

ACCOUNTING FOR UNCOLLECTIBLE ACCOUNTS

Chapter 9

Assume the following data for Mega Company:

Sales:	
Credit Sales	\$300,000
Cash Sales	<u>200,000</u>
Total	<u>\$500,000</u>
Accounts Receivable, end of year:	\$60,000
Allowance for uncollectible accounts, before adjusting entry (credit balance)	\$800

ADJUSTING ENTRIES AND CALCULATIONS UNDER THE VARIOUS METHODS

- a. Income Statement Approach (Percentage of Sales).** Past experience indicates that 1% of credit sales will prove to be uncollectible.

Bad Debts Expense	3,000	
Allowance for Doubtful Accounts		3,000
Calculation: Credit Sales = \$300,000 X .01 (1% of credit sales uncollectible)		

- b. Balance Sheet Approach--Percentage of Receivables.** Past experience indicates that 6% of the year-end accounts receivable will prove to be uncollectible.

Bad Debts Expense	2,800	
Allowance for Doubtful Accounts		2,800
Calculation: Desired credit balance in allowance = 6% of year-end A/R (\$60,000 X .06 = 3,600) less credit balance in allowance before adjustment(\$3,600 – 800).		

- c. Balance Sheet Approach--Aging of Receivables.** First, each individual account is aged to determine how long it has been outstanding. Second, an estimated loss percentage is developed for each age category based on past experience and the advice of the credit department. An Accounts Receivable Aging for Mega Company is shown below.

	Balance Dec 31	Under 30 days	31 - 60 days	61 - 90 days	Over 90 days
Aaron	\$10,000		\$10,000		
Blue	1,400			\$900	\$500
Farley	17,600	15,000		2,100	500
Jacobs	31,000	30,000		1,000	
Totals	<u>\$60,000</u>	<u>\$45,000</u>	<u>\$10,000</u>	<u>\$4,000</u>	<u>\$1,000</u>
Estimated Uncollectible %		4%	7%	15%	40%
Est. Uncollectible Amount		\$1,800	\$700	\$600	\$400
Total Uncollectible	<u>\$3,500</u>				

Bad Debts Expense	2,700	
Allowance for Doubtful Accounts		2,700
Calculation: Desired credit balance in allowance account (\$3,500) less credit balance in allowance before adjustment (\$800).		