I. Introduction
   A. Continuing to focus on “liquid” assets.
   B. Continuing our analysis of “current asset” section of Balance Sheet

II. Accounting for Receivables.
   A. Have you ever bought something on credit? Why do businesses sell on credit?
   B. Common classifications for receivables
      1. Accounts
      2. Notes
      3. Other
   C. Trade receivables--notes and accounts receivable which arise from sales transactions.

III. Accounts Receivable
   A. Arises from sales on credit to customers
      1. Includes amounts due from non-bank credit cards.
   B. Unfortunately, a business will not be able to collect 100% of sales on credit
      1. Credit is a sales tool -- may stimulate sales
   C. Uncollectible accounts receivable (bad debts) represents an expense
   D. Methods of accounting for uncollectibles (bad debts)
      1. Direct write off method
         a. Account is written off and expense recorded only when the account is deemed uncollectible
            
            Bad Debts (Uncollectible accounts) Expense      XX
            Accounts receivable - Jane Jones        XX

            b. No matching of the expense with revenue
            c. Doesn’t show accounts receivable at net realizable value

      2. Allowance method
         a. Involves estimating portion of account receivable which is uncollectible and recording expense
b. Accomplishes two things
   (1) Matches bad debt expense with revenue
   (2) Shows receivables at net realizable value

c. Two ways to estimate uncollectibles
   (1) Based on a percentage of net sales (income statement approach)
      (a) Percentage based on historical average
      (b) Multiply percentage by net sales (possibly credit sales)
      (c) Amount calculated is amount used in adjusting journal entry
   (2) Based on aging of accounts receivable (balance sheet approach)
      (a) See aging schedule page 317
      (b) Amount determined represents balance you want in allowance account!!!
         i) So adjusting journal entry **must** consider what is there
   (3) Simplified balance sheet approach. Take a percentage of ending accounts
       receivable for estimate of allowance needed.

d. Write-off of a specific account
   Allowance for Doubtful Accounts     XX
   Accounts receivable -Jane Jones      XX
   (1) Note -- expense account unaffected
   (2) Net amount of receivables is unchanged

e. What if customer pays after written off?
   (1) Two entries required
      (a) Reinstall the receivable
      (b) Record collection

E. Must use allowance method if bad debts are "material"

F. Disposition of Accounts Receivable
   1. Collection in normal course of business -- we are already familiar with required entry
   2. Sale of accounts receivable may be to a factor (finance company or bank) that buys the
      receivables from businesses for a fee and then collects the remittances directly from the
      customers
   3. Borrow using accounts receivable as collateral. (Not a disposition, but get cash)
IV. Notes Receivable
A. Definition and characteristics
   1. Unconditional promise (in writing) to pay a definite sum of money on demand or at a fixed date
   2. Parties to note
      a. Maker
      b. Payee

B. Accounting for notes receivable
   1. At issuance
      Notes Receivable XXX (at face value)
      Sales or XXX
      Accounts Receivable

   2. Determination of maturity date and maturity value
      a. Interest accrues on a daily basis
      b. Start counting day AFTER note
      c. Include date note is due
         (1) Notes with life expressed in months

      d. Principal X Rate X Time = Interest
         (1) Book uses a 360 day year (not as common anymore)
         (2) Often requires an adjusting entry at year-end to reflect interest.

      e. Maturity value = Principal + Interest

   3. At the end of an accounting period an adjusting entry to record interest earned will likely be necessary.
      Interest receivable XX
      Interest revenue XX

C. “Discounting” note at bank to get immediate cash
   1. Steps in computing discount and proceeds
      a. Compute the maturity value
      b. Compute the bank discount
         (Maturity value X Bank discount rate X Discount period)

      c. Maturity value - bank discount = proceeds

   2. If proceeds > face of note
      a. Excess is interest revenue (assumes with recourse)

   3. If proceeds < face of note
      a. Excess is interest expense (assumes with recourse)

   4. Discounted note is a contingent liability -- disclose
D. If note is dishonored (not paid at maturity) but collection is expected --
   Accounts receivable -- customer XX
   Notes receivable XX
   Interest revenue XX

V. Financial Statement Analysis

A. Accounts receivable turnover--how frequently are we collecting the receivables.

   Net Sales
   ----------------
   Average A/R

B. Number of days sales in receivable--how long does it take to collect receivables.

   A/R, end of year   sometimes
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   Average daily sales on account
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   A/R Turnover