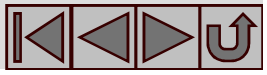
# Sale of Merchandise

- Sales are the mirror image of purchases
  - What the vendor records when you make an inventory purchase
- Sales process for merchandise inventory
- Recording sales
  - Sales Returns and Allowances
  - Sales Discounts
  - Net sales
  - Credit card sales and sales taxes



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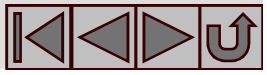


# Sales Process for Merchandise Inventory

- Steps in the sales process
  1. Customer places an order
  2. Company approves the order
  3. Warehouse selects goods for shipment
  4. Company ships goods
  5. Company bills customer for goods
  6. Company receives payment for the goods



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# *Recording Sales*

## *Transaction 5: Revenue* (1 of 3)

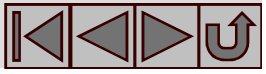
- GPS sells 11 skateboards on account for $250 each
  - Increase Sales $2,750
  - Increase AR $2,750

| | Dr. | Cr. |
|---|---|---|

| | Dr. | Cr. |
|---|---|---|



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# *Recording Sales*

## *Transaction 5: Expense* (2 of 3)

- How much did GPS pay for the 17 (20 – 3 returned) skateboards assuming they paid w/in the discount period?

| | |
|---|---|
| | $3,000 purchase price |
| + | 100 freight-in |
| - | 450 purchase return |
| - | 200 purchase allowance |
| | $2,400 for 17 skateboards |

- How much did each skateboard cost?



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# *Recording Sales*

## *Transaction 5: Expense* (3 of 3)

- GPS sells 11 skateboards on account for $250 each 1/15, n/30
  - Increase or decrease merchandise inventory?
  - Increase CoGS $2,750
    - On which fin. stmt. will you find CoGS?

| Dr. | Cr. |
|---|---|

| Dr. | Cr. |
|---|---|



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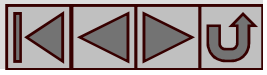
# Sales Returns and Allowances

## Transaction 6 (1 of 5)

- Contra-revenue account
  - Used to reduces a firm's revenue
- Net revenue
  - Revenue less contra-revenue
- Sales Returns and Allowances
  - Decrease revenue because you reduce a customer's AR account or give a cash refund (if the customer paid cash)



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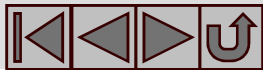
# Sales Returns and Allowances

## Transaction 6 (2 of 5)

- Customer returned one skateboard because it was defective
  - First, undo the revenue side of the transaction
    - What was the sale price of the merchandise?
  - Second, undo the expense side of the transaction
    - How much did the merchandise sold cost?



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# Sales Returns and Allowances

## Transaction 6: Reverse Revenue (3 of 5)

- The sales price was $250
  - Increase Sales Returns and Allowances
    - If revenues increase with credits, how would you increase a contra-revenue?
  - Decrease AR

| Dr. | Cr. |
|---|---|

| Dr. | Cr. |
|---|---|



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# Sales Returns and Allowances

## Transaction 6: Reverse Expense (4 of 5)

- Cost of the merchandise sold was $150
  - Reduce CoGS by $150
  - What happens to the inventory account?

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|---|---|

| Dr. | Cr. |
|---|---|



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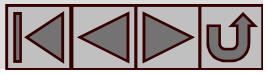
# Sales Returns and Allowances

## Transaction 6: Reverse Expense (5 of 5)

- How would the transaction change if GPS granted a Sales Allowance?
  - Would the revenue side of the sale need to be reversed?
  - Would the expense side of the sale need to be reversed?
- Why would a business record SR&A in a separate account?



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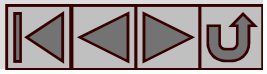


# Sales Discounts
## Transaction 7 (1 of 4)

- Sales discount
  - Reduction in sales price offered for prompt payment
  - Contra-revenue
    - Reduces net sales
  - Based on customer's outstanding balance from sales
    - Sales price less SR&A



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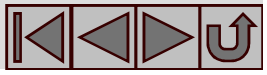


# Sales Discounts
## Transaction 7 (2 of 4)

- Amount to be received if payment is received w/in discount period
  - Cash collected
    - ($2,750 – $250) x (1 – 1%)
  - Sales discount – increases contra revenue
    - ($2,750 – $250) x 1%
  - Accounts receivable decreases by full amount owed
    - Customers balance completely satisfied for 99% of the amount due



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# Sales Discounts

## Transaction 7 (3 of 4)

- Make the journal entry if payment received w/in discount period
  - Increase Cash
  - Increase Sales Discounts
  - Decrease AR

| | | | | Accts. Rec. | |
|---|---|---|---|---|---|
| **Dr.** | **Cr.** | **Dr.** | **Cr.** | **Dr.** | **Cr.** |
| | | | | ❺2,750 | ❻250 |



