# Lesson: Merchandise Accounting

There are two methods:

1. Periodic
2. Perpetual

**To Learn and Practice:**

"***First Practice***" Whole Cycle from Worksheet on.

Remember you can review ALL of this online *WITH* practice exercises at:

www.StudCo.ca

## 1. Journalize

New concept of selling a good versus a service
Requires understanding of Inventory vs. Supplies
Go over inventory cycle here.

*New accounts:*

Merchandise Inventory
Sales, not Fees Earned
Sales Discounts
Sales Returns and Allowances (contra)
Purchases
Purchase Discounts
Purchase Returns and Allowances (contra)
Freight-in
Freight-out (delivery expense)

**To Learn and Practice:**

"***Merch. Lesson***" Journal Entries (printout)

## 2. Post

Nothing new.

## 3. On Worksheet: Balance with Trial Balance

Nothing new.

## 4. On Worksheet: Perform adjustments and complete

Inventory cycle: (B+P-PD-PRA+FI-E=COGS); inventory count (just like supplies)
O/H – New lines, calculate COGS

## 5. Produce Financial Statements

New Format for I/S

**To Learn and Practice:**

"***Exercise 22***" pg 395 in workbook Schedule of Cost of Goods Sold (COGS section of Income Statement.)

**To Learn and Practice:**

"***Exercise 17***" pg 386 Assignment (worksheet, adjustments, closing entries)

## 6. Journalise and Post Adjustments

Same

## 7. Closing Entries

Still close out all accounts from Drawings down.
But also must update Merchandise inventory

# Service Business vs. Merchandising Business

## 1. Journal Entries

### (A) Paying for Goods or Services or Buying Assets (A)

General Journal — PAGE: ______

| Date 2002 | | Particulars | P.R. | Debit | Credit |
|---|---|---|---|---|---|
| Jan | 4 | Supplies | | 540 ~ | |
| | | GST Recoverable | | 30 ~ | |
| | | Accounts Payable | | | 570 ~ |
| | | Purchased $500 of supplies on | | | |
| | | account plus GST and PST. | | | |

Whether an expense or an asset, there is **NO** difference here between the two.

General Journal — PAGE: ______

| Date 2002 | | Particulars | P.R. | Debit | Credit |
|---|---|---|---|---|---|
| Jan | 4 | Auto Expense | | 540 ~ | |
| | | GST Recoverable | | 30 ~ | |
| | | Accounts Payable | | | 570 ~ |
| | | Bought $500 of gas on account | | | |
| | | All taxes were applicable. | | | |

### *(A) Returning (or receiving credit for) Items Other Than Merchandise (A)*

General Journal — PAGE: ______

| Date 2002 | | Particulars | P.R. | Debit | Credit |
|---|---|---|---|---|---|
| Jan | 5 | Accounts Payable | | 570 ~ | |
| | | GST Recoverable | | | 30 ~ |
| | | Supplies | | | 540 ~ |
| | | Returned $500 of supplies bought on account | | | |
| | | GST and PST were applicable | | | |

General Journal — PAGE: ______

| Date 2002 | | Particulars | P.R. | Debit | Credit |
|---|---|---|---|---|---|
| Jan | 5 | Accounts Payable | | 570 ~ | |
| | | GST Recoverable | | | 30 ~ |
| | | Auto Expense | | | 540 ~ |
| | | Received credit for $500 of gas | | | |
| | | GST and PST was applicable | | | |

NOTE that instead of *Accounts Payable*, this could be *Bank* or *Accounts Receivable,* if we've already paid for the goods. This is true for ALL returns.

### (A2) Paying for the Purchase of MERCHANDISE (Goods for Resale) (A2)

Remember: the "PURCHASES" account is only for the purchase of merchandise for resale.

IMPORTANT: Suppliers do not charge PST on items that will be resold.

General Journal — PAGE: ______

| Date 2002 | | Particulars | P.R. | Debit | Credit |
|---|---|---|---|---|---|
| | | Purchases | | 700 ~ | |
| | | GST Recoverable | | 42 ~ | |
| | | Accounts Payable | | | 742 ~ |
| | | Purchased $700 of goods on account | | | |
| | | Only GST applies. | | | |

The **difference** is **here** when merchandise is bought or returned. There is no comparable equivalent for a service business.

### *(A2) Returning a Purchase of MERCHANDISE (A2)*

Likewise, BOTH of the Returns and Allowances accounts are for use only when merchandise items are returned.

