

How Entries For Notes Receivable Valley Designs Issued A 90-day, 8% Note For \$54,000, Dated April 17,

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Understanding the accounting entries related to notes receivable is crucial for businesses to accurately record their financial transactions. In this article, we will explore how Valley Designs issued a 90-day, 8% note for \$54,000 on April 17, and the corresponding journal entries involved in recording this transaction. We will break down each step, discuss the underlying accounting principles, and provide practical examples for clarity.

Overview of Notes Receivable and Their Significance

What Is a Note Receivable?

A note receivable is a written promise from a customer or borrower to pay a specific amount of money at a future date, usually with interest. It serves as evidence of a debt owed to the business and is classified as a current or non-current asset on the company's balance sheet depending on the maturity date.

Importance in Business Transactions

Notes receivable are important because they:

- Provide a formalized, legally binding agreement for repayment
- Help manage credit risk by specifying interest and due date
- Offer opportunities for earning interest income
- Facilitate cash flow management and planning

Details of the Note Issued by Valley Designs

Key Information

The note issued by Valley Designs has the following attributes:

- Principal amount (Face value): \$54,000
- Interest rate: 8% annually
- Term: 90 days
- Date of issuance: April 17

Implications of the Terms

- Since the note is for 90 days, it will mature approximately three months after April 17, which is around July 16.
- The annual interest rate of 8% means that interest for the period must be calculated proportionally for 90 days.

Calculating Interest and Maturity Value

Interest Calculation

Interest on notes receivable is calculated using the formula:

$$\text{Interest} = \text{Principal} \times \text{Rate} \times \text{Time}$$

Where:

- Principal = \$54,000
- Rate = 8% (or 0.08)
- Time = 90 days / 360 days (assuming a 360-day year convention for simplicity)

Calculating:

$$\text{Interest} = \$54,000 \times 0.08 \times (90 / 360)$$

$$\text{Interest} = \$54,000 \times 0.08 \times 0.25$$

$$\text{Interest} = \$54,000 \times 0.02$$

$$\text{Interest} = \$1,080$$

Maturity Value

Total amount to be received at maturity:

$$= \text{Principal} + \text{Interest}$$

$$= \$54,000 + \$1,080$$

$$= \$55,080$$

Recording the Initial Entry on April 17

Journal Entry for Issuance of the Note

When Valley Designs issues the note to the borrower, the company records a notes receivable and reduces cash or accounts receivable depending on the transaction context.

If the note was issued in exchange for services or goods provided, the entry would be:

Debit: Notes Receivable – \$54,000
Credit: Accounts Receivable / Cash – \$54,000

This entry recognizes the company's right to collect \$54,000 at a future date.

Interest Revenue Recognition and Accruals

Interest Accrual at Year-End

If the financial statements are prepared at a date before the maturity (for example, June 30), the company must accrue interest earned but not yet received.

Calculate accrued interest from April 17 to June 30:
- Number of days: April 17 to June 30 = 75 days

Interest accrued:
= $\$54,000 \times 0.08 \times (75 / 360)$
= $\$54,000 \times 0.08 \times 0.2083$
= approximately \$900

Journal Entry on June 30:

Debit: Interest Receivable – \$900
Credit: Interest Revenue – \$900

This ensures that income is recognized in the proper period.

Maturity and Final Settlement Entry

Receiving Payment at Maturity

On July 16, the company receives the total amount including interest:

Total amount received:
= \$55,080

Debit: Cash – \$55,080
Credit: Notes Receivable – \$54,000
Credit: Interest Revenue – \$1,080

Alternatively, if interest was accrued earlier, the interest revenue would have been recognized, and the final entry would involve clearing the receivable and recognizing interest income.

Additional Considerations in Recording Notes Receivable

Discounts and Premiums

In some cases, notes are issued at a discount or premium. For example:

- If issued at less than face value, the difference is a discount and is amortized over the life of the note.
- If issued at more than face value, the excess is a premium.

Impairment and Default Risks

Companies must evaluate the collectibility of notes receivable regularly and recognize impairment losses if necessary.

