

Accounting for Merchandising Activities

Chapter 6 – Appendix 6A

Periodic Inventory

ACC2311 – Accounting Concepts II
Winter 2013

Learning Objectives

1. Compare and contrast the periodic and perpetual merchandise inventory systems
2. Prepare journal entries using a periodic inventory system
3. Prepare financial statements using a periodic inventory system

Merchandising Activities

Merchandiser

A company that earns net income by buying and selling merchandise.

Service Company

A company that sells a 'service'.

Computing Net Income

Merchandiser

Net Sales

—

Cost of Goods Sold

=

Gross Profit

—

Operating Expenses

=

Net Income

Service Company

Revenues

—

Operating Expenses

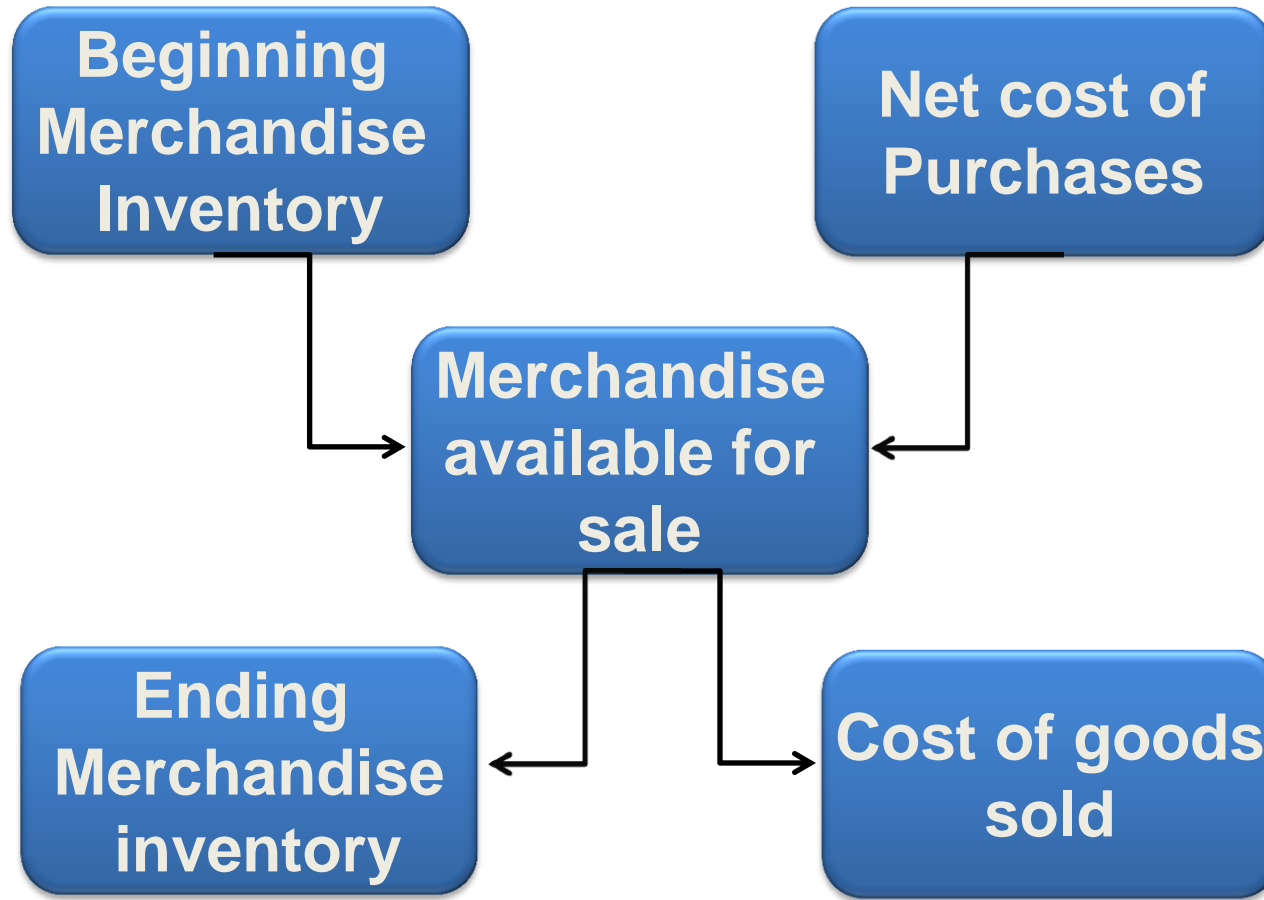
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Net Income

