Accounting for Sales and Accounts Receivable

Kellogg's Company www.kelloggcompany.com

More than 100 years ago, W.K. Kellogg cre-

ated the first-ever breakfast cereal, the single corn flake, and then went on to shape an entire industry. Motivated by a passion for people, quality, and innovation, Kellogg soon became a household name. Today, W.K. Kellogg's legacy continues to inspire the company.

As a leading food producer, the company serves the world a delicious choice of cereals, snacks, meals, drinks, and more. And every day they look for ways to create even better experiences for all of their consumers. The company produces not only cereal. Its other brands include: *Pringles, Keebler, Cheez-Its,* and *Townhouse* and they continue to strive to provide even more.



Thousands of stores all over the world stock Kellogg's food products. In their first quarter of 2013, the company reported net sales of \$3.9 billion. It also reported a net Accounts Receivable balance of nearly \$1.6 billion. Keeping track of these product sales as well as store accounts receivable balances can be a daunting task for any accountant, but careful recordkeeping is a must if Kellogg wants to maintain its strong relationships with customers. The company strives to ensure that sales and accounts receivable data are accurate and that individual records of their customers' accounts receivable are updated daily.

If asked his opinion about the company, their mascot, Tony the Tiger, would say, "They're Grrrrreat!"

thinking critically

Do you think that Kellogg Company varies the discounts that it offers to its various store customers?

LEARNING OBJECTIVES

- **7-1.** Record credit sales in a sales journal.
- **7-2.** Post from the sales journal to the general ledger accounts.
- **7-3.** Post from the sales journal to the customers' accounts in the accounts receivable subsidiary ledger.
- **7-4.** Record sales returns and allowances in the general journal.
- **7-5.** Post sales returns and allowances.
- **7-6.** Prepare a schedule of accounts receivable.
- **7-7.** Compute trade discounts.
- **7-8.** Record credit card sales in appropriate journals.
- 7-9. Prepare the state sales tax return.
- **7-10.** Define the accounting terms new to this chapter.

NEW TERMS

accounts receivable ledger charge-account sales contra revenue account control account credit memorandum invoice list price manufacturing business merchandise inventory merchandising business net price net sales open-account credit

retail business
sales allowance
sales journal
sales return
Sales Returns and
Allowances
schedule of accounts
receivable
service business
special journal
subsidiary ledger
trade discount
wholesale business

SECTION OBJECTIVES

>> 7-1. Record credit sales in a sales journal.

WHY IT'S IMPORTANT

Credit sales are a major source of revenue for many businesses. The sales journal is an efficient option for recording large volumes of credit sales transactions.

>> 7-2. Post from the sales journal to the general ledger accounts.

WHY IT'S IMPORTANT

A well-designed accounting system prevents repetitive tasks.

TERMS TO LEARN

manufacturing business merchandise inventory merchandising business retail business sales journal service business special journal subsidiary ledger

Merchandise Sales

When an accounting system is developed for a firm, one important consideration is the nature of the firm's operations. The three basic types of businesses are a **service business**, which sells services; a merchandising business, which sells goods that it purchases for resale; and a manufacturing business, which sells goods that it produces.

Wells' Consulting Services, the firm that was described in Chapters 2 through 6, is a service business. The firm that we will examine next, Maxx-Out Sporting Goods, is a merchandising business that sells the latest sporting goods and sportswear for men, women, and children. It is a retail business, which sells goods and services directly to individual consumers. Maxx-Out Sporting Goods is a sole proprietorship owned and operated by Max Ferraro, who was formerly a sales manager for a major retail clothing store.

Maxx-Out Sporting Goods must account for purchases and sales of goods, and for merchandise inventory—the stock of goods that is kept on hand. Refer to the chart of accounts for Maxx-Out Sporting Goods on the next page. You will learn about the accounts in this and following chapters.

To allow for efficient recording of financial data, the accounting systems of most merchandising businesses include special journals and subsidiary ledgers.

Special Journals and Subsidiary Ledgers

A special journal is a journal that is used to record only one type of transaction. A subsidiary **ledger** is a ledger that contains accounts of a single type. Table 7.1 lists the journals and ledgers that merchandising businesses generally use in their accounting systems. In this chapter, we will discuss the sales journal and the accounts receivable subsidiary ledger.

