GJ Transactions

Bad debts

A major risk to allowing customers to buy on credit is the possibility that the customer will not pay. A debtor is an asset to the business, since it will change into money when the debtors pays what they owe the business.

In practice it may be very difficult to collect the amount owed by debtors.
A business can take legal action against a defaulting debtor, but legal action may be costly and funds may not be recovered if a client is insolvent or has disappeared.
After doing all legal procedures to collect the owed amount the business may decide that it is not worth it to continue chasing the debtor for payment.

An entry will be made in the General Journal:

Dr **Bad debts** (an **expense** in the Nominal section) → Owner's equity decreases
Cr Debtors control (an **asset** in the Balance sheet section) → Assets decrease
At the same time, the debtor's personal account in the Debtors Ledger will also be credited.

For example: 1

01 A debtor, C Carelse, is insolvent and his account of R150 must be written off as irrecoverable.

The entires below show how to write off a bad debt.

General Journal of FEM Traders - October 2018   GJ10

Doc. No.	Day	Details	Fol.	Debit	Credit	Debtors control		Creditors control	
						Debit	Credit	Debit	Credit
JV4	1	Bad debts	N10	150					
		C Carelse (Account written off as irrecove	D2		150		150		
							150		

B10

Posting to General Ledger
Balance Sheet account

Debtors control (**Asset**)   B10

Date	Details	Fol.	Amount	Date	Details	Fol.	Amount
				2018 Oct	1 Bad debts	GJ10	150

Nominal account

Bad debts (**Owners equity/expense**)   N10

Date	Details	Fol.	Amount	Date	Details	Fol.	Amount
2018 Oct	1 Debtors control	GJ10	150				

Debtors Ledger of FEM Traders

C Carelse   **D2**

Date		Details	Fol.	Debit	Credit	Balance
2018	1	Balance	b/d			150
Oct		Journal voucher no. 4/Bad debts	GJ10		150	-

Notes

- Remember that when you sell goods on credit, you Dr Debtors control and Cr Individual debtors account (in this case it is **C Carelse**).
- So if a debtor does not pay and you write off the amount owing as irrecoverable, you have to do the opposite of what is mention above. This means that you have to Dr Bad debts and Cr Debtors control. Writing off bad debts decreases the debtor's account.
- The *Bad debts* account must be debited since it is a loss that will decrease the owner's equity.

The effect on the accounting equation:

Assets	Owner's equity	Liabilities
- 150 Debtors decreased	- 150 Bad debts are a loss	0

For example: 2

01 C Carelse, a debtor, is insolvent and his estate can pay 50c in the rand. Issued receipt no. 010 for the amount and wrote off the rest as irrecoverable.

What does this mean?

For every rand the debtor owes, he can pay 50c. His debt of R150 must be multiplied by R0,50 to determine how much he can pay.

Calculation

R150 X 0,50 = R75
The rest of the debt, R150 - R75 = R75, must be written off as irrecoverable.

The part for which cash was received is shown below.

Cash Receipts Journal of FEM Traders - October 2019   **CRJ10**

Doc No.	D	Details	Fol	Analysis of Receipts	Bank	Debtors control
010	01	C Carelse	D2	75	75	75

The entries below show how to write off the bad debts.

General Journal of FEM Traders - October 2019   GJ10

Doc. No.	Day	Details	Fol.	Debit	Credit	Debtors control Debit	Debtors control Credit	Creditors control Debit	Creditors control Credit
JV5	01	Bad debts	N10	75					
		C Carelse (Account written off as irrecove	D2		75		75		
							75		

B10

Posting to General Ledger
Balance Sheet account

Debtors control   B10

Date	Details	Fol.	Amount	Date	Details	Fol.	Amount
				2019 Oct 1	Bank	CRJ10	75
				31	Bad debts	GJ10	75

Nominal account

Bad debts   N10

Date	Details	Fol.	Amount	Date	Details	Fol.	Amount
2019 Oct 1	Debtors control	GJ10	75				

Debtors Ledger of FEM Traders

C Carelse   **D2**

Date		Details	Fol.	Debit	Credit	Balance
2019	1	Balance	b/d			**150**
Oct		Receipt no. 010	CRJ10		75	**75**
		Journal voucher no. 5/bad debts	GJ10		75	**-**

The effect on the accounting equation:

Assets	Owner's equity	Liabilities
- 150 Debtors decreased	- 75 Bad debts are a loss	0
+ 75 Cash increased		