ACC 300 · SESSION 15

Cash and trade receivables

Measure customer claims, evaluate collection evidence, and reconcile the allowance.



Side Quest sells on credit

SIDE QUEST

GAMES

BUSINESS

Supplies independent game stores and regional retailers

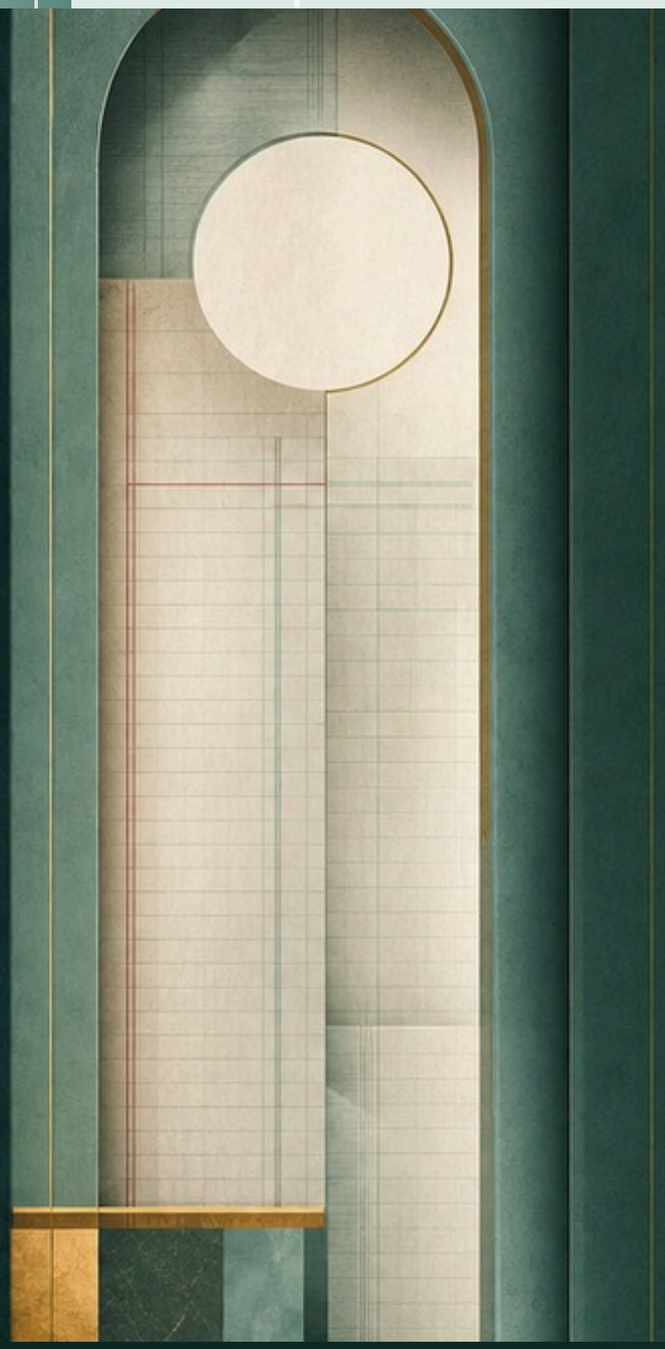
CASE PERIOD

October through December 2026

UNITS

US dollars

Track customer claims from sale through collection, then estimate credit losses on the unpaid balances.



Measure the sale price

Separate the invoice amount from the consideration the seller expects to receive.

Discounts change the agreed price

Trade discount

- Reduces the catalog price.
- Record the discounted price.

Settlement discount

- Rewards early payment.
- Estimate whether the customer will pay in time when measuring revenue.
- An expected settlement discount is variable consideration. Include the estimated consideration only when it is probable that resolving the payment uncertainty will not require a significant revenue reversal.

Receivable measurement: trade and settlement discounts

WALKTHROUGH

SALE

Side Quest delivers 200 games to Checkpoint on November 5.

The catalog price is $30 per game.

TRADE DISCOUNT

Side Quest grants a 20% discount from the catalog price.

PAYMENT TERMS

Payment by November 15 earns a further 2% discount.

Otherwise, payment is due December 5.

EXPECTED PAYMENT

Side Quest expects Checkpoint to pay by November 15, based on its payment history and confirmed payment plan.

Calculate the receivable and sales revenue Side Quest should record on November 5. Prepare the sales entry.

Calculate the expected consideration

WALKTHROUGH

Side Quest | November 5, 2026 | Checkpoint | Invoice SQ01

CATALOG TOTAL

200 games × $30/game = **$6,000**

INVOICE AFTER TRADE DISCOUNT

$6,000 − ($6,000 × 20%) = **$4,800**

EXPECTED SETTLEMENT DISCOUNT

$4,800 × 2% = **$96**

RECEIVABLE AND REVENUE

$4,800 − $96 = **$4,704**

SALES ENTRY

Account	Debit	Credit
Accounts Receivable	$4,704	
Sales Revenue		$4,704

Which payment evidence governs the sale?

iClicker | Question 1 of 5

Side Quest delivers games to a customer that usually earns the early-payment discount. For this sale, Side Quest expects the customer to pay after the discount deadline but before the invoice is due. No credit loss is expected. What receivable and revenue should Side Quest record?

A Use the discounted price because the retailer usually pays early.

B Use the discounted price and expense the difference.

C Record the full invoice as receivable and revenue.

D Record the full receivable but discounted revenue.

E Wait to record revenue until the retailer pays.

Which payment evidence governs the sale?: answer

iClicker | Answer 1 of 5

Correct answer: C.

Side Quest delivers games to a customer that usually earns the early-payment discount. For this sale, Side Quest expects the customer to pay after the discount deadline but before the invoice is due. No credit loss is expected. What receivable and revenue should Side Quest record?

A **Use the discounted price because the retailer usually pays early.**
Incorrect. The current payment schedule is stronger evidence for this order than the usual payment pattern.

B **Use the discounted price and expense the difference.**
Incorrect. The expected payment is the full price; no discount expense arises.

C **Record the full invoice as receivable and revenue.**
Correct. The expected payment falls outside the discount period, so the seller expects the full invoice price.

D **Record the full receivable but discounted revenue.**
Incorrect. No expected discount or other adjustment explains a difference between the receivable and revenue.

E **Wait to record revenue until the retailer pays.**
Incorrect. Payment timing does not postpone revenue for the delivered goods.

Collection or an expired discount

WALKTHROUGH

Side Quest delivered 200 games on November 5 at $30/game, less a 20% trade discount. Invoice: $4,800.

Payment by November 15 earns 2% × $4,800 = $96. Side Quest recorded $4,704, expecting early payment.

November 12: customer pays

Checkpoint pays $4,704 within the discount period. Record the cash and remove the receivable.