The Sales Journal

The sales journal is used to record only sales of merchandise on credit. To understand the need for a sales journal, consider how credit sales made at Maxx-Out Sporting Goods would be entered and posted using a general journal and general ledger. Refer to Figure 7.1 on pages 192–193.

Note the word "Balance" in the ledger accounts. To record beginning balances, enter the date in the Date column, the word "Balance" in the Description column, a check mark in the Posting Reference column, and the amount in the Debit or Credit Balance column.

Most state and many local governments impose a sales tax on retail sales of certain goods and services. Businesses are required to collect this tax from their customers and send it to the proper tax agency at regular intervals. When goods or services are sold on credit, the sales tax

important!

Business Classifications

The term merchandising refers to the type of business operation, not the type of legal entity. Maxx-Out Sporting Goods could have been a partnership or a corporation instead of a sole proprietorship.

is usually recorded at the time of the sale even though it will not be collected immediately. A liability account called *Sales Tax Payable* is credited for the sales tax charged.

| JOURNALS | |
|---|---|
| Type of Journal | Purpose |
| Sales Purchases Cash receipts Cash payments General | To record sales of merchandise on credit To record purchases of merchandise on credit To record cash received from all sources To record all disbursements of cash To record all transactions that are not recorded in another special journal and all adjusting and dosing entries |
| LEDGERS | |
| Type of Ledger | Content |
| General Accounts receivable Accounts payable | Assets, liabilities, owner's equity, revenue, and expense accounts Accounts for credit customers Accounts for creditors |

TABLE 7.1

Journals and Ledgers Used by **Merchandising Businesses**

| | Maxx-Out Sporting Goods Chart of Accounts | |
|---|--|---|
| Assets | Liabilities | Cost of Goods Sold |
| 101 Cash 105 Petty Cash Fund 109 Notes Receivable 111 Accounts Receivable 112 Allowance for Doubtful Accounts 116 Interest Receivable 121 Merchandise Inventory 126 Prepaid Insurance 127 Prepaid Interest 129 Supplies 131 Store Equipment 132 Accumulated Depreciation — Store Equipment 141 Office Equipment 142 Accumulated Depreciation — Office Equipment | 201 Notes Payable — Trade 202 Notes Payable — Bank 205 Accounts Payable 216 Interest Payable 221 Social Security Tax Payable 222 Medicare Tax Payable 223 Employee Income Tax Payable 225 Federal Unemployment Tax Payable 227 State Unemployment Tax Payable 229 Salaries Payable 231 Sales Tax Payable 231 Max Ferraro, Capital 302 Max Ferraro, Drawing 309 Income Summary Revenue 401 Sales 451 Sales Returns and Allowances 491 Interest Income 493 Miscellaneous Income | 501 Purchases 502 Freight In 503 Purchases Returns and Allowances 504 Purchases Discounts Expenses 611 Salaries Expense — Sales 612 Supplies Expense 614 Advertising Expense 617 Cash Short or Over 626 Depreciation Expense — Store Equipment 634 Rent Expense 637 Salaries Expense — Office 639 Insurance Expense 641 Payroll Taxes Expense 643 Utilities Expense 644 Utilities Expense 645 Uncollectible Accounts Expense 656 Delivery Expense 657 Bank Fees Expense 658 Delivery Expense 659 Depreciation Expense 659 Depreciation Expense 651 Interest Expense 651 Interest Expense |