Inventory

- Products a company owns for the purpose of selling to customers.
 - often called Merchandise Inventory
 - classified as a current asset
- Cost of merchandise inventory includes:
 - costs incurred to purchase the goods
 - shipping costs
 - any other costs required to make goods ready for sale

Inventory Cost Flow



Merchandise Inventory Systems

Perpetual

Provides a continuous record of:

- the amount of merchandise inventory on hand
- cost of goods sold to date

Periodic

Requires a physical count of goods to determine:

- the amount of merchandise inventory on hand
- cost of goods sold

Perpetual System - example

Purchases

| | | |
|--|--------------|--------------|
| Nov. 2 Merchandise Inventory | 1,200 | |
| Accounts Payable | | 1,200 |
| <i>Purchased merchandise inv. on account</i> | | |

Purchase Returns and Allowances

| | | |
|--|------------|------------|
| Nov.5 Accounts Payable | 300 | |
| Merchandise Inventory | | 300 |
| <i>Purchase allowance re: debit memo</i> | | |

Perpetual System - example

Purchase Discounts

Assume the purchase of merchandise inventory on November 2 was on the **terms 2/10, n30**.

| | | | | |
|---------------|---------------|--------------------------------|------------|------------|
| Case 1 | Nov.12 | Accounts Payable | 900 | |
| Discount | | Merchandise Inventory | | 18 |
| taken | | Cash | | 882 |
| | | <i>(1,200 - 300) x 2% = 18</i> | | |

| | | | | |
|------------------|---------------|-------------------------|------------|------------|
| Case 2 | Nov.13 | Accounts Payable | 900 | |
| Discount | | Cash | | 900 |
| not taken | | | | |

Perpetual System - example

Transportation Costs

| | | | |
|---------------|---|-----------|-----------|
| Nov.24 | Merchandise Inventory | 75 | |
| | Cash | | 75 |
| | <i>Paid freight charges on purchased merchandise.</i> | | |

Who owns the goods?

FOB Shipping Point: **Buyer pays shipping charges**

FOB Destination: **Seller pays shipping charges**

Perpetual System - example

Sales of Merchandise

| | | | |
|---------------|--|--------------|--------------|
| Nov.12 | Accounts Receivable | 1,000 | |
| | Sales | | 1,000 |
| | <i>Sold merchandise on terms 2/10, n60</i> | | |
| | Cost of goods sold | 600 | |
| | Merchandise Inventory | | 600 |
| | <i>To record cost of merchandise sold</i> | | |

Perpetual System - example

Customer Payment

| | | | | |
|---------------|---------------|----------------------------|--------------|---|
| Case 1 | Nov.22 | Cash | 980 | |
| Customer pays | | Sales discounts | 20 | |
| in 10 days | | Accounts receivable | | 1,000 |
| | | | | <i>Received payment less the discount</i> |
| | | | | |
| Case 2 | Jan.11 | Cash | 1,000 | |
| Customer pays | | Accounts receivable | | 1,000 |
| in 60 days | | | | <i>Received payment for Nov. 12 sale</i> |

Perpetual System - example

Sales Returns and Allowances

| | | | |
|--------------|--|------------|------------|
| Nov.6 | Sales Returns & Allowances | 800 | |
| | Accounts Receivable | | 800 |
| | <i>Customer returned merchandise</i> | | |
| | Merchandise Inventory | 600 | |
| | Cost of Goods Sold | | 600 |
| | <i>Returned goods to merchandise inventory</i> | | |

Periodic vs. Perpetual Merchandise Inventory Systems

Perpetual

Merchandise Inventory is updated after each sale or purchase.

