Let's do a complete a/r allowance activity project! Prepare a balance sheet and income statement for the following as of and for the three month period ending March 31:

Make sales to customers in January, February and March totaling $4,850,000. Terms 2/10 net 30.

Allowance for doubtful accounts at BOY is $575,000.

Inventory at the beginning of the period is $5,000,000, purchases were $2,000,000 and ending inventory is $4,000,000.

Loss incurrence rate over trailing twelve months (ttm) is 1%.

Management writes off $100,000 of receivables in the ordinary course.

Management reviews the accounts receivable at the end of March and notes that an old receivable from prior year sales in the amount of $1,000,000 is from a customer which is no longer in existence. Management concludes that the allowance against current period sales still appears appropriate and that an additional $500,000 of expense is justified for this item (b/c there was already $500,000 in the reserve account at the beginning of the year). The old customer balance should be written-off.

Collected $2,500,000 of accounts receivable during the three month period, all of which was received within 10 days. Gross method employed.

BOY retained earnings was $4,425,000.
Record sales activity:
Accounts receivable $4,850,000
Sales $4,850,000

Record % of Sales A/R Reserve
Bad debt expense $48,500
Allowance for doubtful accounts $48,500

Record Ordinary Write-Offs
Allowance for DA’s $100,000
Accounts receivable $100,000

Direct Write-Off of Large Balance (per management analysis)
Bad debt expense $500,000
Accounts receivable $500,000
Allowance for doubtful accounts $500,000
Accounts receivable $500,000

Compute A/R Paid on Discount
Cash received $2,500,000
Divided by Discount (1-.02) .98
A/R $2,552,020

Record Cash Collections
Cash $2,500,000
Trade discounts (sales) $51,020
Accounts receivable $2,551,020

Compute COS:
Inventory at BOY $5,000,000
Purchases $2,000,000
Ending balance ($4,000,000)
COS $3,000,000

Record Inventory activity:
COS $3,000,000
Inventory $3,000,000
Inventory $2,000,000
Cash $2,000,000

Analyze adequacy (valuation) of A/R allowance:
Balance at beginning of year $575,000
Additions during year $48,500
Ordinary write-off’s ($100,000)
Direct write-off (no impact)
Ending balance $523,500
Amount estimated for 90 days sales ($48,500)
“Cushion” $475,000

Is this adequate? Depends on many factors such as: What is the balance of the >90 days aging component, what is the quality of the past 3 months sales, etc.
ROLLFORWARDS FOR STATEMENT PREPARATION (CAN USE T-ACCOUNTS OR WHATEVER WORKS FOR YOU!)

NOTE: CREDITS IN BRACKETS IN THIS PRESENTATION

**A/R**
BOY 0
Debits $4,850,000
Credits ($3,651,020)
EOY $1,198,980

**Allowance**
BOY (575,000)
Debits $600,000
Credits (48,500)
EOY ($23,500)

**Bad Debt Expense**
BOY 0
Debits $548,500
Credits (none)
EOY $548,500

**INVENTORY**
BOY 5,000,000
Debits 2,000,000
Credits -3,000,000
EOY 4,000,000

**SALES**
BOY 0
Debits $51,020
Credits (4,850,000)
EOY (4,798,980)

**CASH**
BOY 0
Debits $2,500,000
Credits (2,000,000)
EOY $500,000

**COS**
BOY 0
Debits $3,000,000
Credits (none)
EOY $3,000,000

**RETIRED EARNINGS**
BOY (4,425,000)
Debits $0
Credits (Net income) (1,250,480)
EOY ($5,675,480)
### XYZ INC
**BALANCE SHEET**
*3/31/XX*

<table>
<thead>
<tr>
<th>ASSETS</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash</td>
<td>500,000</td>
</tr>
<tr>
<td>Accounts Receivable, net of $23,500 allowance</td>
<td>1,175,480</td>
</tr>
<tr>
<td>Inventory</td>
<td>4,000,000</td>
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<tr>
<td><strong>Total current assets</strong></td>
<td>5,675,480</td>
</tr>
<tr>
<td><strong>Total Assets</strong></td>
<td>5,675,480</td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>LIABILITIES &amp; EQUITY</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Current liabilities</td>
<td>none in example</td>
</tr>
<tr>
<td><strong>EQUITY</strong></td>
<td></td>
</tr>
<tr>
<td>Retained Earnings</td>
<td>5,675,480</td>
</tr>
<tr>
<td>Liabilities &amp; Equity</td>
<td>5,675,480</td>
</tr>
</tbody>
</table>

| XYZ INC
**INCOME STATEMENT**
*3 MONTHS ENDED MARH 31, XX*

| Revenue                                    | 4,798,980 |
| COS                                        | 3,000,000 |
| Gross profit                               | 1,798,980 |
| Bad debt expense                           | 548,500  |
| Provision for income taxes                 | nothing in example |
| **Net income**                             | 1,250,480 |