

CHAPTER TWELVE

THE PURCHASING CYCLE: PURCHASES PURCHASE RETURNS CASH PAYMENTS

PURCHASES

- Merchandise for resale
- Businesses-to-business purchases usually on account

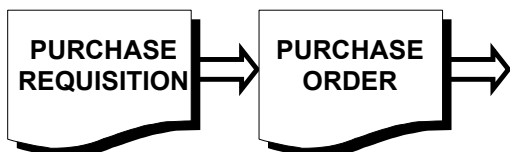
PURCHASING DOCUMENTS



PURCHASE REQUISITION

- Request purchase of inventory
- Created by assistant store manager
- Approved by store manager
- Three copies
 - Original to Purchasing department
 - Copy to Accounting department
 - Copy kept in originating store

PURCHASING DOCUMENTS



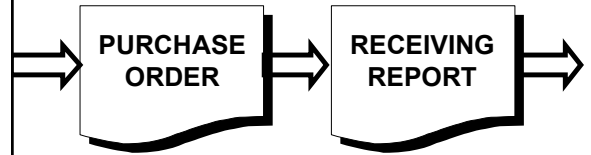
PURCHASE ORDER

- Written order to buy goods
- One central office for entire company
- Purchasing department
 - Reviews purchase requisitions
 - Approves purchase requisitions
 - Groups together, makes large purchases
 - Select vendor from approved list

PURCHASE ORDER

- Prepared by assistant manager
- Approved by purchasing manager
- Purchase order (five copies)
 - Original to vendor
 - Copy to Accounting department
 - Copy kept in Purchasing department
 - Copy to receiving department
 - Copy to store initiating purchase

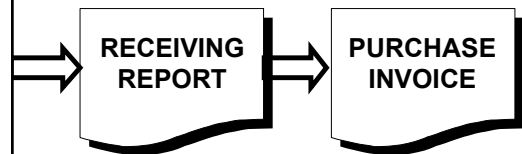
PURCHASING DOCUMENTS



RECEIVING REPORT

- Prepared by the receiving clerk
- Approved by receiving manager
- Match purchase order to merchandise
- Lists merchandise received
 - Date of receipt
 - Condition of goods
- Three copies of receiving report
 - One copy to Purchasing
 - One copy to Accounting
 - Keep original in Receiving

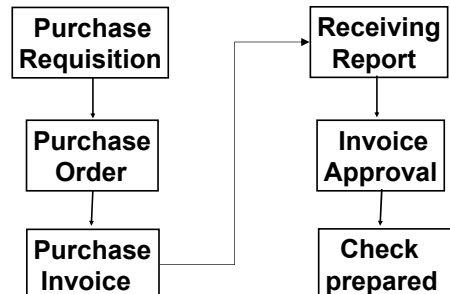
PURCHASING DOCUMENTS



PURCHASE INVOICE

- Prepared by seller
- Refer to purchase order number
- Bill for merchandise shipped
- List items shipped
- List back ordered items
- Seller calls it a sales invoice.
- Buyer calls it a purchase invoice.

PURCHASING DOCUMENTS



Document Flow for Merchandise

PAYMENT APPROVAL

- **Accounting manager matches**
 - Purchase Requisition
 - Purchase Order
 - Receiving Report
 - Invoice
- **Check documents for agreement**
- **Print check**
- **Place four documents and check in folder**
- **Owner reviews documents, signs check**
- **If amount over \$10,000 two signatures**

CASH DISCOUNTS

- **From chapter 11**
- **Available if amount due paid within discount period**
- **Example: 2/10 n/30**
- **Buyer calls it a Purchase Discount.**
- **Seller calls it a Sales Discount.**

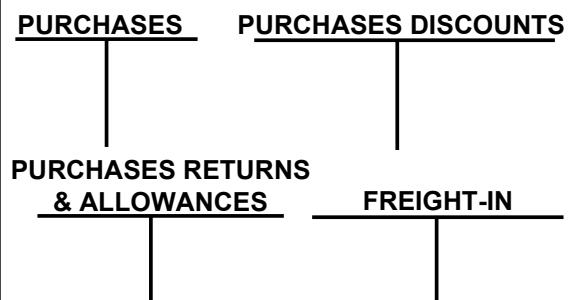
TRADE DISCOUNTS

- **Offered by seller**
- **Reduction from the list price**
 - High volume customer customers
 - Sales promotions
- **Buyer and seller record transaction at NET amount (after discount)**