Account	Debit	Credit
Cash	$4,704	
Accounts Receivable		$4,704

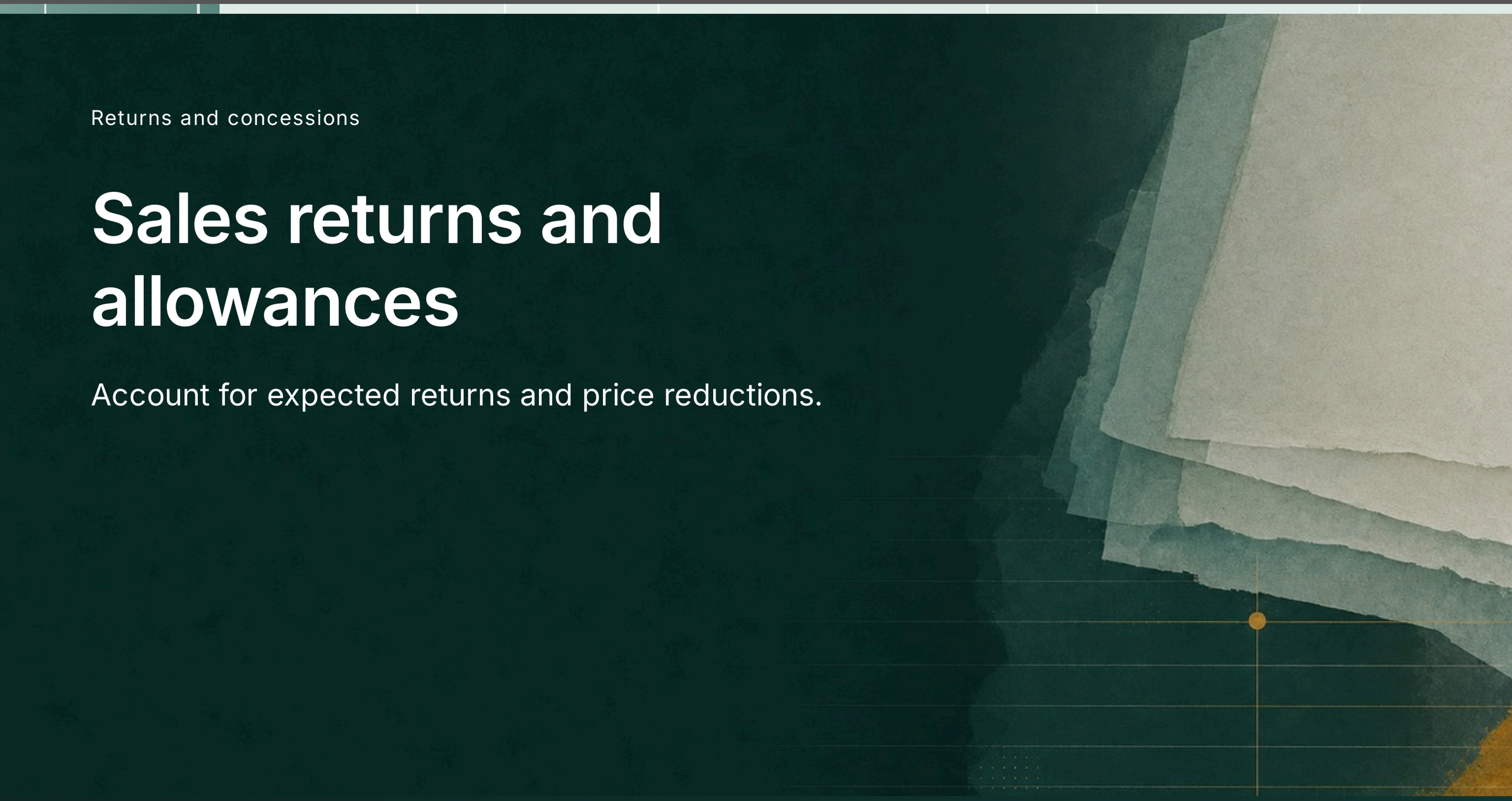
November 16: discount expires

Instead, assume Checkpoint has not paid. Restore the expired $96 discount to the receivable and revenue.

Account	Debit	Credit
Accounts Receivable	$96	
Sales Revenue		$96

Sales returns and allowances

Account for expected returns and price reductions.



Sales returns and allowances: what changes?

SALES RETURN

Returns the goods

The customer receives a refund or credit.

REVENUE

Reduce revenue for the refund or credit.

INVENTORY

Account for the goods recovered.

SALES ALLOWANCE

Keeps the goods

The customer receives a price reduction.

REVENUE

Reduce revenue for the price reduction.

INVENTORY

No goods return; no inventory recovery.

AT THE SALE DATE

Estimate expected returns when recording the sale.

Account for expected refunds and inventory recovery

Record the expected effects at the sale date, before customers return any goods.

REVENUE

Exclude expected refunds

RECEIVABLE

Record the full invoice amount the customer owes.

REFUND LIABILITY

Record the amount expected to be refunded or credited. Exclude that amount from revenue.

INVENTORY COST

Recognize expected recovery

INVENTORY

Remove the cost of all goods delivered.

RETURN RECOVERY ASSET

Record the cost of goods expected back, less recovery costs and expected value declines. This asset reduces cost of goods sold.

Table Talk may return unopened games

WALKTHROUGH

SALE

On November 10, Side Quest delivers 100 games at $40 each.

RETURN RIGHT

Table Talk owes the full invoice, due December 10, but may return unopened games through November 30.

EXPECTED RETURNS

Side Quest expects 10 returns. Each game cost $20; recovery will cost $2 per returned game.

Assume no value decline, discount, or credit loss. We will reduce revenue for the expected 10% returns. It is probable that actual returns will not significantly exceed that estimate, so a significant further reduction in revenue is unlikely.

FIRST: SALES ENTRY

Calculate the receivable, refund liability, and revenue. Record the sales entry.

THEN: INVENTORY ENTRY

Calculate the recovery asset and cost of goods sold. Record the inventory entry.

Record revenue and expected refunds

WALKTHROUGH

Side Quest | November 10, 2026 | Table Talk

RECEIVABLE

Games sold × price per game

100 games × $40/game = **$4,000**

REFUND LIABILITY

Expected returns × refund per game

10 games × $40/game = **$400**

REVENUE

Receivable − refund liability

= $4,000 − $400 = **$3,600**

SALES ENTRY

Table Talk owes the full invoice; the refund liability covers expected returns.

Account	Debit	Credit
Accounts Receivable	$4,000	
Sales Revenue		$3,600
Refund Liability		$400

Record inventory cost and expected recovery

WALKTHROUGH

Side Quest | November 10, 2026 | No expected value decline

INVENTORY COST

Games sold × cost per game

100 games × $20/game = **$2,000**

RECOVERY ASSET

Expected returns × (unit cost − recovery cost)

10 games × ($20/game − $2/game) = **$180**

COST OF GOODS SOLD

Inventory cost − recovery asset

= $2,000 − $180 = **$1,820**

INVENTORY ENTRY

The recovery asset excludes the cost of recovering the returned games.

Account	Debit	Credit
Cost of Goods Sold	$1,820	
Return Recovery Asset	$180	
Inventory		$2,000

Settle the actual return

WALKTHROUGH

On November 25, Table Talk returns exactly the expected 10 games. Credit: $40/game. Inventory cost: $20/game. Recovery costs equal the estimate of $2/game.

NOVEMBER 25: CREDIT THE CUSTOMER

10 games × $40/game = $400

Account	Debit	Credit
Refund Liability	$400	
Accounts Receivable		$400

NOVEMBER 25: RECOVER INVENTORY

10 games × ($20 − $2)/game = $180 recovery asset

Account	Debit	Credit
Inventory	$200	
Return Recovery Asset		$180
Cash		$20

DECEMBER 5: COLLECT THE BALANCE

Table Talk pays the remaining $3,600. No additional revenue reduction is needed.

Account	Debit	Credit
Cash	$3,600	
Accounts Receivable		$3,600

Sales allowance for retained goods

WALKTHROUGH

Side Quest | December 18, 2026 | Game Circuit | Invoice SQ06

WHAT HAPPENED

Game Circuit owes $12,000 on invoice SQ06 for games purchased on credit. It reports cosmetic box damage.