Journalizing and Posting Credit Sales

| | | | GENERAL JO | DURNAL | | | | | PA | GE | Ē_ | | 2 | _ |
|----|------|----|------------------------------|--------------|----|-----|---|----|----|----|----|----|----|----|
| | DATE | | DESCRIPTION | POST. REF | DE | ΕΒΙ | Т | | | CR | ED | ΙT | | |
| 1 | 2016 | | | | | | | | | | | | | 1 |
| 2 | Jan. | 3 | Accounts Receivable | 111 | 7 | 0 | 2 | 00 | | | | | | 2 |
| 3 | | | Sales Tax Payable | 231 | | | | | | Г | 5 | 2 | 00 | 3 |
| 4 | | | Sales | 401 | | | | | | 6 | 5 | 0 | 00 | 4 |
| 5 | | | Sold merchandise on | | | | | | | | | | | 5 |
| 6 | | | credit to Ann Anh, | | | | | | | | | | | 6 |
| 7 | | | Sales Slip 1101 | | | | | | | | | | | 7 |
| 8 | | | | | | | | | | Г | | | | 8 |
| 9 | | 8 | Accounts Receivable | 111 | 6 | 4 | 8 | 00 | | | | | | 9 |
| 10 | | | Sales Tax Payable | 231 | | | | | | | 4 | 8 | 00 | 10 |
| 11 | | | Sales | 401 | | | | | | 6 | 0 | 0 | 00 | 11 |
| 12 | | | Sold merchandise on | | | | | | | Г | | | | 12 |
| 13 | | | credit to Cathy Ball, | | | | | | | Г | | | | 13 |
| 14 | | | Sales Slip 1102 | | | | | | | | | | | 14 |
| 15 | | | | | | | | | | | | | | 15 |
| 16 | | 11 | Accounts Receivable | 111 | 7 | 5 | 6 | 00 | | | | | | 16 |
| 17 | | | Sales Tax Payable | 231 | | | | | | Г | 5 | 6 | 00 | 17 |
| 18 | | | Sales | 401 | | | | | | 7 | 0 | 0 | 00 | 18 |
| 19 | | | Sold merchandise on | | | | | | | | | | | 19 |
| 20 | | | credit to Barbara Coe, Sales | | | | | | | | | | | 20 |
| 21 | | | Slip 1103 | | | | | | | | | | | 21 |
| 22 | | | | | | | | | | | | | | 22 |
| 23 | | 15 | Accounts Receivable | 111 | 3 | 2 | 4 | 00 | | | | | | 23 |
| 24 | | | Sales Tax Payable | 231 | | | | | | | 2 | 4 | 00 | 24 |
| 25 | | | Sales | 401 | | | | | | 3 | 0 | 0 | 00 | 25 |
| 26 | | | Sold merchandise on | | | | | | | | | | | 26 |
| 27 | | | credit to Amalia Rodriguez, | | | | | | | | | | | 27 |
| 28 | | | Sales Slip 1104 | | | | | | | | | | | 28 |
| 29 | | | | | | | | | | | | | | 29 |
| 30 | | | | | | | | | | | | | | 30 |
| 31 | | | | | | | | | | | | | | 31 |
| 32 | | | | | | | | | | | | | | 32 |
| | | | | | | | | | | | | | | |

| ACCO | UN | T_Accounts | Receivo | able | | | | | | | | | _ | Α | CC | COU | NT N | 10. | | 11: | 1 | |
|------|----|-------------|---------------|------|----|----|---|----|----|-----|---|---|----|----|----|------|------|-----|-----|-----|------|-----|
| DAT | E | DESCRIPTION | POST. REF. | | DE | ΒI | Т | | CR | EDI | Т | | DE | BI | | BALA | NCE | CR | EDI | ΙΤ | | |
| 2016 | | | | | | | | | | | | | | | | | | Γ | | П | | |
| Jan. | 1 | Balance | 1 | | | | | | | | | 3 | 2 | 4 | 0 | 00 | | Т | | | | |
| | 3 | | J2 | | 7 | 0 | 2 | 00 | | | | 3 | 9 | 4 | 2 | 00 | | | | | | |
| | 8 | | J2 | | 6 | 4 | 8 | 00 | | T | | 4 | 5 | 9 | 0 | 00 | | Т | | | | Ī |
| | 11 | | J2 | | 7 | 5 | 6 | 00 | | T | | 5 | 3 | 4 | 6 | 00 | | Т | П | П | | Γ |
| | 15 | | J2 | | 3 | 2 | 4 | 00 | | | | 5 | 6 | 7 | 0 | 00 | | | | T | | |
| | | | | | | | | | | | | | | | | | | Г | | | | |
| | | | | | | | | | | | | | | | | | | Г | | | | Γ |
| | | | | | | | | | | | | | | | | | | | / | | nuec | IN. |

As you can see, a great amount of repetition is involved in both journalizing and posting these sales. The four credit sales made on January 3, 8, 11, and 15 required four separate entries in the general journal and involved four debits to *Accounts Receivable*, four credits to *Sales Tax Payable*, four credits to *Sales* (the firm's revenue account), and four descriptions. The posting of 12 items to the three general ledger accounts represents still further duplication of effort. This recording procedure is not efficient for a business that has a substantial number of credit sales each month.