TRADE DISCOUNT

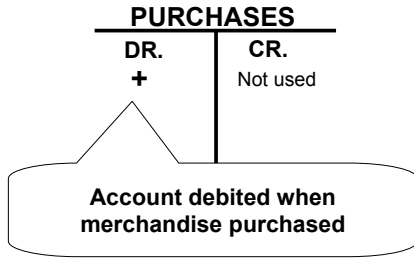
List price	\$1,000
Trade discount	<u>10%</u>
Net amount (1,000 x 90%)	\$900
Trade discount	<u>20%</u>
Net amount (900 x 80%)	<u>\$720</u>
Buyer and seller record \$720	

MERCHANDISE ACCOUNTS



PURCHASES ACCOUNT

Used to record cost of merchandise purchased



GENERAL JOURNAL					
DATE	DESCRIPTION	PR	DEBIT	CREDIT	
1	Purchases		100 00		
2	Cash			100 00	
3	Made cash purchase				
4					
5					
6					
7					
8					
9					
10					
11					

Made \$100 purchase for cash

GENERAL JOURNAL					
DATE	DESCRIPTION	PR	DEBIT	CREDIT	
1	Purchases		100 00		
2	Accts. Payable/Vendor			100 00	
3	Made purchase on account				
4					
5					
6					
7					
8					
9					
10					
11					

What if purchase made on account?

GENERAL JOURNAL					
DATE	DESCRIPTION	PR	DEBIT	CREDIT	
1	Purchases		100 00		
2	Accts. Payable/Vendor			100 00	
3	Made purchase on account				
4					
5					
6					
7					
8					
9					
10					
11					

Credit Accounts Payable instead of cash

GENERAL JOURNAL					
DATE	DESCRIPTION	PR	DEBIT	CREDIT	
1	Purchases		100 00		
2	Accts. Payable/Vendor			100 00	
3	Made purchase on account				
4					
5					
6					
7					
8					
9					
10					
11					

The specific supplier is identified.

PURCHASE RETURNS AND ALLOWANCES

CONTRA account to record purchase returns and purchase allowances.

PURCHASES RETURNS & ALLOWANCES

DR.	CR.
Not used	+

The account is credited for the amount of returns and allowances.

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1					
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					

Merchandise purchased on account for \$200 is defective and returned to the supplier.

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Accts. Payable/Vendor		200 00	
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					

Accounts Payable debited. Specific vendor is identified.

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Accts. Payable/Vendor		200 00	
2		Pur. Returns & Allow.			200 00
3		Returned merchandise			
4					
5					
6					
7					
8					
9					
10					
11					

Purchases Returns & Allowances credited. Shown as deduction from Purchases account on Income Statement.

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1					
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					

Merchandise retained but supplier grants a price reduction of \$45 because of defects

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Accts. Payable/Vendor		45 00	
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					

Accounts Payable debited to reflect price reduction.

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Accts. Payable/Vendor		45 00	
2		Pur. Returns & Allow.			45 00
3		Allowance for defective merchandise			
4					
5					
6					
7					
8					
9					
10					
11					

Purchases Returns & Allowances credited. Same as the entry for Returns!

PURCHASES DISCOUNTS

CONTRA account to record cash discounts

PURCHASES DISCOUNTS

DR. Not used	CR. +
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Credited for discount granted by vendor for prompt payment, 2/10 n/30.

GENERAL JOURNAL

DATE	DESCRIPTION	PR	DEBIT	CREDIT
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				

Merchandise purchased for \$100
credit terms 2/10, n/30
payment made within discount period.

GENERAL JOURNAL

DATE	DESCRIPTION	PR	DEBIT	CREDIT
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				

Accounts Payable debited for entire amount of purchase

GENERAL JOURNAL

DATE	DESCRIPTION	PR	DEBIT	CREDIT
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				

Cash credited for actual amount paid, \$98
(\$100 - \$2 discount)

GENERAL JOURNAL

DATE	DESCRIPTION	PR	DEBIT	CREDIT
1				
2				
3				
4				
5				
6				
7				
8				
9				
10				
11				

Purchase Discounts credited for discount amount, \$2 (\$100 x 2%).