Side Quest grants a $1,000 price reduction. Game Circuit keeps the games.

RECORD THE ALLOWANCE

Account	Debit	Credit
Sales Allowances	$1,000	
Accounts Receivable		$1,000

REVENUE EFFECT

The Sales Allowances account reduces revenue.

RECEIVABLE AFTER THE ALLOWANCE

$12,000 − $1,000 = $11,000

Do both customer credits reduce revenue?

iClicker | Question 2 of 5

A customer returns goods. The seller had already included that return in its refund liability and now credits the unpaid invoice. It also grants another customer a new price reduction for damaged goods the customer keeps. Which treatment fits the customer credits? Ignore inventory entries.

A Debit Refund Liability for the return; Sales Allowances for the price reduction.

B Debit Sales Allowances for both credits.

C Debit Refund Liability for both credits.

D Debit Sales Allowances for the return; Refund Liability for the price reduction.

E Debit Accounts Receivable for both credits.

Do both customer credits reduce revenue?: answer

iClicker | Answer 2 of 5

Correct answer: A.

A customer returns goods. The seller had already included that return in its refund liability and now credits the unpaid invoice. It also grants another customer a new price reduction for damaged goods the customer keeps. Which treatment fits the customer credits? Ignore inventory entries.

A **Debit Refund Liability for the return; Sales Allowances for the price reduction.**
Correct. The actual return settles the refund liability recorded earlier. The new price reduction reduces revenue through Sales Allowances.

B **Debit Sales Allowances for both credits.**
Incorrect. Revenue already excludes the expected return. Reducing it again would count that return twice.

C **Debit Refund Liability for both credits.**
Incorrect. The existing refund liability covers the returned goods, not the new price reduction.

D **Debit Sales Allowances for the return; Refund Liability for the price reduction.**
Incorrect. The proposed debits reverse the treatments required by the facts.

E **Debit Accounts Receivable for both credits.**
Incorrect. Both customer credits reduce the unpaid claims, so the seller credits Accounts Receivable.

Receivables and the credit loss allowance

Track collections, write-offs, and recoveries before estimating what remains uncollectible.



Why will the customer pay less?

Price reduction

The seller accepts a lower price through a return or price concession.

The reduction affects revenue.

Credit loss

The customer still owes the agreed amount, but the seller expects to collect less.

The shortfall is a credit loss.

BEFORE CHOOSING THE TREATMENT

Investigate contract terms and expected concessions. Financial difficulty alone does not settle which treatment applies.

The allowance reduces reported receivables

Gross receivables	−	Allowance for credit losses	=	Net receivables
Amounts customers still owe.		Estimated amounts the seller will not collect.		The amount expected to be collected.

Estimate expected losses

Estimate nonpayment over the remaining contractual lives, including invoices not yet due.

Adjust the allowance through credit loss expense.

Write off a specific claim

Remove an amount the seller considers uncollectible. Reassess the remaining allowance separately.

Reduce receivables and the allowance together.

Determine the year-end credit loss adjustment

Step 1 · Establish recorded balances

Post customer activity. Find gross receivables and the allowance already recorded.

Step 2 · Estimate expected credit losses

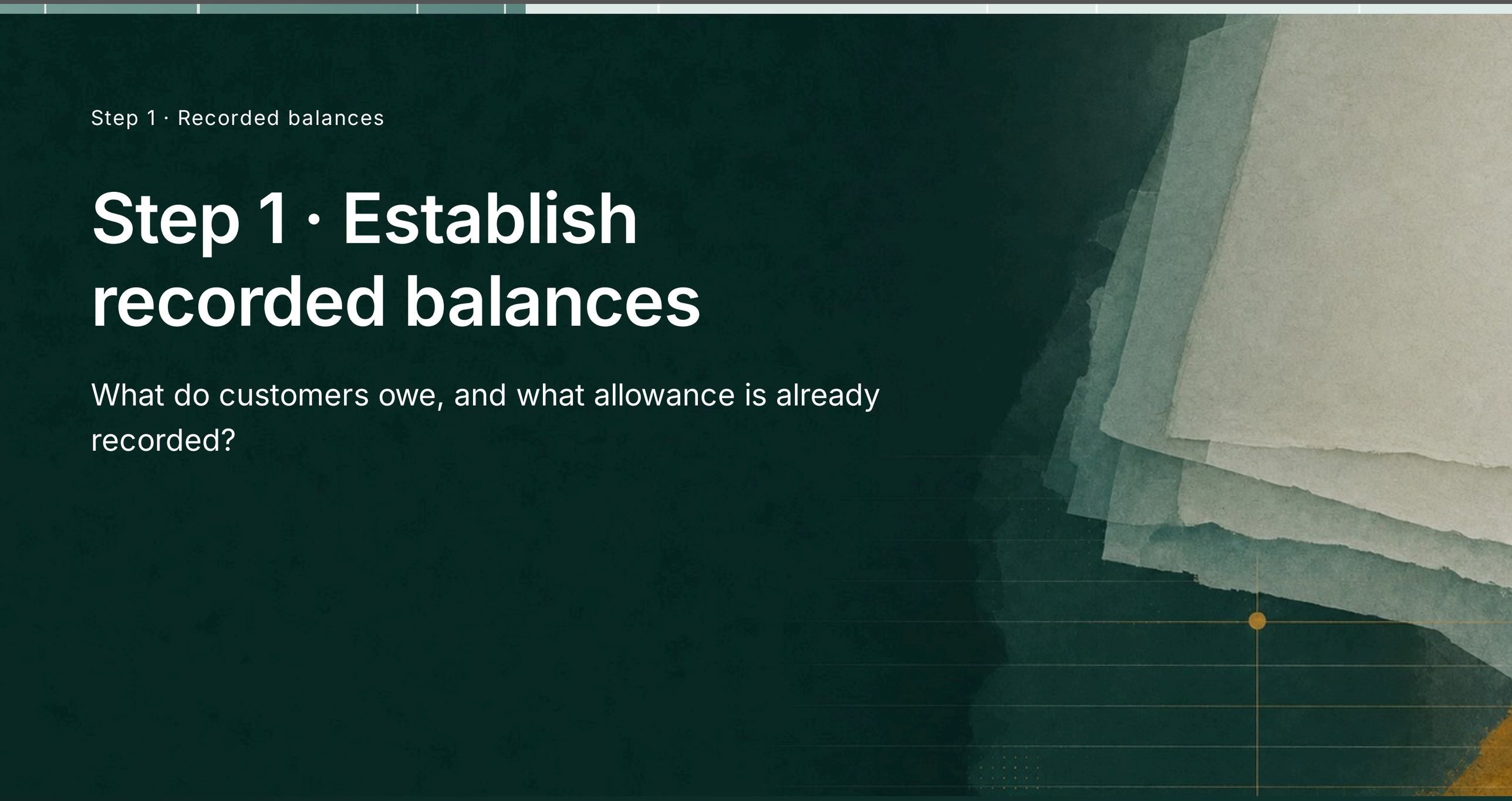
Evaluate unpaid receivables to determine the required allowance.

Step 3 · Record the allowance adjustment

Compare the required allowance with the recorded balance. Record the difference.

Step 1 · Establish recorded balances

What do customers owe, and what allowance is already recorded?



Resolve the opening customer claims

WALKTHROUGH

Side Quest | Quarter beginning October 1, 2026 | US dollars

OPENING CLAIMS AND COLLECTIONS

Customer	Opening claim	Collection	Remaining claim
Checkpoint	$12,000	$12,000 on October 15	None
Old Oak	$8,000	$6,500 on October 20	$1,500

Opening gross receivables total $20,000. The opening credit allowance is $1,200.