FIGURE 7.1 (continued)

| ACCC | DUN | T_Sales Ta. | x Paya | ble | | | | | | | | | | | | ΑC | CC | :OL | JN ⁻ | ΓN | Э. | | 23 | 1 | _ | | | | | | | |
|------|-----|-------------|--------|-----|------|-----|-------|-----|---------------|-----|-----|----|-----|---|----|----|----|------|-----------------|----|-----|-----|----|-----|---|------|------|----|-----|-----|----|---|
| DAT | E | DESCRIPTIO | N POST | Г. | | DE | віт | | | CRE | ΞDI | ΙT | | ŀ | DE | ВП | | BAL | ANG | | CRE | ΞDI | ΙΤ | | - | | | | | | | |
| 2016 | | | | | | | | | | | | | | Т | | | I | | | | | | | | | | | | | | | |
| Jan. | 1 | Balance | 1 | | | | | | | | | | | | | | | | | | 7 | 5 | 6 | 0 | 0 | | | | | | | |
| | 3 | | J2 | | | | | | | | 5 | 2 | 00 |) | | | | | | | 8 | 0 | 8 | 0 | 0 | | | | | | | |
| | 8 | | J2 | | | | | | | | 4 | 8 | 00 |) | | | | | | | 8 | 5 | 6 | 0 | 0 | | | | | | | |
| | 11 | | J2 | | | | | | | | | 6 | 00 |) | | | | | | | | 1 | | 0 | 0 | | | | | | | |
| | 15 | | J2 | | | | | | | | 2 | 4 | 00 |) | | | | | | | 9 | 3 | 6 | 0 | 0 | | | | | | | |
| | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | | | ACCC | UN | IT_ | Sai | les. | | | | | | | | | | | | | | | | | Α | C | COU | NT N | 1C |) | 40 |)1 | _ |
| | | | | _ | 5.50 | | | | POST. REF. | | | | | _ | | | | | _ | | | | | | | BALA | ANCE | | | | | Т |
| | | | DAT | E | DES | SCF | KIP I | ION | REF. | | | DE | BIT | _ | | (| JH | EDI. | ' | | | | DE | ΞBΙ | Т | | | CI | RED | TIC | _ | |
| | | | 2016 | | | | | | | | | | | 1 | | | | | L | | | | L | | | | | l | | L | | |
| | | | Jan. | 3 | | | | | J2 | | | L | | 1 | | | | 5 (| _ | 00 | | | L | | | | | - | 5 5 | - | _ | _ |
| | | | | 8 | | | | | J2 | | | | | | | | | 0 (| _ | 00 | | | | | | | | | | | 00 | |
| | | | | 11 | | | | | J2 | | | | | | | | | 0 (| _ | 00 | | | | | | | | _ | _ | _ | 00 | _ |
| | | | | 15 | | | | | J2 | | | | | | | | 3 | 0 (| 0 (| 00 | | | | | | | 2 | 2 | 2 5 | 0 | 00 | 2 |
| | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |
| | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | | |

RECORDING TRANSACTIONS IN A SALES JOURNAL

A special journal intended only for credit sales provides a more efficient method of recording these transactions. Figure 7.2 shows the January credit sales of Maxx-Out Sporting Goods recorded in a sales journal. Since Maxx-Out Sporting Goods is located in a state that has an 8 percent sales tax on retail transactions, its sales journal includes a Sales Tax Payable Credit column. For the sake of simplicity, the sales journal shown here includes a limited number of transactions. The firm actually has many more credit sales each month.

Notice that the headings and columns in the sales journal speed up the recording process. No general ledger account names are entered. Only one line is needed to record all information for each transaction—date, sales slip number, customer's name, debit to *Accounts Receivable*, credit to *Sales Tax Payable*, and credit to *Sales*. Since the sales journal is used for a single purpose, there is no need to enter any descriptions. Thus, a great deal of repetition is avoided.

