Cash and Cash Equivalents

1. **Cash** = coin and currency on hand, checks and money orders from customers, and deposits in checking accounts.
2. **Cash Equivalents** = investments, such as certificates of deposit and U.S. Treasury notes, that have a term of less than 90 days.

Accounts Receivable

Accounts Receivable are short-term liquid assets that represent payment due from credit customers.
Uncollectible Accounts (bad debts) are credit accounts that are not paid and are an expense of selling on credit. Companies offer credit sales knowing some customers may not pay because the net effect of the offering is increased sales/profit.

Recognizing Uncollectible Accounts

1. Direct Charge-off Method --loss is recognized at the time it is determined to be uncollectible with this journal entry:

DEBIT: Bad Debts Expense
CREDIT: Accounts Receivable

This method DOES NOT match revenues and expenses.

2. Allowance Method --An estimate of uncollectible accounts is made at the end of the accounting period. Then an adjusting entry is made:
DEBIT: Bad Debts Expense
CREDIT: Allowance for Uncollectible Accounts

Methods of Estimation for Uncollectible Accounts Expense

1. Percentage of Sales Method --the estimated percentage for bad debts is multiplied by net sales for the period. The product is then used in the adjusting entry for uncollectible accounts. The balance in the Allowance for Uncollectible Accounts has NO bearing on the adjusting entry.
2. Percentage of Accounts Receivable Method -- the estimated percentage for bad debts is multiplied by accounts receivable for the period. The product represents the desired balance in the allowance for uncollectible accounts account. The credit amount needed to achieve that desired balance is the amount of the adjustment.
3. Accounts Receivable Aging Method --Customers are placed in distinct categories. The amounts in each category are totaled and each total is multiplied by a different percentage for estimated bad debts. The sum of these products represents estimated bad debts in ENDING Accounts Receivable. The expense journal entry is for the amount needed to bring Allowance for Uncollectible Accounts to the amount calculated in the aging calculation.

Remember:
*Allowing sales on account increases sales

*Some accounts receivable will not be collectible

*Uncollected accounts receivable must be recorded as an *expense* in the period in which the revenue from the sale was made.

Writing off a customer
Under the allowance method, when a customer who is not going to pay has been *identified*, the customer is written out of the books by closing his/her account. This is done in the general journal with a:

debit to: Allowance For Uncollectible Accounts
credit to: Accounts Receivable/customer name

*Remember that the credit must be posted to two places: the accounts receivable account in the general ledger AND the customer's accounts receivable account in the subsidiary accounts receivable ledger.

*Note that the book value of accounts receivable (accounts receivable - allowance for uncollectible accounts) does NOT change.
After a specific amount is written off, Accounts Receivable and Allowance for Uncollectible Accounts decrease by the same amount, but the net figure for expected receivables stays the same.

Reinstating a written-off account -When a customer whose account has been written off pays in part or in full, two entries must be made:

DEBIT: Accounts Receivable
CREDIT: Allowance for Uncollectible Accounts

DEBIT: Cash
CREDIT: Accounts Receivable

Promissory Notes
A **Promissory Note** is a written promise to pay a definite sum of money on demand at a future date. The person who signs the note and thereby promises to pay is called the **maker**. The person to whom the money is owed is called the **payee**. The payee records short or long-term notes receivable and the maker records short or long-term notes payable.

The **maturity date** is the date payment is due.

Interest is the cost of borrowing money for the borrower and the reward of lending money for the lender.

Principal is the amount of money borrowed or loaned.

The **Interest Rate** is the annual charge for borrowing and is expressed as a percentage.
Interest is computed as follows:
Interest = Principle x Interest Rate x Time (where time is stated in terms of years)

The **Maturity Value** of an interest-bearing note is the face value of the note (principal) plus interest.

Notes Receivable Journal Entries

1. Receipt of a note:
DEBIT: Notes Receivable
CREDIT: Accounts Receivable
Or
DEBIT: Notes Receivable
CREDIT: Cash

2. Collection on a note:
DEBIT: Cash (for the maturity value)
CREDIT: Notes Receivable (for the face value)
CREDIT: Interest Income

3. Recording of a Dishonored Note:
DEBIT: Accounts Receivable (for Maturity Value)
CREDIT: Notes Receivable
CREDIT: Interest Income

4 . Recording Adjusting Entries (accrued interest)
DEBIT: Interest Receivable
CREDIT: Interest Earned
5. Recording Receipt of Maturity value after adjustment
DEBIT: Cash
CREDIT: Interest Receivable
CREDIT: Interest Earned
CREDIT: Notes Receivable