On October 31, Side Quest considers Old Oak's remaining claim uncollectible.

WRITE OFF THE CLAIM

Account	Debit	Credit
Allowance for Credit Losses	$1,500	
Accounts Receivable		$1,500

USE THE EXISTING ALLOWANCE

The write-off uses the allowance already recorded. It does not create another expense.

No expense adjustment has been recorded this quarter.

EFFECT ON NET RECEIVABLES

Gross receivables and the allowance fall equally. **Net receivables stay unchanged.**

Does a write-off reduce net receivables?

iClicker | Question 3 of 5

Growing Concern writes off a customer's $600 balance. A manager says, "That means our reported net receivables just fell by $600." No other entries are made. Is the manager correct?

A Yes. Any decrease in Accounts Receivable reduces net receivables.

B Yes. The write-off creates another $600 of credit loss expense.

C No. The write-off reduces revenue instead.

D No. Net receivables increase because the allowance decreases.

E No. Net receivables are unchanged.

Does a write-off reduce net receivables?: answer

iClicker | Answer 3 of 5 — **Correct answer: E.**

Growing Concern writes off a customer's $600 balance. A manager says, "That means our reported net receivables just fell by $600." No other entries are made. Is the manager correct?

A **Yes. Any decrease in Accounts Receivable reduces net receivables.**
Incorrect. This ignores the equal decrease in the allowance.

B **Yes. The write-off creates another $600 of credit loss expense.**
Incorrect. The write-off uses the allowance; it does not record another expense.

C **No. The write-off reduces revenue instead.**
Incorrect. Writing off an uncollectible claim does not change the sale price or revenue.

D **No. Net receivables increase because the allowance decreases.**
Incorrect. Accounts Receivable decreases by the same amount as the allowance.

E **No. Net receivables are unchanged.**
Correct. Accounts Receivable and the allowance both decrease by $600. The two decreases offset.

Collect a previously written-off claim

WALKTHROUGH

Replay unexpectedly pays $400 on November 20. Its claim was written off before October 1 and is absent from opening receivables.

FIRST

Reinstate the claim

Increase gross receivables and the allowance equally.

Account	Debit	Credit
Accounts Receivable	$400	
Allowance for Credit Losses		$400

THEN

Record collection

Replace the reinstated receivable with cash.

Account	Debit	Credit
Cash	$400	
Accounts Receivable		$400

REVENUE EFFECT

Neither entry creates sales revenue.

Reconcile the customer claims

WALKTHROUGH

Side Quest | October–December 2026 | Accounts Receivable

Find the claims still owed at year-end. The unpaid customer balances in the aging schedule should add up to the $55,000 Accounts Receivable balance.

Accounts Receivable

DEBIT		CREDIT	
Opening claims	$20,000		
New receivable debits	$66,704		
		$1,400	Return and sales allowance
		$28,804	Collections excluding Replay
		$1,500	Old Oak write-off
Replay reinstatement	$400		
		$400	Replay collection
Ending gross receivables	$55,000		

Find the recorded allowance

WALKTHROUGH

Side Quest | Before the year-end estimate

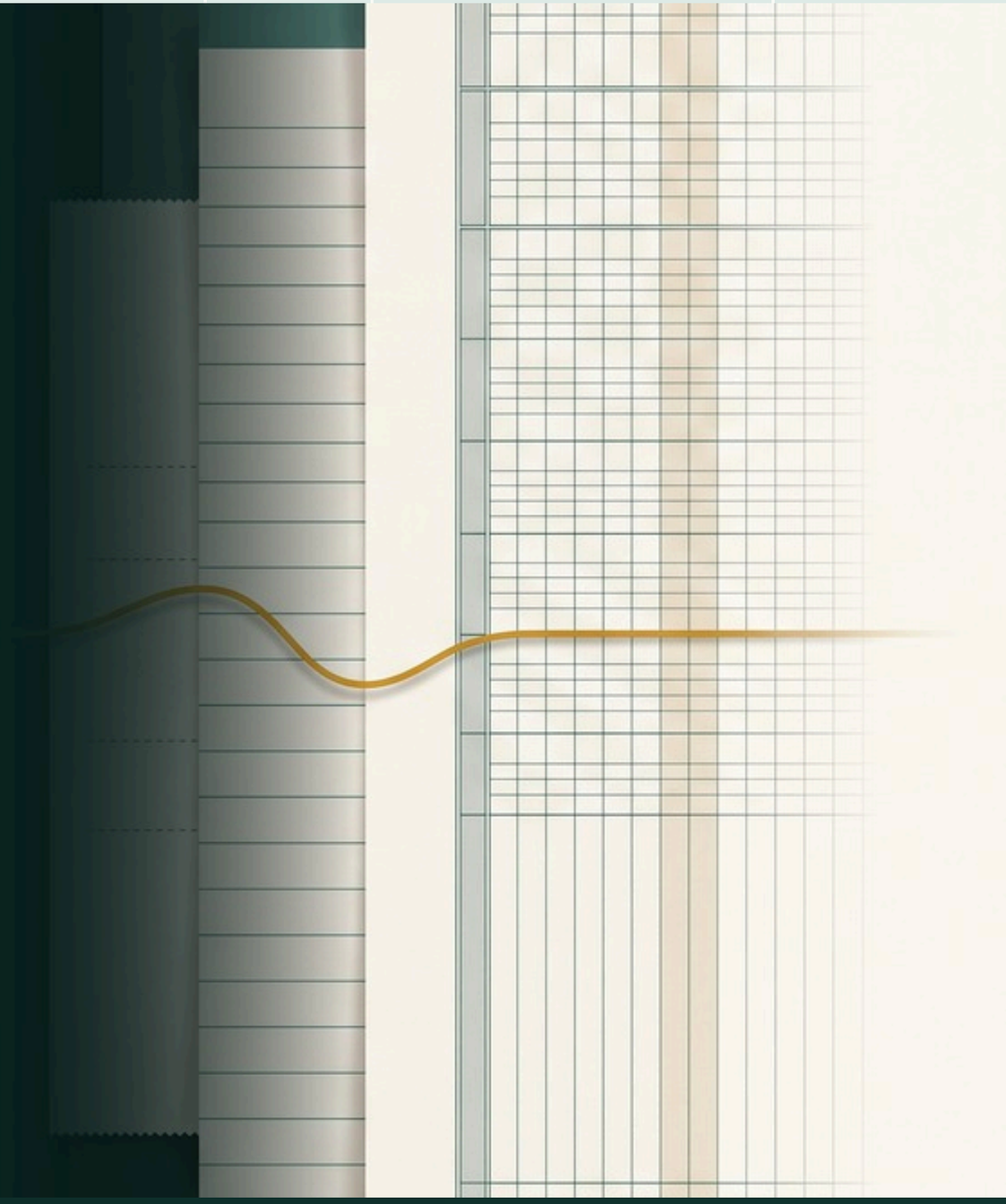
Allowance for Credit Losses

DEBIT		CREDIT	
		$1,200	Opening balance
Old Oak write-off	**$1,500**		
		$400	Replay reinstatement
		$100	Unadjusted credit balance
		?	Adjusting entry
		?	Required ending balance

Next, estimate credit losses on the remaining receivables. Compare the required allowance with this **$100 credit balance** to calculate the adjustment.

Step 2 · Estimate expected credit losses

Use the unpaid customer balances to estimate the required allowance.