Entries in the sales journal are usually made daily. In a retail business such as Maxx-Out Sporting Goods, the data needed for each entry is taken from a copy of the customer's sales slip, as shown in Figure 7.3.

| | | | | SALES | JOUR | NAL | | | | | | | | PAGE | : _ | | 1 | |
|----|------|----|----------------------|----------------------------|---------------|------------|----|-----|----|----|-----|----------------------|----|------|----------|----------|----|----|
| | DAT | E | SALES SLIP NO. | CUSTOMER'S ACCOUNT DEBITED | POST. REF. | ACC REC | Eľ | | | P/ | XYA | S TA ABLI EDIT | Ē | S | AI RE | ES DI | Г | |
| 1 | 2016 | | | | | | | | | | | | | | | | | 1 |
| 2 | Jan. | 3 | 1101 | Ann Anh | | | 7 | 0 2 | 00 | | | 5 2 | 00 | | 6 | 5 (| 00 | 2 |
| 3 | | 8 | 1102 | Cathy Ball | | | 6 | 48 | 00 | | | 48 | 00 | | 6 | 00 | 00 | 3 |
| 4 | | 11 | 1103 | Barbara Coe | | | 7 | 5 6 | 00 | | | 5 6 | 00 | | 7 | 00 | 00 | 4 |
| 5 | | 15 | 1104 | Amalia Rodriguez | | | 3 | 24 | 00 | | | 24 | 00 | | 3 | 00 | 00 | 5 |
| 6 | | 18 | 1105 | Fred Wu | | | 8 | 10 | 00 | | | 60 | 00 | | 7 | 5 (| 00 | 6 |
| 7 | | 21 | 1106 | Linda Carter | | | 4 | 86 | 00 | | | 3 6 | 00 | | 4 | 5 (| 00 | 7 |
| 8 | | 28 | 1107 | Kim Ramirez | | | 1 | 0 8 | 00 | | | 8 | 00 | | 1 | 00 | 00 | 8 |
| 9 | | 29 | 1108 | Mesia Davis | | 1 | 0 | 80 | 00 | | | 80 | 00 | 1 | 0 | 00 | 00 | 9 |
| 10 | | 31 | 1109 | Alma Sanchez | | | 9 | 72 | 00 | | | 72 | 00 | | 9 | 00 | 00 | 10 |
| 11 | | 31 | 1110 | Ann Anh | | | 2 | 70 | 00 | | | 20 | 00 | | 2 | 5 (| 00 | 11 |
| 12 | | | | | | | | | | | | | | | | | | 12 |
| | | | | | | | | | | | | | | | | | | |

>> 7-1. OBJECTIVE

Record credit sales in a sales journal.



Journals

A journal is a day-to-day record of a firm's transactions.

FIGURE 7.2

A Sales Journal

Customer's Sales Slip

>> 7-2. OBJECTIVE

Post from the sales journal to the general ledger accounts.

Many small retail firms use a sales journal similar to the one shown in Figure 7.2. However, keep in mind that special journals vary in format according to the needs of individual businesses.

POSTING FROM A SALES JOURNAL

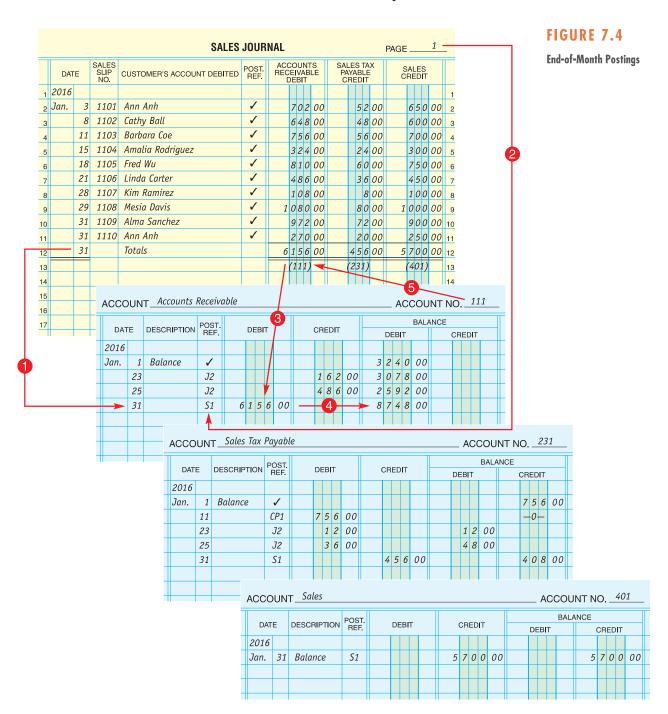
A sales journal not only simplifies the initial recording of credit sales, it also eliminates a great deal of repetition in posting these transactions. With a sales journal, it is not necessary to post each credit sale individually to general ledger accounts. Instead, summary postings are made at the end of the month after the amount columns of the sales journal are totaled. See Figure 7.4 for an illustration of posting from the sales journal to the general ledger.