General Journal — PAGE: ______

| Date 2002 | | Particulars | P.R. | Debit | Credit |
|---|---|---|---|---|---|
| Jan | 5 | Accounts Payable | | 742 ~ | |
| | | GST Recoverable | | | 42 ~ |
| | | Purchase Returns & Allowances | | | 700 ~ |
| | | Returned $500 of goods bought on account | | | |
| | | Only GST was applicable. | | | |

# Service Business Merchandis

## (B) Selling a Good or Service (B)

| General Journal | | | | | PAGE: ______ |
|---|---|---|---|---|---|
| Date 2002 | | Particulars | P.R. | Debit | Credit |
| Jan | 5 | Accounts Receivable | | 1060~ | |
| | | GST Payable | | | 60~ |
| | | Fees Revenue | | | 1000~ |
| | | Performed legal services | | | |
| | | on account for $1000. No PST | | | |

Remember: there is no PST on services.

| General Journal | | | | | PAGE: ______ |
|---|---|---|---|---|---|
| Date 2002 | | Particulars | P.R. | Debit | Credit |
| Jan | 5 | Accounts Receivable | | 1140~ | |
| | | GST Payable | | | 60~ |
| | | PST Payable | | | 80~ |
| | | Sales | | | 1000~ |
| | | Sold goods on account for | | | |
| | | $1000. GST and PST applied | | | |

## *(B) Having a Sale Returned or Granting a Credit for a Service Performed (B)*

| General Journal | | | | | PAGE: _____ |
|---|---|---|---|---|---|
| Date 2002 | | Particulars | P.R. | Debit | Credit |
| Jan | 5 | Fees Revenue | | 1000~ | |
| | | GST Payable | | 60~ | |
| | | Accounts Receivable | | | 1060~ |
| | | Credit given to irate customer | | | |
| | | for $1000. No PST applied | | | |
| | | | | | |

Remember: there is no PST on services.

| General Journal | | | | | PAGE: _____ |
|---|---|---|---|---|---|
| Date 2002 | | Particulars | P.R. | Debit | Credit |
| Jan | 5 | Sales Returns & Allowances | | 1000~ | |
| | | GST Payable | | 60~ | |
| | | PST Payable | | 80~ | |
| | | Accounts Receivable | | | 1140~ |
| | | Sales on account of $1000 were | | | |
| | | returned. Both taxes applied. | | | |

NOTE that instead of *Accounts Receivable*, this could be *Bank* or *Accounts Payable* if the customer has already paid.

BOTH of the Returns and Allowances accounts are for use only when merchandise items are returned.

**Remember:**

Value Before Taxes = Value with taxes / (1 + tax rate)

$$\text{Value Before Taxes} = \frac{\text{Value with taxes}}{(1 + \text{tax rate})}$$

## 2. Posting

There is no difference here.

## 3. Worksheet

NOTE: the only difference on the Worksheet is the line for Merchandise Inventory. All other accounts (new and old) are handled in the same fashion. Can you see how the 5 lines below calculate the Cost of Goods Sold? That's why they're listed on the Income Statement.

A Partial Worksheet for a **Merchandising** Company

| Accounts | Trial Balance DR | Trial Balance CR | Adjustments DR | Adjustments CR | Income Statement DR | Income Statement CR | Balance Sheet DR | Balance Sheet CR |
|---|---|---|---|---|---|---|---|---|
| Merchandise Inventory | 13 500 ~ | | | | 13 500 ~ | 15 250 ~ | 15 250 ~ | |
| | | | | | | | | |
| | | | | | | | | |
| Purchases | 5 000 ~ | | | | 5 000 ~ | | | |
| Purchase Discounts | | 250 ~ | | | | 250 ~ | | |
| Purchase Returns and Allowances | | 500 ~ | | | | 500 ~ | | |
| Freight-in | 500 ~ | | | | 500 ~ | | | |

Beginning Inventory

Inventory appears on the I/S because it is needed to calculate the C.O.G.S.

Ending Inventory

## 4. Adjusting Entries

There is no difference here

# 5. The Financial Statements

**NOTE: there is no real difference in the way you construct the Balance Sheet. You use the new 3-column format for both types of businesses. The only exception is the Merchandise Inventory account: it obviously doesn't appear on the Balance Sheet of a Service company since you have no inventory.**

**There are numerous differences in the Income Statement between a service company and a merchandising business. The largest difference is that a service business has no need for a *Cost of Goods Sold* section.**

**From the worksheet the following statements would be constructed:**

| | | |
|---|---|---|
| **A Service Company** | | |
| Income Statement | | |
| Month Ended January 31, 2003 | | |
| **Revenue** | | |
| Fees Revenue | $ 10,000 | |
| *Total Revenue* | | $ 10,000 |
| **Operating Expenses** | | |
| Auto Expense | $ 1,000 | |
| Delivery Expense | 100 | |
| Depreciation Expense - Auto | 300 | |
| Insurance Expense | 200 | |
| Salaries Expense | 1,500 | |
| Supplies Expense | 500 | |
| *Total Operating Expenses* | | 3,600 |
| **Income before Interest, Taxes (and Extraordinary Items)** | | **$ 6,400** |
| Loss on Disposal of Asset | $ 1,000 | |
| *Total Non-Operating Expenses* | | 1,000 |
| **Net Income** | | **$ 5,400** |