Practical Example and Summary

Suppose Valley Designs lends \$54,000 on April 17, issuing a 90-day, 8% note. The journal entries involved are:

1. At issuance (April 17):

Debit: Notes Receivable – \$54,000
Credit: Accounts Receivable or Cash – \$54,000

2. At year-end (if applicable, e.g., June 30):

Debit: Interest Receivable – \$900

Credit: Interest Revenue – \$900

3. At maturity (July 16):

Debit: Cash – \$55,080

Credit: Notes Receivable – \$54,000

Credit: Interest Revenue – \$1,080

Summary:

This process ensures that the company's financial statements accurately reflect the assets, income, and cash flows related to notes receivable. Proper recording and understanding of the interest calculations and timing are essential for compliance with accounting standards and for providing clear financial information.

Conclusion

Understanding how to record entries for notes receivable like the one Valley Designs issued is fundamental for accurate financial reporting. The key steps involve recognizing the note at face value, accruing interest income over the period, and recording the receipt of payment at maturity. These processes not only ensure compliance with accounting principles but also aid in effective cash flow management and financial analysis. Whether for internal management or external reporting, mastering these entries enhances a company's financial integrity and transparency.

Frequently Asked Questions

What is the significance of Valley Designs issuing a 90-day, 8% note for \$54,000 on April 17?

This note represents a formal written promise from Valley Designs to pay \$54,000 plus interest over 90 days, indicating a short-term borrowing or receivable transaction that impacts their financial statements.

How do you calculate the interest on the note issued by Valley Designs?

Interest is calculated using the formula: $\text{Principal} \times \text{Rate} \times \text{Time}$. For this note, it would be $\$54,000 \times 8\% \times (90/360) = \$1,080$, representing the interest earned over 90 days.

What journal entry should Valley Designs make upon issuing the note on April 17?

The entry would be: Debit Notes Receivable \$54,000; Credit Cash or Accounts Receivable \$54,000, reflecting the issuance of the note receivable.

When will Valley Designs recognize interest revenue from this note?

Interest revenue is recognized over the life of the note, typically accrued periodically. At maturity (after 90 days), the total interest of \$1,080 is recognized, and the note receivable is settled.

How does the maturity date of the note affect Valley Designs' financial reporting?

On the maturity date, Valley Designs will record the collection of the note, including principal and interest, impacting their cash flows and revenue recognition in the financial statements.

What are the key considerations for Valley Designs in accounting for this 90-day note?

Key considerations include accurately calculating and recording interest, ensuring proper classification of the note as a current asset, and recognizing interest income at the appropriate time in accordance with accounting standards.

Additional Resources

Understanding the Entries for Notes Receivable: Valley Designs' 90-Day, 8% Note for \$54,000 Issued on April 17

When analyzing accounting transactions related to notes receivable, it's crucial to understand the underlying concepts, journal entries, and their implications on financial statements. In this detailed review, we will explore how Valley Designs issued a 90-day, 8% note for \$54,000 on April 17, and how to record this transaction accurately in the accounting records. This analysis not only provides clarity on the specific entry but also offers insight into the broader principles governing notes receivable accounting.

Overview of Notes Receivable and Their Significance

Notes receivable are written promises from customers or other parties to pay a specified amount of money at a future date, usually with interest. They are a formal alternative to accounts receivable and are often used when extending credit with more formal terms.

Key features of notes receivable include:

- Principal amount: The face value of the note, in this case, \$54,000.
- Interest rate: The annual rate, here 8%, which determines interest income.
- Term: The duration until maturity—in this case, 90 days.
- Date of issuance: April 17, which sets the timeline for interest calculation and maturity.

Why notes receivable matter:

- They provide a more secure and formalized method of collecting receivables.
- They often involve interest income, impacting revenue recognition.
- They require specific accounting entries at inception, during the period, and upon collection or maturity.

Initial Recognition of the Note on April 17

The issuance of the note involves recording the creation of a receivable with associated interest components. The journal entry on April 17 will include:

- Recording the receivable at face value.
- Recognizing any accrued interest if applicable (though generally, interest is not accrued at issuance unless explicitly stated).

Step-by-step breakdown:

1. Debit Notes Receivable: This increases the asset account to reflect the amount owed by the customer.
2. Credit Accounts or Cash: Since the note is issued in exchange for a receivable, typically, the entry is only to Notes Receivable unless the note is issued in exchange for cash or other consideration.

Sample journal entry:

Date	Account	Debit	Credit
April 17	Notes Receivable	\$54,000	
	Accounts or Cash		\$54,000

Note: If the note is issued in exchange for a receivable, the entry might differ, reflecting a transfer from accounts receivable to notes receivable.

