



Accounting for Merchandising Operations

Recording transactions related to the purchase of merchandise can be tricky as the entries change depending on whether the journal entries are for the BUYER or the SELLER. It is very important to be clear about which company is which when asked to record a transaction in the journal. There are four basic transactions listed below, with the BUYER's journal entries to the left and the corresponding entries in the SELLER's journal to the right.

- (1) Purchase/sale of merchandise:** For the **buyer**, purchases of merchandise are debited to Merchandise Inventory account and credited to cash or accounts payable. For the **seller**, the journal entries are a bit more involved. The first entry recognizes the revenue earned on the sale and the second entry recognizes the expense (Cost of Goods Sold) and the depletion of the seller's Merchandise Inventory. *If you have a problem where a company buys a good and resells it, you must find the cost of the good based on whether shipping was paid by the buyer, returns were made, and if discounts were received in buying it.*

Date	BUYER	Debit	Credit	SELLER	Debit	Credit
	Merchandise Inventory	\$800		Accounts Receivable**	\$800	
	Accounts Payable**		\$800	Sales Revenue		\$800
				Cost of Goods Sold	\$560	
**could also be Cash				Merchandise Inventory		\$560

- (2) Sales returns & allowances:** The **buyer** returns goods that are damaged or defective, or are not what the buyer ordered. The buyer receives a credit on A/P or debit to cash, depending on how goods were bought, and merchandise inventory is reduced by the value of the goods returned. A purchase allowance is similar, except the **buyer** chooses to keep the merchandise. For the **seller**, the expense account Sales Returns & Allowances must be debited and the A/R or cash credited for the amount of returned goods. Similarly, Merchandise Inventory and Cost of Goods Sold must also be adjusted for the cost of goods **returned**. (This second entry does not occur when a sales allowance is granted).

Date	BUYER	Debit	Credit	SELLER	Debit	Credit
	Accounts Payable**	\$400		Sales Returns & Allowances	\$400	
	Merchandise Inventory		\$400	Accounts Receivable**		\$400
				Merchandise Inventory	\$280	
**could also be Cash				Cost of Goods Sold		\$280

- (3) Sales Discounts:** If the goods are bought on account, the **buyer** may receive a cash discount for prompt payment of the purchase. When an invoice is paid within the discount period, both Cash and Merchandise Inventory are credited. Cash is the actual amount paid after discount, and the balance of the total purchase goes to Merchandise Inventory. This makes sense since the buyer has reduced the cost of the merchandise by paying quickly.

The **seller** has comparable entries, but debits the expense account Sales Discount for the amount of discount offered on payment.

Date	BUYER	Debit	Credit		SELLER	Debit	Credit
	Accounts Payable	\$400			Cash	\$380	
	Cash		\$380		Sales Discount	\$20	
	Merchandise Inventory		\$20		Accounts Receivable		\$400

(4) Freight Costs: The buyer or the seller may be responsible for the cost of transporting the merchandise. **FOB shipping point** means the buyer pays the costs of shipping. In the **buyer's** books, a transaction with FOB shipping point is recorded as debit to Merchandise Inventory and credit to cash for payment. **FOB destination** means the seller pays the shipping costs. When the **seller** is recording payment for FOB destination, the shipping costs are debited to Freight-out. Payment for shipping costs is always credited to Cash.

Date	BUYER (FOB shipping point)	Debit	Credit	OR	SELLER (FOB destination)	Debit	Credit
	Merchandise Inventory	\$50			Freight-out	\$50	
	Cash		\$50		Cash		\$50

Example: Journalize the following transactions for both companies.

August 1: JZ & Co purchases 200 necklaces from Bling-Bling at \$55 each with terms 2/20, n /30 FOB shipping. The cost of each necklace for Bling-Bling was \$20.

August 2: JZ & Co pays \$40 shipping.

August 3: JZ & Co returns 10 necklaces with broken clasps.

August 4: JZ & Co pays for the necklaces.

August 10: JZ & Co sells 60 necklaces for \$70 each to HipHop Inc with terms 5/10, n/30.