An aging schedule groups unpaid receivables

An **aging schedule** lists unpaid receivables by how long they are past due. It helps the seller compare collection risk across payment groups.

Days past due

- Count from the payment due date to the reporting date.
- Payment not yet due: current.
- Group overdue invoices into ranges suited to the receivables. For example: 1–30, 31–60, or over 60 days past due.

Amount in each group

- Find each invoice's unpaid balance after recorded credits and collections.
- Add the unpaid balances within each payment-status group.
- The groups must total gross Accounts Receivable. Keep the allowance separate.

Calculate these unpaid balances

YOUR TURN

> Take a few minutes to work through this on your own or with those around you.

Side Quest | Reporting date: December 31, 2026

Invoice	Due date	Original claim	Recorded collection
SQ03, Critical Hit	January 9, 2027	$14,000	None
SQ04, Table Talk	December 20, 2026	$10,000	$2,000
SQ05, Dice & Co.	November 25, 2026	$6,000	None

No credits or discounts remain for these invoices. The company has recorded the $2,000 partial collection shown for SQ04.

Find each unpaid amount and its days past due.

Use the contractual due dates

WALKTHROUGH

Side Quest | Reporting date: December 31, 2026

Invoice	Due date	Unpaid amount	Days past due	Aging group
SQ03, Critical Hit	January 9, 2027	$14,000	0	Current
SQ04, Table Talk	December 20, 2026	$10,000 − $2,000 = $8,000	11	1-30 days
SQ05, Dice & Co.	November 25, 2026	$6,000	36	31-60 days

SQ03 is not yet due. For SQ04 and SQ05, count elapsed days from each due date through December 31.

Group receivables by shared collection risk

SHARED RISK

- A pool contains receivables with similar collection risks.
- Compare payment patterns, customer finances, and relevant business conditions.

SEPARATE ASSESSMENT

- Assess a claim individually when its risk differs from the pools.
- Exclude that claim from pooled estimates so its loss is counted once.

ALL CLOSING CUSTOMER CLAIMS

Invoice	Unpaid	Payment status	Estimation group
SQ03, Critical Hit	$14,000	Current	Independent stores
SQ04, Table Talk	$8,000	1-30 days	Independent stores
SQ05, Dice & Co.	$6,000	31-60 days	Independent stores
SQ06, Game Circuit	$11,000	Current	Regional retailers
SQ07, Playroom Stores	$9,000	1-30 days	Regional retailers
SQ08, Final Level	$7,000	Over 60 days	Assess individually

Does an overdue invoice need separate assessment?

iClicker | Question 4 of 5

A retailer is overdue. Its payment pattern, financial condition, and exposure to local conditions match other retailers in the same overdue group. The accountant proposes individual assessment solely because the invoice is late. What should the seller do?

A Assess it individually because every overdue invoice is unique.

B Apply the current-invoice rate because the retailer still operates.

C Exclude it from the estimate until collection efforts fail.

D Keep it in the pool with similar overdue retailers.

E Add an individual estimate to its share of the pooled estimate.

Does an overdue invoice need separate assessment?: answer

iClicker | Answer 4 of 5 — **Correct answer: D.**

A retailer is overdue. Its payment pattern, financial condition, and exposure to local conditions match other retailers in the same overdue group. The accountant proposes individual assessment solely because the invoice is late. What should the seller do?

A **Assess it individually because every overdue invoice is unique.**
Incorrect. Lateness alone does not distinguish this retailer from the other customers in its overdue group.

B **Apply the current-invoice rate because the retailer still operates.**
Incorrect. The retailer is overdue; continued operation does not make its invoice current.

C **Exclude it from the estimate until collection efforts fail.**
Incorrect. The seller estimates expected losses before collection efforts fail.

D **Keep it in the pool with similar overdue retailers.**
Correct. The stated payment and financial facts support similar risk characteristics within the overdue pool.

E **Add an individual estimate to its share of the pooled estimate.**
Incorrect. The pooled estimate already includes this claim. Adding a separate estimate would count its exposure twice.

Choose relevant historical invoices

Start with all unpaid invoices in a comparable group at an earlier reporting date. Follow every invoice in that group through collection or write-off, including later recoveries.

MATCH TODAY'S RECEIVABLES

- Compare customer risk, payment terms, payment status, and season.
- Compare invoices at similar points in collection.
- Follow the same invoices from their starting balances through later collections and losses.

DEFINE A COMPLETE COMPARISON GROUP

- For overdue winter invoices, use earlier overdue winter invoices with similar customers and terms.
- New spring invoices may differ in customer risk, payment status, and season.
- Include both paid and unpaid outcomes. Choosing only customers who paid would understate losses.

Derive the historical loss rate

WALKTHROUGH

HISTORICAL POPULATION

Comparable independent-store invoices that were current at earlier December year-ends.

UNPAID BALANCES

$200,000 originally unpaid.

COLLECTIONS

$198,000 ultimately collected, including recoveries.

NET LOSS

$200,000 − $198,000 = **$2,000**

HISTORICAL RATE

$$\frac{\$2{,}000}{\$200{,}000} = \mathbf{1\%}$$

SAME INVOICES, SAME LOSS

The records for these invoices also report write-offs of $2,500 and recoveries of $500. Their difference equals the uncollected amount because collection is complete and no price credits apply.

These are past populations, not this quarter's activity.

Adjust historical rates for changed collection risk

Historical rates describe earlier collection experience. Adjust them when today's risks or supported forecasts differ from that experience.

Evidence	Effect on the estimate
Weaker receipts and payment extensions	Consider higher losses for the affected customers. Establish how much their payment capacity changed.
Some customers obtain financing	Evaluate those customers; do not assume the whole pool improved.
Payment patterns and conditions match history	The evidence does not justify an extra adjustment for overdue risk already included in the rate.

FORECAST REVERSION

Reversion means returning to relevant historical loss information for periods beyond those management can reasonably forecast. Use a consistent, rational method.

SIZE OF THE ADJUSTMENT

Use customer cash forecasts and comparable loss experience to justify the adjustment's size. More sales alone do not establish a higher loss rate.

Adjust rates before calculating dollars

WALKTHROUGH

HISTORICAL RATE

The independent current group's historical loss rate is 1%.

PROPOSED INCREASE

Management proposes adding 0.5 percentage points. A percentage-point change adds to the rate itself.

UNPAID BALANCE

The group owes $14,000.

PROPOSED RATE

1% + 0.5 percentage points = **1.5%**

PROPOSED LOSS

$14,000 × 1.5% = **$210**

The arithmetic implements a proposed assumption. Management must still justify the direction and size of the adjustment.

Does January information change the December loss estimate?

Evidence about December

January documents confirm that Final Level entered restructuring in December. Use that evidence to assess expected credit losses at December 31.

A condition arising in January

Another customer suffers an uninsured January fire. Do not include losses caused by that new event in the December estimate.

For the December estimate, ask whether the information concerns a condition that existed at December 31.

Does the proposed adjustment count risk twice?

iClicker | Question 5 of 5

A seller uses historical loss rates for each overdue group. Management proposes an extra increase solely because those invoices are overdue. Payment patterns, customer mix, and forecasts match the historical groups. How should you evaluate the increase?

A. Accept it because overdue invoices always require an extra adjustment.

B. Reject the stated rationale because the historical rates already reflect lateness.

C. Apply the increase only to the largest invoices.

D. Replace the overdue rates with the current-invoice rate.

E. Remove the allowance until a customer actually defaults.

Does the proposed adjustment count risk twice?: answer

iClicker | Answer 5 of 5 — **Correct answer: B.**

A seller uses historical loss rates for each overdue group. Management proposes an extra increase solely because those invoices are overdue. Payment patterns, customer mix, and forecasts match the historical groups. How should you evaluate the increase?