In actual practice, before any posting takes place, the equality of the debits and credits recorded in the sales journal is proved by comparing the column totals. The proof for the sales journal in Figure 7.4 is given below. All multicolumn special journals should be proved in a similar manner before their totals are posted.

| Proof of Sales Journ | nal |
|--|---|
| | Debits |
| Accounts Receivable Debit column | \$6,1 <u>56.00</u> |
| | Credits |
| Sales Tax Payable Credit column Sales Credit column | \$ 456.00 _5,700.00 \$6,156.00 = 1 |

After the equality of the debits and credits has been verified, the sales journal is ruled and the column totals are posted to the general ledger accounts involved. To indicate that the postings have been made, the general ledger account numbers are entered in parentheses under the column totals in the sales journal. The abbreviation S1 is written in the Posting Reference column of the accounts, showing that the data was posted from page 1 of the sales journal.

The check marks in the sales journal in Figure 7.4 indicate that the amounts have been posted to the individual customer accounts. Posting from the sales journal to the customer accounts in the subsidiary ledger is illustrated later in this chapter.



ADVANTAGES OF A SALES JOURNAL

Using a special journal for credit sales saves time, effort, and recording space. Both the journalizing process and the posting process become more efficient, but the advantage in the posting process is especially significant. If a business used the general journal to record 300 credit sales a month, the firm would have to make 900 postings to the general ledger—300 to *Accounts Receivable*, 300 to *Sales Tax Payable*, and 300 to *Sales*. With a sales journal, the firm makes only three summary postings to the general ledger at the end of each month no matter how many credit sales were entered.

important!

Posting

When posting from the sales journal, post information moving from left to right across the ledger form.

The use of a sales journal and other special journals also allows division of work. In a business with a fairly large volume of transactions, it is essential that several employees be able to record transactions at the same time.

Finally, the sales journal improves the audit trail by bringing together all entries for credit sales in one place and listing them by source document number as well as by date. This procedure makes it easier to trace the details of such transactions.

Section Self Review

QUESTIONS

- 1. What is a special journal? Give four examples of special journals.
- What type of transaction is recorded in the sales journal?
- 3. What is a subsidiary ledger? Give two examples of subsidiary ledgers.

EXERCISES

- 4. Types of business operations are:
 - a. service, merchandising, corporation.
 - **b.** sole proprietorship, merchandising, manufacturing.
 - c. service, merchandising, manufacturing.

- 5. Which of the following is not a reason to use a sales journal?
 - a. increases efficiency
 - **b.** allows division of work
 - c. increases credit sales
 - d. improves audit trail

ANALYSIS

6. All sales recorded in the sales journal below were made on account and are taxable at a rate of 8 percent. What errors have been made in the entries? Assume the Sales Credit column is correct.

(Answers to Section 1 Self Review are on pages 232–233.)

| | | | | SALES | JOUR | NAL | | | | | | | PAGE | :_ | | 1 | - |
|-----|------|----|----------------------|----------------------------|---------------|-----|-----|-----|----|-----------------|-----|----|------|-----------|-----------|----|-----|
| | DAT | | SALES SLIP NO. | CUSTOMER'S ACCOUNT DEBITED | POST. REF. | | | ABI | | ES YA REI | BLI | E | C | SAL RE | ES DIT | | |
| | | | | | | | _ | _ | | | _ | | | _ | | | |
| 12 | Apr. | 25 | 4100 | Carolyn Harris | | | 6 4 | 2 | 00 | 2 | 42 | 00 | | 6 | 00 | 00 | 12 |
| 13 | | 25 | 4101 | Teresa Wells | | | 8 7 | 2 | 00 | 7 | 72 | 00 | | 9 | 00 | 00 | 13 |
| 4.4 | | | | | | | | П | | | | | | | | | 4.4 |

Section 2

SECTION OBJECTIVES

>> 7-3. Post from the sales journal to the customers' accounts in the accounts receivable subsidiary ledger.