FREIGHT-IN

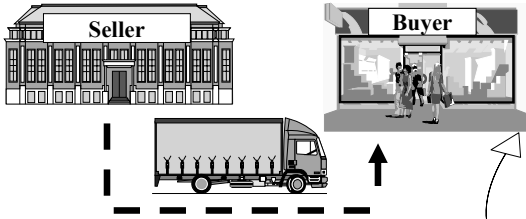
ADJUNCT-PURCHASES account to record transportation charges

FREIGHT-IN

DR. +	CR. Not used
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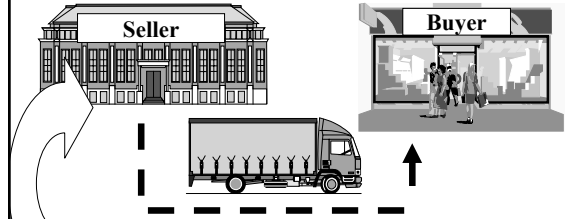
Account debited for transportation charges.

FOB DESTINATION



- Title passes at destination
- No sale or purchase recorded until destination
- Seller responsible for inventory while in transit

FOB SHIPPING POINT



- Title passes at shipping point
- Both sale and purchase recorded upon shipment
- Buyer responsible for inventory while in transit

TRANSPORTATION CHARGES

Where does title change hands?

- FOB Shipping Point:**
 - When goods placed on truck by seller
 - Buyer pays transportation, insurance charges
 - If seller pays buyer charged on invoice
- FOB Destination:**
 - When goods placed on receiving dock of buyer
 - Seller pays transportation, insurance charges

GENERAL JOURNAL

	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1					
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					

Merchandise purchased
for \$400 plus freight charges of \$38

GENERAL JOURNAL

	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Purchases		400 00	
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					

Purchases debited for
cost of merchandise.

GENERAL JOURNAL

	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Purchases		400 00	
2		Freight-In		38 00	
3					
4					
5					
6					
7					
8					
9					
10					
11					

Freight-In debited
for transportation costs,
FOB shipping point,
buyer pays freight.

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Purchases		400 00	
2		Freight-In		38 00	
3		Accts. Payable/Vendor			438 00
4		Made purchase on account			
5					
6					
7					
8					
9					
10					
11					

Accounts Payable credited for entire purchase price (merchandise + freight).

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1					
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					

What if freight charges were on a separate bill from the transportation company?

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Purchases		400 00	
2					
3					
4					
5					
6					
7					
8					
9					
10					
11					

Purchases debited for cost of merchandise

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Purchases		400 00	
2		Accts. Payable/Vendor			400 00
3		Made purchase on account			
4					
5					
6					
7					
8					
9					
10					
11					

Accounts Payable credited for amount due to supplier

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Purchases		400 00	
2		Accts. Payable/Vendor			400 00
3		Made purchase on account			
4					
5					
6					
7					
8					
9					
10					
11					

Separate journal entry made to record freight charges.

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1		Purchases		400 00	
2		Accts. Payable/Vendor			400 00
3		Made purchase on account			
4					
5		Freight-In		38 00	
6		Accts. Payable/Shipper			38 00
7		Freight charges on purchase			
8					
9					
10					
11					

Accounts Payable credited, vendor is transportation company

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1	April 10	Accts. Payable/B.B. Small		4,800 00	
2		Cash			4,800 00
3		Made payment on account			
4					
5					
6					
7					
8					
9					
10					
11					

Cash Payments

ACCOUNTS PAYABLE VENDOR LEDGERS

- Individual accounts payable account for each vendor
- When A/P debited or credited vendor ledger debited or credited
- Accounts Payable general ledger account called "control account."

ACCOUNTS PAYABLE VENDOR LEDGERS

Also called

- Subsidiary ledgers
- Accounts Payable ledgers

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1	April 4	Purchases		3,300 00	
2		Accts. Pay/Compucraft			3,300 00
3		Invoice No. 631			
4					
5					
6					
7					
8					
9					
10					
11					

**Organize transactions by
vendor and invoice**

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1	April 4	Purchases		3,300 00	
2		Accts. Pay./Compucraft			3,300 00
3		Invoice No. 631			
4					
5					
6					
7					
8					
9					
10					
11					

Credit posted to controlling account

POST TO ACCOUNTS PAYABLE

ACCOUNTS PAYABLE	
DR.	CR.
	3300.00

As we have always done...

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1	April 4	Purchases		3,300 00	
2		Accts. Pay./Compucraft			3,300 00
3		Invoice No. 631			
4					
5					
6					
7					
8					
9					
10					
11					

Now we need to post to the individual supplier's account.