A **Accept it because overdue invoices always require an extra adjustment.**
Incorrect. The historical overdue groups already incorporate the risk associated with their payment status.

B **Reject the stated rationale because the historical rates already reflect lateness.**
Correct. Management has identified no change from the comparable historical groups to justify an additional increase.

C **Apply the increase only to the largest invoices.**
Incorrect. Invoice size does not resolve the duplicate treatment of overdue risk.

D **Replace the overdue rates with the current-invoice rate.**
Incorrect. The invoices remain overdue, so the current-invoice rate is not the appropriate comparison.

E **Remove the allowance until a customer actually defaults.**
Incorrect. The seller still needs an expected loss estimate even without an additional rate increase.

Calculate management's proposed allowance

WALKTHROUGH

Side Quest | December 31, 2026

Use the closing customer balances from the grouping schedule. Management supplies the proposed rates below; only the current independent-store rate was calculated earlier.

Multiply each pool by its proposed rate. For Final Level, subtract expected collection from the unpaid claim.

Group	Unpaid	Proposed rate or collection	Expected loss
Independent, current	$14,000	1.5%	$210
Independent, 1-30 days	$8,000	5%	$400
Independent, 31-60 days	$6,000	11%	$660
Regional, current	$11,000	0.5%	$55
Regional, 1-30 days	$9,000	2.5%	$225
Final Level	$7,000	Collect $2,000	$5,000

Pooled loss $1,550 + individual loss $5,000 = **$6,550 required allowance**.

Step 3 · Record the allowance adjustment

Bring the recorded allowance to the required ending balance.



Compare required and recorded balances

- **Recorded balance:** Earlier estimates, less write-offs, plus recovery reinstatements.
- **Required balance:** Expected losses on the receivables still unpaid.

REQUIRED BALANCE IS LARGER

Allowance for Credit Losses

DEBIT	CREDIT
	Recorded balance
	Credit adjustment
	Required ending balance

Possible reasons:

- More unpaid receivables or weaker collection prospects.
- Write-offs have reduced the recorded balance below the amount needed.

Credit the allowance and debit Credit Loss Expense.

RECORDED BALANCE IS LARGER

Allowance for Credit Losses

DEBIT	CREDIT
	Recorded balance
Debit adjustment	
	Required ending balance

Possible reasons:

- Collections have reduced the receivables still unpaid.
- Improved collection prospects have reduced expected losses.

Debit the allowance and credit Credit Loss Expense to reduce the balance.

Record Side Quest's adjustment

WALKTHROUGH

Side Quest | December 31, 2026

The proposed losses total $1,550 for the pools plus $5,000 for Final Level. The required allowance is $6,550.

Allowance for Credit Losses

DEBIT		CREDIT	
		$1,200	Opening balance
Old Oak write-off	**$1,500**		
		$400	Replay reinstatement
		$100	Unadjusted balance
		$6,450	Adjusting entry
		$6,550	Required ending balance

ADJUSTING ENTRY

Account	Debit	Credit
Credit Loss Expense	$6,450	
Allowance for Credit Losses		$6,450

BALANCE SHEET

Receivables	Amount
Gross receivables	$55,000
Less allowance	($6,550)
Net receivables	**$48,450**

Prepare an alternative year-end adjustment

YOUR TURN

> Take a few minutes to work through this on your own or with those around you.

Alternative Side Quest case | December 31, 2026

ACCOUNT ACTIVITY

- Opening allowance: $9,100 credit balance.
- Write-offs: $1,500.
- Recoveries: $400, recorded through reinstatement and collection.
- No expense adjustment has been recorded.

REMAINING RECEIVABLES

- Gross receivables: $55,000.
- Expected collections: $48,450, based on the year-end review.

Find the recorded and required allowance balances. Prepare the adjusting entry and explain its effects on net receivables, income, and cash.

Reduce the excessive allowance

WALKTHROUGH

Alternative Side Quest case | December 31, 2026

Gross receivables are $55,000; expected collections are $48,450. The required allowance is $6,550.

Allowance for Credit Losses

DEBIT		CREDIT	
		$9,100	Opening balance
Write-offs	**$1,500**		
		$400	Recovery reinstatement
		$8,000	Unadjusted balance
Adjusting entry	**$1,450**		
		$6,550	Required ending balance

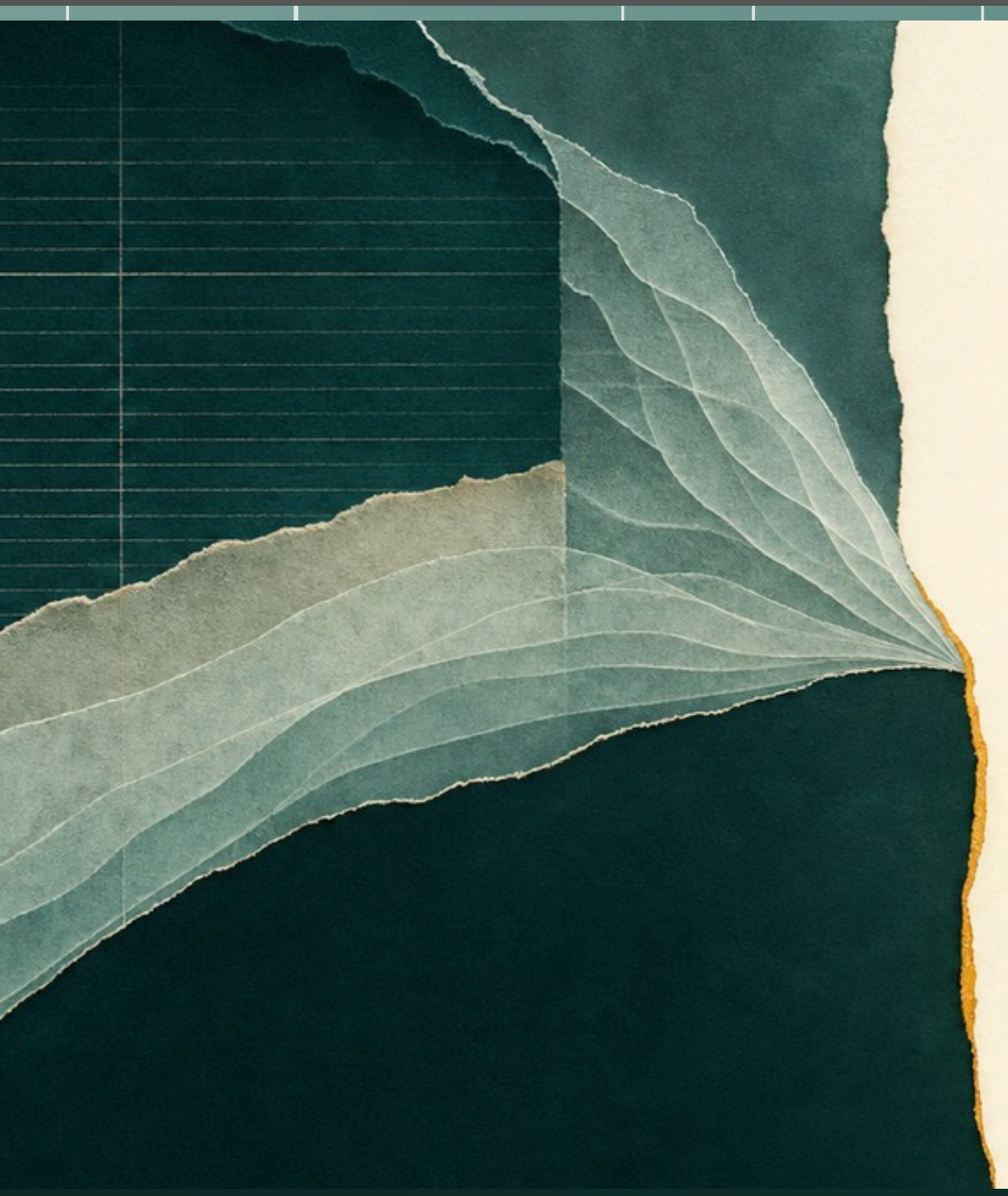
ADJUSTING ENTRY

Account	Debit	Credit
Allowance for Credit Losses	$1,450	
Credit Loss Expense		$1,450

