{2 4}$ hours after an application is received.

The rest of the cash minus the factor's fees is then returned to the manufacturer as the receivables are collected. If the manufacturer's customers pay slowly, the discount rates that apply grow accordingly larger.
(a)

|  | 2008 | 2007 | 2006 |
| :---: | :---: | :---: | :---: |
| Net credit sales ......... | \$500,000 | \$600,000 | \$400,000 |

Credit and collection expenses
Collection agency fees $\qquad$
\$ 2,450 \$ 2,500 \$ 2,400

Salary of accounts receivable clerk

4,100
4,100
4,100
Uncollectible accounts $\qquad$

| 8,000 | 9,600 | 6,400 |
| ---: | ---: | ---: |
| 2,500 | 3,000 | 2,000 |
| 7500 | 900 | 600 |
| $\$ 17,800$ | $\$ 20,100$ | $\$ 15,500$ |

Total expenses as a percentage of net credit sales $\qquad$ 3.56\%
3.35\%
3.88\%
(b) Average accounts receivable (5\%)
$\$ 25,000$
\$ 30,000
$\$ 20,000$
Investment earnings (8\%)
$\$ \quad \mathbf{2 , 0 0 0}$
$\$ \quad 2,400$
\$ 1,600
Total credit and collection expenses per above

$$
\begin{array}{r}
\$ 17,800 \\
\hline 2,000 \\
\hline \$ 19,800 \\
\hline
\end{array}
$$

Add: Investment earnings* $\qquad$
Net credit and collection expenses $\qquad$

$$
\$ 20,100
$$

\$ 15,500
Billing and mailing costs. $\qquad$
\$ 17,800
\$ 20,100
15,500

Net expenses as a percentage of net credit sales $\qquad$ 3.96\%
3.75\%
4.28\%
*The investment earnings on the cash tied up in accounts receivable is an additional expense of continuing the existing credit policies.
(c) The analysis shows that the credit card fee of $4 \%$ of net credit sales will be higher than the percentage cost of credit and collection expenses in each year before considering the effect of earnings from other investment opportunities. However, after considering investment earnings, the credit card fee of $4 \%$ will be less than the company's percentage cost if annual net credit sales are less than $\$ 500,000$.

Finally, the decision hinges on: (1) the accuracy of the estimate of investment earnings, (2) the expected trend in credit sales, and (3) the effect the new policy will have on sales. Nonfinancial factors include the effects on customer relationships of the alternative credit policies and whether the Maynes want to continue with the problem of handling their own accounts receivable.

Of course, this solution will differ from student to student. Important factors to look for would be definitions of the methods, how they are similar and how they differ. Also, use of good sentence structure, correct spelling, etc.

Example:
Dear Rene,
The three methods you asked about are methods of dealing with uncollectible accounts receivable. Two of them, percentage-of-sales and percentage-ofreceivables, are "allowance" methods used to estimate the amount uncollectible. Under the percentage-of-sales basis, management establishes a percentage relationship between the amount of credit sales and expected losses from uncollectible accounts. This is based on past experience and anticipated credit policy. The percentage is then applied to either total credit sales or net credit sales of the current year. This basis of estimating emphasizes the matching of expenses with revenues.

Under the percentage-of-receivables basis, management establishes a percentage relationship between the amount of receivables and expected losses from uncollectible accounts. Customer accounts are classified by the length of time they have been unpaid. This basis emphasizes cash realizable value of receivables and is therefore deemed a "balance sheet" approach.

The direct write-off method does not estimate losses and an allowance account is not used. Instead, when an account is determined to be uncollectible, it is written off directly to Bad Debts Expense. Unless bad debt losses are insignificant, this method is not acceptable for financial reporting purposes.

Sincerely,
(a) The stakeholders in this situation are:

- The president of Ruiz Co.
- The controller of Ruiz Co.
- The stockholders.
(b) Yes. The controller is posed with an ethical dilemma-should he/she follow the president's "suggestion" and prepare misleading financial statements (understated net income) or should he/she attempt to stand up to and possibly anger the president by preparing a fair (realistic) income statement.
(c) Ruiz Co.'s growth rate should be a product of fair and accurate financial statements, not vice versa. That is, one should not prepare financial statements with the objective of achieving or sustaining a predetermined growth rate. The growth rate should be a product of management and operating results, not of creative accounting.


## BYP 9-7 <br> ALL ABOUT YOU ACTIVITY

(a) There are a number of sources that compare features of credit cards. Here are three: www.creditcards.com/, www.federalreserve.gov/pubs/shop/, and www.creditorweb.com/.
(b) Here are some of the features you should consider: annual percentage rate, credit limit, annual fees, billing and due dates, minimum payment, penalties and fees, premiums received (airlines miles, hotel discounts etc.), and cash rebates.
(c) Answer depends on present credit card and your personal situation.