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# Sales Discounts
## Transaction 7 (4 of 4)

- How would the journal entry change if the customer paid outside the discount period?
  - How much cash is received?

| | | | | Accts. Rec. | |
|---|---|---|---|---|---|
| Dr. | Cr. | Dr. | Cr. | Dr. | Cr. |
| | | | | ❺2,750 | ❻250 |



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# Net Sales

Sales

- Allowances given
- Sales Discounts

Net sales



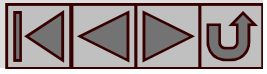
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# Credit Card Sales and Sales Taxes
*(1 of 4)*

- Bank cards
  - Cash sale
  - Credit card company pays seller full amount less a service fee (2% - 4%)
    - Service fee is an expense
  - E.g, Visa, MasterCard, American Express



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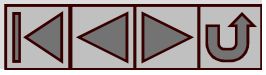


# Credit Card Sales and Sales Taxes
(2 of 4)

- Sales tax
  - Seller collects sales tax from customer and remits to state/local government
  - Liability
    - Sales tax payable



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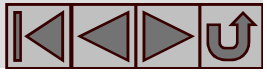


# Credit Card Sales and Sales Taxes
*(3 of 4)*

- Sell $100 of merchandise to customer
  - Sales tax rate is 5%
  - Customer pays with bank card with a 3% service fee
- Cash collected
  - $100 – (3% x $100) + (5% x $100)
- Service Revenue = $100



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# Credit Card Sales and Sales Taxes
(4 of 4)

- Journal entry
  - Increase Cash
  - Increase Service Fee (expense)
  - Increase Sales
  - Increase Sales Tax Payable

| Dr. | Cr. |
|---|---|

| Dr. | Cr. |
|---|---|

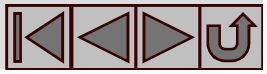
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# Recording Inventory
(1 of 2)

- Perpetual inventory system
  - Inventory records updated every time a purchase, sale, or return is made
- Periodic inventory system
  - Inventory records only updated at end of accounting period
- Both systems require an actual inventory count at end of period



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# Recording Inventory
(2 of 2)

- Perpetual inventory system can detect shrinkage
  - Shrinkage = Inventory account balance less actual inventory $$ amount based on physical count of merchandise



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# Multistep Income Statement
(1 of 2)

- Single-step income statement
  - All revenues presented first
  - All expense subtracted to arrive at net income



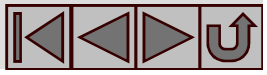
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# Multistep Income Statement
(2 of 2)

- Multiple-step income statement
  - Gross profit
    - Sales – CoGS
  - Operating income
    - Gross profit – operating expenses
  - Other revenues and expenses not directly related to firm's day-to-day operations



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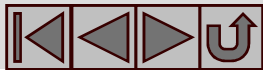
# Financial Statement Analysis

## Profitability Measures (1 of 4)

- Gross profit ratio
  - Gross Profit ÷ Sales
  - Portion of each sales $ a company has left after paying for goods it sold
  - Amount left over to cover operating and non-operating expenses and generate a profit



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# Financial Statement Analysis

## Profitability Measures (2 of 4)

- Profit margin ratio
  - Net Income ÷ Sales
  - Measures % of each sales $ that results in net income
  - A measure of how well a company is controlling its operating expenses



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# Financial Statement Analysis

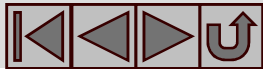
## Profitability Measures (3 of 4)

- Example: GPS's results for 2008 & 2009

| Year | 2008 | 2009 |
|---|---|---|
| Sales | $500,000 | $600,000 |
| CoGS | $300,000 | $400,000 |
| Net Income | $ 50,000 | $ 80,000 |
| Gross Profit Ratio | $200K/$500K=40% | $200K/$600K=33% |
| Profit Margin Ratio | $50K/$500K=10% | $80K/$600K=13% |



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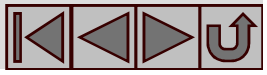
# Financial Statement Analysis

## Profitability Measures (4 of 4)

- Explain the trend in GPS's gross profit ratio
- Explain the trend in GPS's profit margin ratio
- What can you say about GPS's profitability based on these ratios?



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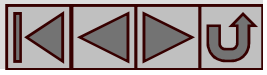


# Business Risk, Control, and Ethics

- Segregation of duties
  - Person with physical control over merchandise should NOT also do the record-keeping on the merchandise under her control
  - However, this control can be defeated if both people get together to commit fraud
    - See In the News—Risks and Controls



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