Periodic

Merchandise Inventory is updated at the end of the period based on a physical count.

Periodic vs. Perpetual Merchandise Inventory Systems

Perpetual

- keeps a running total of inventory levels by recording sales and purchase transactions
- periodic adjustments must be made to account for shrinkage (loss due to theft or deterioration of merchandise inventory).

Periodic vs. Perpetual Merchandise Inventory Systems

Periodic

- only periodically determine your inventory level (with a physical count)
- more difficult to determine shrinkage

Quick Check ✓

Prepare journal entries for each of the following transactions.
Assume a **perpetual** merchandise inventory system:

Oct 6: Purchased 650 units of merch. inventory at \$5/unit
The seller offered a cash discount of 2/10, n/30.

| | | | |
|--------------|------------------------------|--------------|--------------|
| Oct.6 | Merchandise Inventory | 3,250 | |
| | A/P | | 3,250 |
| | <i>(650 x 5)</i> | | |

Quick Check ✓

Prepare journal entries for each of the following transactions. Assume a **perpetual** merchandise inventory system:

Oct 8: Returned 25 defective units and received full credit.

| | | | |
|---------------|------------------------------|------------|------------|
| Oct. 8 | A/P | 125 | |
| | Merchandise Inventory | | 125 |
| | <i>(25 x 5)</i> | | |

Quick Check ✓

Prepare journal entries for each of the following transactions.
Assume a **perpetual** merchandise inventory system:

Oct 10: Paid the amount in full, less the returned items.

| | | | |
|----------------|------------------------------|--------------|-----------------|
| Oct. 10 | A/P | 3,125 | |
| | Merchandise Inventory | | 62.50 |
| | Cash | | 3,062.50 |
| | <i>(3,250-125) x 2%</i> | | |

Periodic System - compared

Periodic System

Perpetual System

Purchase of Merchandise

| | | | | | |
|------------------|-------|-------|------------------|-------|-------|
| Purchases | 1,200 | | Merchandise Inv. | 1,200 | |
| Accounts Payable | | 1,200 | Accounts Payable | | 1,200 |

Return of Merchandise

| | | | | | |
|------------------|-----|-----|------------------|-----|-----|
| Accounts Payable | 300 | | Accounts Payable | 300 | |
| Purchase Returns | | 300 | Merchandise Inv. | | 300 |

Periodic System - compared

Periodic System

Perpetual System

Purchase Discount Taken (2/10, n30)

| | | | | | |
|--------------------|-----|-----|------------------|-----|-----|
| Accounts Payable | 900 | | Accounts Payable | 900 | |
| Purchase Discounts | | 18 | Merchandise Inv. | | 18 |
| Cash | | 882 | Cash | | 882 |

Transportation Charges

| | | | | | |
|-------------------|----|----|------------------|----|----|
| Transportation-in | 75 | | Merchandise Inv. | 75 | |
| Accounts Payable | | 75 | Accounts Payable | | 75 |

Periodic System - compared

Periodic System

Perpetual System

Sale of merchandise

| | | | | | |
|---------------------|-------|-------|---------------------|-------|-------|
| Accounts Receivable | 2,400 | | Accounts Receivable | 2,400 | |
| Sales | | 2,400 | Sales | | 2,400 |
| | | | Cost of Goods Sold | 1,600 | |
| | | | Merchandise Inv. | | 1,600 |

Periodic System - compared

Periodic System

Perpetual System

Sales Return

| | | | | | |
|---------------------|-----|-----|---------------------|-----|-----|
| Sales Returns | 800 | | Sales Returns | 800 | |
| Accounts Receivable | | 800 | Accounts Receivable | | 800 |
| | | | Merchandise Inv. | 600 | |
| | | | Cost of Goods Sold | | 600 |

Periodic System - compared

Periodic System

Perpetual System

Inventory adjustment following physical count:

| | | | | | |
|----------|--|--|---|-----|-----|
| No entry | | | Cost of goods sold | 800 | |
| | | | Merch inventory | | 800 |
| | | | To record inventory shrinkage revealed by physical count. | | |

Quick Check ✓

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