WHY IT'S IMPORTANT

This ledger contains individual records that reflect all transactions of each customer.

>> 7-4. Record sales returns and allowances in the general journal.

WHY IT'S IMPORTANT

Companies can see how much revenue is lost due to merchandise problems.

>> 7-5. Post sales returns and allowances.

WHY IT'S IMPORTANT

Accurate, up-to-date customer records contribute to overall customer satisfaction.

>> 7-6. Prepare a schedule of accounts receivable.

WHY IT'S IMPORTANT

This schedule provides a snapshot of amounts due from customers.

TERMS TO LEARN

accounts receivable ledger contra revenue account control account credit memorandum net sales sales allowance sales return

Sales Returns and Allowances schedule of accounts receivable

Accounts Receivable

A business that extends credit to customers must manage its accounts receivable carefully. Accounts receivable represents a substantial asset for many businesses, and this asset must be converted into cash in a timely manner. Otherwise, a firm may not be able to pay its bills even though it has a large volume of sales and earns a satisfactory profit.

The Accounts Receivable Ledger

The accountant needs detailed information about the transactions with credit customers and the balances owed by such customers at all times. This information is provided by an **accounts receivable ledger** with individual accounts for all credit customers. The accounts receivable ledger is referred to as a subsidiary ledger because it is separate from and subordinate to the general ledger.

Using an accounts receivable ledger makes it possible to verify that customers are paying their balances on time and that they are within their credit limits. The accounts receivable ledger also provides a convenient way to answer questions from credit customers. Customers may ask about their current balances or about a possible billing error.

The accounts for credit customers are maintained in a balance ledger form with three money columns, as shown in Figure 7.5 on the next page. Notice that this form does not contain a column for indicating the type of account balance. The balances in the customer accounts are presumed to be debit balances since asset accounts normally have debit balances. However, occasionally there is a credit balance because a customer has overpaid an amount owed or has returned goods that were already paid for. One common procedure for dealing with this situation is to circle the balance in order to show that it is a credit amount.

For a small business such as Maxx-Out Sporting Goods, customer accounts are alphabetized in the accounts receivable ledger. Larger firms and firms that use computers assign an account number to each credit customer and arrange the customer accounts in numeric order. Postings

>> 7-3. OBJECTIVE

Post from the sales journal to the customers' accounts in the accounts receivable subsidiary ledger.

>> 7-4. OBJECTIVE

Record sales returns and allowances in the general journal.

FIGURE 7.5

Posting from the Sales Journal to the Accounts Receivable Ledger

to the accounts receivable ledger are usually made daily so that the customer accounts can be kept up to date at all times.

POSTING A CREDIT SALE

Each credit sale recorded in the sales journal is posted to the appropriate customer's account in the accounts receivable ledger, as shown in Figure 7.5. The date, the sales slip number, and the amount that the customer owes as a result of the sale are transferred from the sales journal to the customer's account. The amount is taken from the Accounts Receivable Debit column of the journal and is entered in the Debit column of the account. Next, the new balance is determined and recorded.

To show that the posting has been completed, a check mark (\checkmark) is entered in the sales journal and the abbreviation S1 is entered in the Posting Reference column of the customer's account. As noted before, this abbreviation identifies page 1 of the sales journal.

POSTING CASH RECEIVED ON ACCOUNT

When the transaction involves cash received on account from a credit customer, the cash collected is first recorded in a cash receipts journal. (The necessary entry in the cash receipts journal is discussed in Chapter 9.) The cash is then posted to the individual customer account in the accounts receivable ledger. Figure 7.6 shows a posting for cash received on January 7 from Ann Anh, a credit customer of Maxx-Out Sporting Goods.

Sales Returns and Allowances

A sale is entered in the accounting records when the goods are sold or the service is provided. If something is wrong with the goods or service, the firm may take back the goods, resulting in a **sales return**, or give the customer a reduction in price, resulting in a **sales allowance**.