Interest Calculation at the Time of Issuance

Interest on notes receivable is typically accrued over the life of the note. The calculation involves:

Interest = Principal × Rate × Time

- Principal: \$54,000
- Annual Interest Rate: 8% (or 0.08)
- Time: 90 days (expressed as a fraction of a year: 90/365)

Calculating the interest:

$$\text{Interest} = \$54,000 \times 0.08 \times (90/365)$$

$$\text{Interest} \approx \$54,000 \times 0.08 \times 0.2466$$

$$\text{Interest} \approx \$54,000 \times 0.019728$$

$$\text{Interest} \approx \$1,065.31$$

This interest is not typically recorded at issuance but is accrued over time, generally monthly or at the end of the period.

Recording the Note and Interest Accrual Over the Period

During the 90-day period, interest accrual is necessary to recognize earned revenue in accordance with the matching principle.

Monthly accrual example:

$$\text{- Monthly interest} = \text{Total interest} / 3 \approx \$1,065.31 / 3 \approx \$355.10$$

End-of-period entries:

At the end of each month, the company would:

- Debit Interest Receivable for \$355.10.
- Credit Interest Revenue for \$355.10.

Sample journal entry after one month:

Date	Account	Debit	Credit
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End of Month	Interest Receivable	\$355.10	
	Interest Revenue		\$355.10

This process continues until the maturity date.

Maturity and Final Collection Entry

At the end of 90 days (on July 16):

- The note matures, and the company receives the principal plus interest.
- The collection involves recording receipt of cash and removing the receivable.

Total interest earned: approximately \$1,065.31

Final journal entry:

Date	Account	Debit	Credit
July 16	Cash	\$55,065.31	
	Notes Receivable		\$54,000
	Interest Receivable		\$355.10 (if accrued)
	Interest Revenue		\$710.21 (remaining interest)

Note: The precise entries depend on when interest was accrued during the period. If interest was accrued monthly, the final entry adjusts for all accrued interest.

Implications on Financial Statements

Balance Sheet:

- Notes Receivable: Recorded at face value (\$54,000) until collection.
- Interest Receivable: Recognized as an asset if interest has accrued but not yet received.
- Cash: Increased upon collection of the note.

Income Statement:

- Interest Revenue: Recognized over the period as interest accrues.
- Impact: Enhances the company's earnings during the period.

Cash Flow Statement:

- Operating Activities: The collection of the note appears under cash inflows from operating activities if the note is related to core operations.

Accounting Principles and Best Practices

Consistency and Accuracy:

- Use the accrual basis of accounting to match revenue and expenses.
- Properly calculate and accrue interest over the life of the note.

Documentation:

- Maintain detailed records of the note's terms, including interest rate, maturity date, and any

payments.

Internal Controls:

- Verify the note's terms before recording.
- Reconcile interest accrued periodically.

Compliance:

- Ensure adherence to GAAP or IFRS standards regarding recognition and measurement of notes receivable.

Additional Considerations in Recording Notes Receivable

Discounting Notes:

- If Valley Designs discounts the note before maturity, it must recognize a discount on the note and record interest revenue accordingly.

Impairment of Notes:

- If there's doubt about collectibility, an allowance for doubtful accounts might be necessary.

Transfer and Sale of Notes:

- If Valley Designs sells or transfers the note before maturity, appropriate accounting for sale or transfer must be performed.

Conclusion: The Significance of Proper Entries for Notes Receivable

In conclusion, the issuance of a 90-day, 8% note for \$54,000 by Valley Designs on April 17 involves a series of well-defined accounting entries that ensure accurate reflection of the company's financial position and performance. From initial recognition, interest accruals, to final collection, each step demands meticulous attention to detail and adherence to accounting standards.

Properly recording these transactions:

- Ensures compliance with GAAP or IFRS.
- Provides stakeholders with transparent and reliable financial information.

- Facilitates effective cash flow and receivables management.

By understanding each aspect—interest calculation, timing, journal entries, and implications—accountants and financial managers can manage notes receivable efficiently, minimizing errors and optimizing financial reporting.

Final Thoughts:

Mastering the accounting treatment of notes receivable like those issued by Valley Designs not only enhances financial accuracy but also supports strategic decision-making. Whether managing credit policies, assessing liquidity, or forecasting revenue, accurate entries and understanding of the underlying principles are fundamental for sound financial management.

How Entries For Notes Receivable Valley Designs Issued A 90 Day 8 Note For 54 000 Dated April 17

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