POST TO VENDOR LEDGER	
ACCOUNTS PAYABLE COMPUCRAFT	
DR.	CR.
	3300.00

When Accounts Payable credited vendor ledger credited

GENERAL JOURNAL					
	DATE	DESCRIPTION	PR	DEBIT	CREDIT
1	May 4	Accts. Payable/Televax		200 00	
2		Purchases Ret. & Allow.			200 00
3		Returned Merchandise			
4					
5					
6					
7					
8					
9					
10					
11					

Purchase Returns

SCHEDULE OF ACCOUNTS PAYABLE
<ul style="list-style-type: none"> ▪ Listing of vendors and balances ▪ Prepared end of month ▪ Total of vendor balances must equal Accounts Payable account

Northern Micro Schedule of Accounts Payable April 30, 20--		
Compucraft, Inc.		\$3,300
Datasoft		2,500
Printpro Corp.		800
Televax, Inc.		5,300
		<u>\$11,900</u>

Total should equal Accounts Payable general ledger

PRACTICE PROBLEMS
Exercises 1, 2, 3, 5, 6, 7, 8

GROSS PROFIT

- Textbook page 412
- Also called Gross Margin
- Difference between selling price and purchase cost of units sold

GROSS PROFIT

$$\begin{array}{r} \text{NET SALES} \\ - \text{COST OF GOODS SOLD} \\ \hline \text{GROSS PROFIT} \end{array}$$

EXAMPLE

20 hats sold. Selling price \$10 each.
Purchase cost \$7.50 each.

$$\begin{array}{r} \text{NET SALES} \\ - \text{COST OF GOODS SOLD} \\ \hline \text{GROSS PROFIT} \end{array}$$

\$200

20 hats x \$10 each = \$200 Sales
No Sales Returns & Allowances
No Sales Discounts

EXAMPLE

20 hats sold. Selling price \$10 each.
Purchase cost \$7.50 each.

$$\begin{array}{r} \text{NET SALES} \\ - \text{COST OF GOODS SOLD} \\ \hline \text{GROSS PROFIT} \end{array}$$

\$200 — \$150

20 hats x \$7.50 each = \$150

EXAMPLE

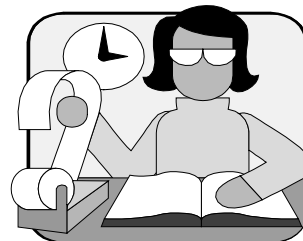
20 hats sold. Selling price \$10 each.
Purchase cost \$7.50 each.

$$\begin{array}{r} \text{NET SALES} \\ - \text{COST OF GOODS SOLD} \\ \hline \text{GROSS PROFIT} \end{array}$$

\$200 — \$150 = \$50

\$50 available to pay operating expenses

GROSS PROFIT



COST OF GOODS SOLD

GOODS AVAILABLE FOR SALE
— ENDING INVENTORY

COST OF GOODS SOLD

Sales			\$200,500	
Less: Sales returns & allow.			\$1,200	
Net Sales				\$199,300
Cost of Goods Sold:				
Merchandise Inv., Jan 1			\$26,000	
Purchases		\$105,000		
Less: Purchases ret. & allow.	\$ 800			
Purchases discounts	1,000	1,800		
Net purchases		\$103,200		
Add freight-in		300		
Cost of goods purchased			103,500	
Goods available for sale			\$129,500	
Less Merch. Inv., Dec. 31			18,000	

Out of \$129,500 of merchandise available to sell, \$18,000 not sold.

Sales			\$200,500	
Less: Sales returns & allow.			1,200	
Net Sales				\$199,300
Cost of Goods Sold:				
Merchandise Inv., Jan 1			\$26,000	
Purchases		\$105,000		
Less: Purchases ret. & allow.	\$ 800			
Purchases discounts	1,000	1,800		
Net purchases		103,200		
Add freight-in		300		
Cost of goods purchased			103,500	
Goods available for sale			129,500	
Less Merch. Inv., Dec. 31			18,000	
Cost of Goods Sold				111,500

Therefore \$111,500 of merchandise sold

GROSS PROFIT

NET SALES
— COST OF GOODS SOLD

GROSS PROFIT

Sales			\$200,500	
Less: Sales returns & allow.			1,200	
Net Sales				\$199,300
Cost of Goods Sold:				
Merchandise Inv., Jan 1			\$26,000	
Purchases		\$105,000		
Less: Purchases ret. & allow.	\$ 800			
Purchases discounts	1,000	1,800		
Net purchases		103,200		
Add freight-in		300		
Cost of goods purchased			103,500	
Goods available for sale			129,500	
Less Merch. Inv., Dec. 31			18,000	
Cost of Goods Sold				111,500
Gross Profit				87,800

The merchandise was sold for \$87,800 more than its cost.

End of Chapter 12