INCOME EFFECT

The credit reduces credit loss expense. If the credit reduces the period’s credit loss expense below zero, the net amount is a **credit loss benefit**, which increases income.

Net receivables increase. Cash and gross customer claims remain unchanged.



Independent application

Practice: estimate credit losses

Use customer records and collection evidence to estimate credit losses and prepare the adjusting entry.

Classify the nursery's unpaid claims

YOUR TURN

> Take a few minutes to work through this on your own or with those around you.

Growing Concern sells nursery stock to garden centers and landscapers in a mild-winter region. It reports at December 31, 2026.

Group	Due date	Unpaid balance
Garden centers	January 14, 2027	$18,000
Landscapers due in January	January 9, 2027	$12,000
Landscapers due in December	December 15, 2026	$6,000
Insolvent landscaper	November 14, 2026	$4,000

No discount or return rights remain. The insolvent customer is expected to pay $1,000.

Classify each row as current or overdue. Decide how to group or individually assess these receivables, and explain why.

Growing Concern's aging and risk groups

ANSWER

Growing Concern | December 31, 2026

Group	Due date	Aging at December 31	Assessment
Garden centers	January 14, 2027	Current; not yet due	Separate current garden center pool
Landscapers due in January	January 9, 2027	Current; not yet due	Separate current landscaper pool
Landscapers due in December	December 15, 2026	16 days overdue	Landscaper pool, 1-30 days overdue
Insolvent landscaper	November 14, 2026	47 days overdue	Individual assessment

December 31 − December 15 = 16 days. November 14 to December 31 = 47 days.

Group customers with similar collection risks. Keep customer types and payment-status groups separate because their collection experience differs.

Assess the insolvent customer separately because its financial condition differs from the pools. Exclude its claim from pooled balances to avoid counting it twice.

Derive Growing Concern's historical rates

YOUR TURN

> Take a few minutes to work through this on your own or with those around you.

These are earlier winter invoices for similar customers with similar payment terms. Collection efforts have ended, so the total collected, including recoveries, is known.

Historical group	Originally unpaid	Ultimately collected
Garden centers, current	$200,000	$198,000
Landscapers, current	$100,000	$97,000
Landscapers, 1-30 days overdue	$50,000	$46,000

Calculate each rate. Explain why new spring invoices might be a poor substitute for these historical populations.

Growing Concern's historical loss rates

ANSWER

Historical loss rate = (originally unpaid − ultimately collected) ÷ originally unpaid.

Historical group	Loss calculation	Loss rate calculation
Garden centers, current	$200,000 − $198,000 = $2,000	$2,000 ÷ $200,000 = **1%**
Landscapers, current	$100,000 − $97,000 = $3,000	$3,000 ÷ $100,000 = **3%**
Landscapers, 1-30 days overdue	$50,000 − $46,000 = $4,000	$4,000 ÷ $50,000 = **8%**

Why not substitute new spring invoices?

Spring customers may face different seasonal cash flows. New invoices also have had less time for collection, so unpaid amounts may still be collected.

Use completed collection records for comparable winter customers, payment terms, and payment-status groups. Include recoveries in total collections, as these records do.

Test the proposed rate reductions

DISCUSSION

Group	Derived historical rate	Management's proposal
Garden centers, current	1%	1%
Landscapers, current	3%	2%
Landscapers, 1-30 days overdue	8%	6%

Landscapers owing $6,000 of the $12,000 current balance have signed refinancing agreements with their banks. The agreements refinance their bank debt, not their amounts owed to Growing Concern. The amount and timing of cash available to pay Growing Concern are not yet known.

No overdue landscapers have these agreements. An overdue customer missed a promised payment.

Garden-center payment patterns remain stable. Which reductions need more evidence? What information would you request?

Both rate reductions need more evidence

WALKTHROUGH

Garden-center payment patterns remain stable. The supplied facts do not support either proposed landscaper rate reduction.

WHICH REDUCTIONS NEED SUPPORT?

- **Current landscapers:** Refinancing covers only some customers; available cash is unknown.
- **Overdue landscapers:** None refinanced, and a missed payment raises concern rather than supporting lower losses.

WHAT EVIDENCE SHOULD WE REQUEST?

- Bank agreement terms and customer cash forecasts showing funds available to pay Growing Concern.
- Recent payment records and reasons for the missed payment, by customer, to reassess groups and rates.

Obtain the evidence before choosing rates. Next, calculate the accounting amounts using management's proposal as an assumption for practice.

Apply the proposed rates for practice

YOUR TURN

> Take a few minutes to work through this on your own or with those around you.

Growing Concern | December 31, 2026

Group	Unpaid	Proposed treatment
Current garden centers	$18,000	Apply 1%.
Current landscapers	$12,000	Apply 2%.
Overdue landscapers	$6,000	Apply 6%.
Insolvent landscaper	$4,000	Expected collection is $1,000.

Calculate pooled losses, the individual loss, and the proposed required allowance.

Calculate the allowance under the proposed rates

WALKTHROUGH

Component	Calculation	Proposed loss
Garden centers	$18,000 × 1%	$180
Current landscapers	$12,000 × 2%	$240
Overdue landscapers	$6,000 × 6%	$360
Individual customer	$4,000 − $1,000	$3,000
Required allowance under proposal	**$780 + $3,000**	**$3,780**

These amounts follow management's proposed rates. Continue with this allowance for the remaining practice entries; it is not an approved estimate.

Find the nursery's recorded allowance

YOUR TURN

> Take a few minutes to work through this on your own or with those around you.

Growing Concern | Before the December 31 adjustment

OPENING ALLOWANCE

Growing Concern begins with a $900 credit allowance.

WRITE-OFF

The nursery writes off $1,300.

RECOVERY

It recovers $100, using reinstatement then collection.

No expense adjustment has been recorded.

RECORDED ALLOWANCE

Calculate the balance and identify its debit or credit position.

Growing Concern has a debit allowance before adjustment

WALKTHROUGH

Growing Concern | Before adjustment

Allowance for Credit Losses

DEBIT		CREDIT	
		$900	Opening balance
Write-offs	$1,300		
		$100	Recovery reinstatement
Unadjusted debit balance	$300		

> The adjusting entry must take the allowance from this debit balance to the required ending credit balance.

Record Growing Concern's adjusting entry

WALKTHROUGH

Growing Concern | December 31, 2026

Using management’s proposed rates for this exercise, the required allowance is $3,780. The ledger has a $300 debit balance before adjustment.