Date	JZ & Co	Debit	Credit		Bling-Bling	Debit	Credit
Aug 1	Merchandise Inventory	\$11000			Accounts Receivable	\$11000	
	Accounts Payable		\$11000		Sales Revenue		11000
					Cost of Goods Sold	\$4000	
					Merchandise Inventory		\$4000
Aug 2	Merchandise Inventory	40					
	Cash		40				
Aug 3	Accounts Payable	550			Sales returns	550	
	Merchandise Inventory		550		Accounts Receivable		550
					Merchandise Inventory	200	
					Cost of Goods Sold		200
Aug 4	Accounts Payable	10450			Sales discount	209	
	Cash		10241		Cash	10241	
	Merchandise Inventory		209		Accounts Receivable		10450
	JZ & Co				HipHop Inc.		
Aug 10	Accounts Receivable	4200			Merchandise Inventory	4200	
	Sales Revenue		4200		Accounts Payable		4200
	Cost of Goods Sold**	3246.63					
	Merchandise Inventory		3246.63				

**To find Cost of Goods Sold = $(\$11,000 + 40 - 550 - 209)/190$ necklaces = \$54.11/necklace. \$54.11/necklace x 60 necklaces = \$3246.63

Exercises

1. On October 5, MDMaxx bought 50 pairs of jeans on account from Zinc Co. The selling price of the jeans was \$65 per pair and the cost to Zinc Co. was \$40 per pair. On October 10, MDMaxx returned 10 pairs of jeans. Record the transactions for both companies.
2. Gambits & Games needs to record the following transactions in their journal.
 - a. On February 3, purchased merchandise from Antics Co. for \$15,000 terms 3/10, net/30, FOB destination.
 - b. On February 6, purchased equipment on account for \$12,000.
 - c. On February 8, returned defective merchandise to Antics Co. and was granted a \$5,000 allowance for returned merchandise.
 - d. On February 12, paid the amount due to Antics Co. in full.

(A) Prepare entries for the company under a perpetual inventory system.
 (B) Assume that on the Feb 3 transaction, the terms were for FOB shipping point and freight costs of \$800 were paid on Feb 5. Prepare the journal entry to record this transaction.
3. During November, the following transactions occurred for Mark's Polo Wear. Journalize the November transactions under a perpetual inventory system.

Nov.	4	Purchased 60 blazers at \$52 each from Alize Co. terms 4/15, n/30, FOB shipping point.
	7	Paid shipping costs of \$90 on blazers purchased from Alize Co.
	11	Returned 5 blazers to Alize Co. because they were damaged.
	13	Paid Alize Co. for half the amount owing.
	21	Paid Alize Co. the remaining amount owing.
	22	Sold 40 blazers to DeLuco Country Club for \$75 each terms 2/10, n/30, FOB destination.
	23	Paid freight costs of \$60 for merchandise sold to DeLuco Country Club.
	25	Granted credit of \$150 to DeLuco Country Club for return of 2 damaged blazers.
	30	Received payment in full from DeLuco Country Club.

Solutions

1. MDMaxx			
5-Oct	Merchandise Inventory	3,250	
	Accounts Payable		3,250
10-Oct	Accounts Payable	650	
	Merchandise Inventory		650
Zinc Co.			
5-Oct	Accounts Receivable	3,250	
	Sales Revenue		3,250
	Cost of Goods Sold	2,000	
	Merchandise Inventory		2,000
10-Oct	Sales Returns	650	
	Accounts Receivable		650
	Merchandise Inventory	400	
	Cost of Goods Sold		400

2. (A) Gambits & Games			
3-Feb	Merchandise Inventory	15,000	
	Accounts Payable		15,000
6-Feb	Equipment	12,000	
	Accounts Payable		12,000
8-Feb	Accounts Payable	5,000	
	Merchandise Inventory		5,000
12-Feb	Accounts Payable	10,000	
	Cash		9,700
	Merchandise Inventory		300
(B)			
5-Feb	Merchandise Inventory	800	
	Cash		800

3.

4-Nov	Merchandise Inventory	3,120.00	
	Accounts Payable		3,120.00
7-Nov	Merchandise Inventory	90.00	
	Cash		90.00
11-Nov	Accounts Payable	260.00	
	Merchandise Inventory		260.00
13-Nov	Accounts Payable	1430.00	
	Cash		1372.80
	Merchandise Inventory		57.20
21-Nov	Accounts Payable	1430.00	
	Cash		1430.00
22-Nov	Accounts Receivable	3000.00	
	Sales Revenue		3000.00
	Cost of Goods Sold	2103.85	
	Merchandise Inventory		2103.85
23-Nov	Freightout	60.00	
	Cash		60.00
25-Nov	Sales returns	150.00	
	Accounts receivable		150.00
	Merchandise Inventory	105.19	
	Cost of Goods Sold		105.19
30-Nov	Cash	2793.00	
	Sales Discount	57.00	
	Accounts receivable		2850.00