

**Irrecoverable Debts and Provision for Doubtful Debts**

1 Gary is a manufacturer of kitchen equipment. His financial year ends on 30 September.

On 1 August 2019 Ed, a credit customer, was declared bankrupt and the balance of his account of \$326 was written off as irrecoverable.

No other debts were written off during the year.

**REQUIRED**

(a) Prepare a journal entry to write off the amount owed by Ed.

A narrative **is** required.

Gary  
General Journal

Date	Details	Debit \$	Credit \$
2019			
.....	.....	.....	.....
.....	.....	.....	.....
.....	.....	.....	.....
.....	.....	.....	.....

[3]

On 1 June 2018 the account of Sally, a credit customer who owed \$440, was written off as irrecoverable.

On 4 September 2019 Sally settled her account with \$180 in cash and a computer valued at \$260.

**REQUIRED**

(b) State how Gary would record the transaction on 4 September 2019.

account debited	account credited
\$	\$
.....	.....
.....	.....

[3]



- (e) Complete the table to indicate the **effect of omitting** to record the bad debt, the bad debt recovered and the adjustment to the provision for doubtful debts.

The first one has been completed as an example.

item omitted	effect on profit for the year ended 30 September 2019		effect on current assets at 30 September 2019	
		\$		\$
bad debts	<i>overstated</i>	326	<i>overstated</i>	326
bad debt recovered				
adjustment to provision for doubtful debts				

[4]

- 2 Hamila is a trader. Her financial year ends on 28 February. All goods are bought and sold on credit terms.

Hamila provided the following information for February 2019.

2019

- February 1 Safiya, a credit customer, owed \$320  
 12 Safiya paid the balance due on 1 February by cheque  
 16 Safiya purchased goods on credit, list price \$250, less 20% trade discount  
 18 The bank returned Safiya's cheque because of insufficient funds in the account  
 24 Safiya paid \$400 in cash  
 27 The balance of Safiya's account was written off as irrecoverable

**REQUIRED**

- (a) Prepare the account of Safiya as it would appear in Hamila's ledger for the month of February 2019.

Hamila  
Safiya account

Date 2019	Details	\$	Date 2019	Details	\$
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....

[6]

- (b) Complete the bad debts account in Hamila's ledger for the month of February 2019. Close the account by making an appropriate year-end transfer.

Hamila  
Bad debts account

Date 2019	Details	\$	Date 2019	Details	\$
Feb 27	Total to date	674	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....

(2)

Hamila maintains a provision for doubtful debts. The following account appeared in Hamila's ledger.

Hamila  
Provision for doubtful debts account

Date 2019	Details	\$	Date 2018	Details	\$
Feb 28	Income statement	130	Mar 1	Balance b/d	1500
	Balance c/d	<u>1370</u>			
		<u>1500</u>			<u>1500</u>

**REQUIRED**

- (c) (i) Explain the following entries in the provision for doubtful debts account.

Name the account in which the double entry would be made for each item. State whether the account would be debited or credited.

1 March 2018 Balance b/d

Explanation .....

.....

.....

Name of account .....

Debit or credit .....

28 February 2019 Balance c/d

Explanation .....

.....

.....

Name of account .....

Debit or credit .....

[4]

- (ii) Explain the following entry in the provision for doubtful debts account.

28 February 2019 Income statement

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..... [2]

- (d) Explain how Hamila is applying the principle of prudence by maintaining a provision for doubtful debts.

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..... [2]

- (e) Explain how Hamila is applying the principle of accruals (matching) by maintaining a provision for doubtful debts.

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..... [2]

- (f) Suggest **two** ways in which Hamila could reduce the possibility of bad debts.

1 .....

2 .....

[2]

- 3 Tej is a trader who sells goods on credit. His year end is 28 February. Tej provided the following information.

	\$
At 1 March 2020	
Trade receivables	6250
Other receivables (rent prepaid)	300
For the year ended 28 February 2021	
Rent charge for the year	3900
Cheque payments for rent	1950
30 June 2020	
30 November 2020	2100
At 28 February 2021	
Trade receivables	7000

The provision for doubtful debts was 4% of trade receivables at 1 March 2020 and 6% of trade receivables at 28 February 2021.

**REQUIRED**

- (a) Prepare the provision for doubtful debts account for the year ended 28 February 2021. Balance the account and bring down the balance on 1 March 2021.

Tej  
Provision for doubtful debts account

Date	Details	\$	Date	Details	\$
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....
.....	.....	.....	.....	.....	.....

[4]

(b) (i) Explain how the realisation principle is applied to the recording of Tej's credit sales.

.....  
.....  
.....  
..... [2]

(ii) Explain how the prudence principle is applied to the maintenance of Tej's provision for doubtful debts.

.....  
.....  
.....  
..... [2]

Tej sells to a small number of customers. He has good working relationships with them and they sometimes recommend him to potential customers.

Tej is concerned that his customers are taking a long time to pay him. He is considering charging interest on overdue accounts.

**REQUIRED**

(c) Advise Tej whether or not he should charge interest on overdue accounts. Justify your answer.

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..... [5]