# A Merchandising Company

## Income Statement

## Month Ended January 31, 2003

### Operating Revenue

| | | | |
|---|---|---|---|
| Sales | | $ 10,000 | |
| Less: Sales Discounts | (100) | | |
| Less: Sales Returns and Allowances | (400) | (500) | |
| *Net Sales* | | | $ 9,500 |

### Cost of Goods Sold

| | | | |
|---|---|---|---|
| Merchandise Inventory, January 1 | | $ 13,500 | |
| Add: Purchases | $ 5,000 | | |
| Less: Purchase Discounts | (250) | | |
| Less: Purchase Returns and Allowances | (500) | | |
| Net Purchases | | 4,250 | |
| Add: Freight-in | | 500 | |
| Goods Available for Sale | | 18,250 | |
| Less: Merchandise Inventory, January 31 | | (15,250) | |
| Cost of Goods Sold | | | 3,000 |
| *Gross Profit* | | | $ 6,500 |

### Operating Expenses

| | | | |
|---|---|---|---|
| Auto Expense | | $ 1,000 | |
| Freight-out/Delivery Expense | | 100 | |
| Depreciation Exp. - Auto | | 300 | |
| Insurance Expense | | 200 | |
| Salaries Expense | | 1,500 | |
| Supplies Expense | | 500 | |
| *Total Operating Expenses* | | | 3,600 |
| **Operating Income** (Income before Interest, Taxes and Extraordinary Items) | | | **$ 2,900** |
| Loss on Disposal of Asset | | $ 1,000 | |
| *Total Non-Operating Expenses* | | | 1,000 |
| **Net Income** | | | **$ 1,900** |

# 6. Closing Entries

This is an asset. It is the new inventory balance. This is why it's a debit. This entry sets up the new inventory balance in the account for next period.

General Journal PAGE: ______

| Date 2003 | | Particulars | P.R. | Debit | Credit |
|---|---|---|---|---|---|
| Jan | 31 | Fees Revenue | | 10 0 0 0 ~ | |
| | | Income Summary | | | 10 0 0 0 ~ |
| | | | | | |
| | 31 | Income Summary | | 4 6 0 0 ~ | |
| | | Auto Expense | | | 1 0 0 0 ~ |
| | | Delivery Expense | | | 1 0 0 ~ |
| | | Depreciation Exp. - Auto | | | 3 0 0 ~ |
| | | Insurance Expense | | | 2 0 0 ~ |
| | | Loss on disposal of Asset | | | 1 0 0 0 ~ |
| | | Salaries Expense | | | 1 5 0 0 ~ |
| | | Supplies Expense | | | 5 0 0 ~ |
| | | | | | |
| | 31 | Income Summary | | 5 4 0 0 ~ | |
| | | J. Smith, Capital | | | 5 4 0 0 ~ |
| | | | | | |
| | 31 | J. Smith, Capital | | 5 0 0 ~ | |
| | | J. Smith, Drawings | | | 5 0 |
| | | | | | |

General Journal PAGE: ______

| Date 2003 | | Particulars | P.R. | Debit | Credit |
|---|---|---|---|---|---|
| Jan | 31 | Sales | | 10 0 0 0 ~ | |
| | | Purchase Discounts | | 2 5 0 | |
| | | Purchase Returns & Allowances | | 5 0 0 ~ | |
| | | **Merchandise Inventory (ending)** | | 15 2 5 0 ~ | |
| | | Income Summary | | | 26 0 0 0 ~ |
| | | | | | |
| | 31 | Income Summary | | 24 1 0 0 ~ | |
| | | **Merchandise Inventory (begin.)** | | | 13 5 0 0 ~ |
| | | Auto Expense | | | 1 0 0 0 ~ |
| | | Delivery Expense | | | 1 0 0 ~ |
| | | Depreciation Exp. - Auto | | | 3 0 0 ~ |
| | | Insurance Expense | | | 2 0 0 ~ |
| | | Loss on disposal of Asset | | | 1 0 0 0 ~ |
| | | Purchases | | | 5 0 0 0 ~ |
| | | Freight-in | | | 5 0 0 ~ |
| | | Salaries Expense | | | 1 5 0 0 ~ |
| | | Sales Discounts | | | 1 0 0 ~ |
| | | Sales Returns & Allowances | | | 4 0 0 ~ |
| | | Supplies Expense | | | 5 0 0 ~ |
| | | | | | |
| | 31 | Income Summary | | 1 9 0 0 ~ | |
| | | J. Smith, Capital | | | 1 9 0 0 ~ |
| | | | | | |
| | 31 | J. Smith, Capital | | 5 0 0 ~ | |
| | | J. Smith, Drawings | | | 5 0 0 ~ |
| | | | | | |
| | | | | | |

This credit entry eliminates the old inventory balance from the account to start fresh for next period.