Allowance for Credit Losses

DEBIT		CREDIT	
Unadjusted debit	**$300**		
		$4,080	Adjusting entry
		$3,780	Required ending credit

ADJUSTING ENTRY

Account	Debit	Credit
Credit Loss Expense	$4,080	
Allowance for Credit Losses		$4,080

NET RECEIVABLES

$40,000 gross − $3,780 allowance = **$36,220**.

Revising an unsupported loss rate changes the allowance and expense. It does not change what customers owe.

Reconcile the cash already held

Explain the difference between the bank statement and the company records.



Review: cash and cash equivalents

Recall cash and cash equivalents from **Preparing the statement of cash flows**.

Cash and cash equivalents

Cash includes currency and deposits available on demand.

Cash equivalents are highly liquid investments, readily convertible to known cash amounts with insignificant value risk. Their maturity when acquired is generally 3 months or less.

Identify restrictions on cash and present restricted amounts appropriately.

Customer receivables

A receivable is a claim to future cash. The customer still needs to pay.

Collection replaces that claim with cash; it does not create another sale.

Decide which record needs adjustment

A bank statement and the company's cash ledger can include different transactions at the same date. Bring both balances to corrected cash.

Company recorded it first

Deposit in transit: The company records a deposit after the bank's processing cutoff. The bank posts it later. Add it to the statement balance.

Outstanding check: The company records a check when issued; the bank records payment when it clears. Subtract it from the statement balance.

Bank recorded it first

Customer receipt: A customer pays directly into the company's bank account. The bank posts it before the company records the receipt. Add it to book cash and record the collection.

Bank fee: The bank deducts a fee. If unrecorded, subtract it from book cash and record the expense.

Correct an error on the side that contains it. Company corrections need entries; report bank errors to the bank.

Reconcile Side Quest's cash

YOUR TURN

> Take a few minutes to work through this on your own or with those around you.

Side Quest | December 31, 2026

Selected entries through December 31; all differences are included. Amounts are US dollars.

Bank statement

Ending balance: $17,000

Transaction	In	Out
Checkpoint deposit	$12,000	
Old Oak deposit	$6,500	
SQ04 collection	$2,000	
Service charge		$100

Company cash ledger

Ending balance: $15,600

Transaction	In	Out
Checkpoint deposit	$12,000	
Old Oak deposit	$6,500	
December 31 deposit	$3,000	
Checks issued		$2,500

Reconcile the two balances and prepare any required company journal entries.

Both schedules reach corrected cash

WALKTHROUGH

Side Quest | December 31, 2026 | US dollars

BANK STATEMENT

Item	Amount
Statement balance	$17,000
Add deposit in transit	$3,000
Subtract outstanding checks	($2,500)
Corrected cash	**$17,500**

The company already recorded these items. No new company entry is needed.

COMPANY RECORDS

Item	Amount
Unadjusted cash	$15,600
Add SQ04 collection	$2,000
Subtract service charge	($100)
Corrected cash	**$17,500**

Record the missing collection and bank fee in the company ledger.

Post the missing company transactions

WALKTHROUGH

Side Quest | December 31, 2026

The bank reports an SQ04 customer receipt of $2,000 and a $100 fee. Both are missing from Side Quest's cash records.

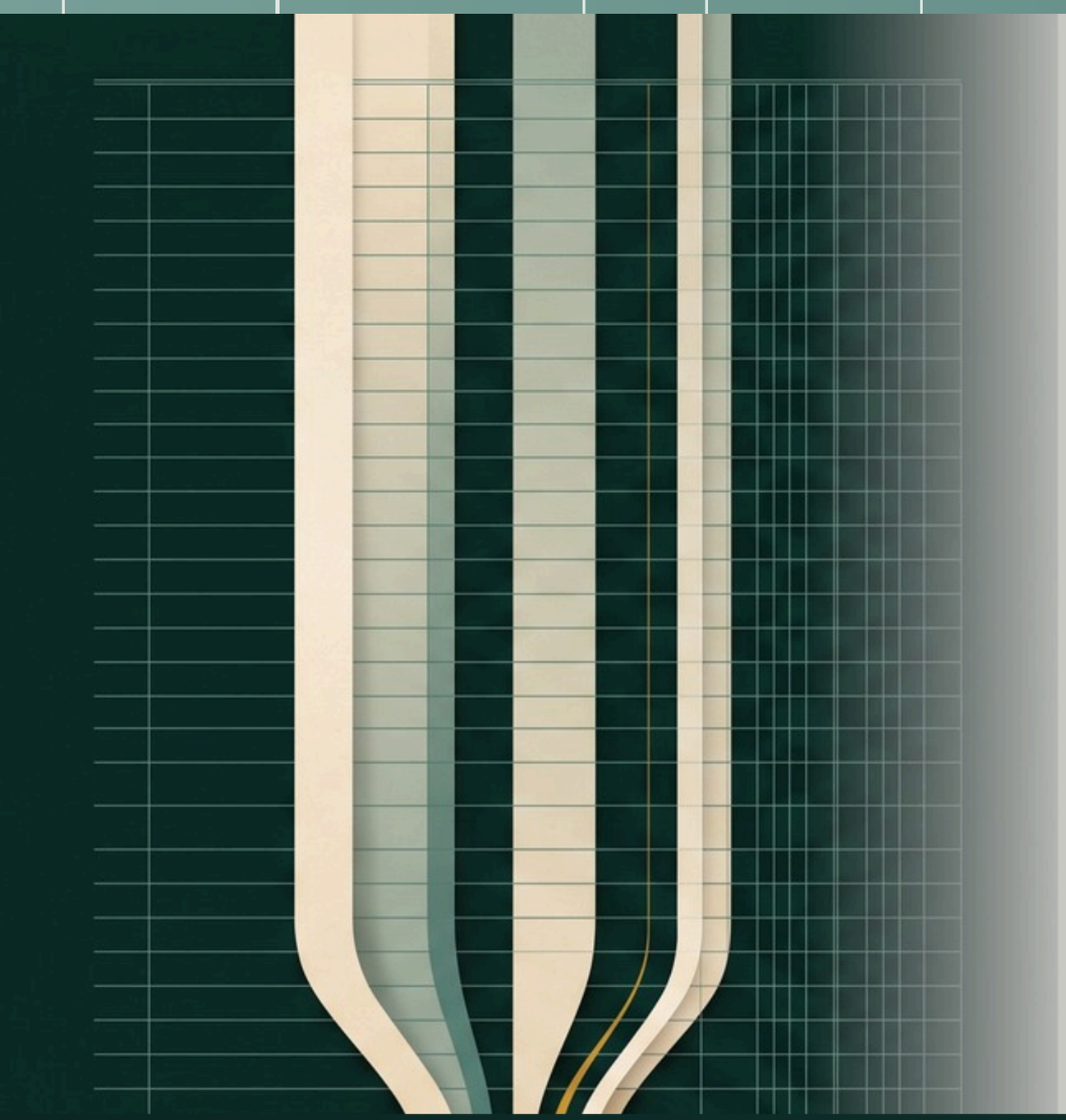
SQ04 ELECTRONIC COLLECTION

Account	Debit	Credit
Cash	$2,000	
Accounts Receivable		$2,000

SERVICE CHARGE

Account	Debit	Credit
Bank Fee Expense	$100	
Cash		$100

The SQ04 receipt is already included in the final aging and receivable reconciliation we used. Post it once, not again after the loss estimate.



Next meeting

Next class: Units 3 and 4 mini-exam

Thursday, October 22, 2026

Unit 4 review assignment: Sunday, October 25, at 11:59 PM.