When a return or allowance is related to a credit sale, the normal practice is to issue a document called a **credit memorandum** to the customer rather than giving a cash refund. The

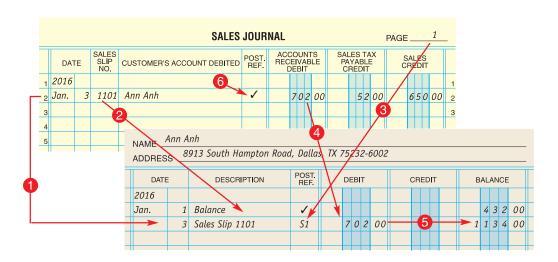


FIGURE 7.6

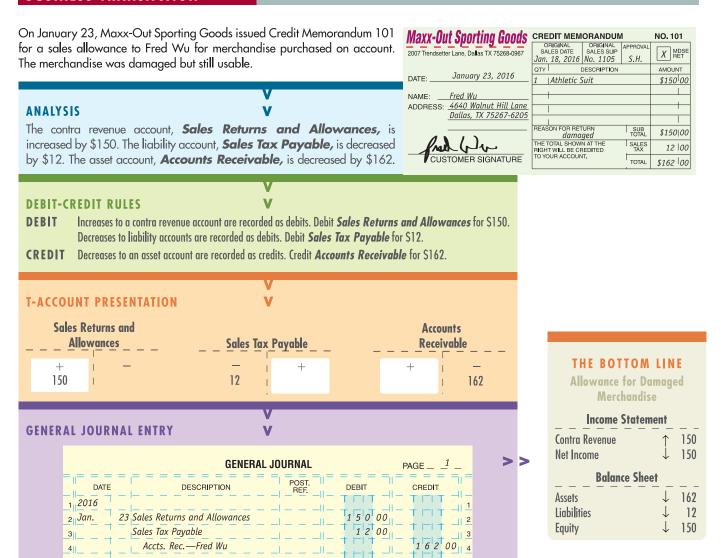
Posting for Cash Received on Account

| NAME _^A | Ann A S8 | nh 913 South Hampton Roa | d, Dallas | s, TX : | 752 | 23. | 2-6 | 5002 | | | | | | | | | | |
|----------|-------------|-----------------------------|---------------|---------|-----|-----|-----|------|----|----|----|----|---|----|----|-----|----|--|
| DATE | | DESCRIPTION | POST. REF. | | DE | ВІ | Т | | CF | EC | ìΤ | | В | AL | ΑN | ICE | | |
| 2016 | | | | | | | | | | | | | | | | | | |
| Jan. | 1 | Balance | 1 | | | | | | | | | | | 4 | 3 | 2 | 00 | |
| | 3 | Sales Slip 1101 | S1 | | 7 | 0 | 2 | 00 | | | | | 1 | 1 | 3 | 4 | 00 | |
| | 7 | | CR1 | | | | | | 4 | 3 | 2 | 00 | | 7 | 0 | 2 | 00 | |
| | | | | | | | | | | | | | | | | | | |

credit memorandum states that the customer's account is being reduced by the amount of the return or allowance plus any sales tax. A copy of the credit memorandum provides the data needed to enter the transaction in the firm's accounting records.

A debit to the **Sales Returns and Allowances** account is preferred to making a direct debit to **Sales**. This procedure gives a complete record of sales returns and allowances for each accounting period. Business managers use this record as a measure of operating efficiency. The **Sales Returns and Allowances** account is a **contrar revenue account** because it has a debit balance, which is contrary, or opposite, to the normal credit balance for a revenue account.

BUSINESS TRANSACTION



What is the ultimate effect of this transaction on the financial statements? An increase in contra revenue causes a decrease in net income. Note that the \$150 decrease in net income causes a \$150 decrease in owner's equity. The asset *Accounts Receivable* is decreased, and the liability *Sales Tax Payable* is also decreased. The eventual effect of this transaction on the income statement and the balance sheet is summarized in the box titled *The Bottom Line*.

RECORDING SALES RETURNS AND ALLOWANCES

Depending on the volume of sales returns and allowances, a business may use a general journal to record these transactions, or it may use a special sales returns and allowances journal.

Using the General Journal for Sales Returns and Allowances A small firm that has a limited number of sales returns and allowances each month has no need to establish a special journal for such transactions. Instead, the required entries are made in the general journal.

Using a Sales Returns and Allowances Journal In a business having many sales returns and allowances, it is efficient to use a special journal for these transactions. An example of a *sales returns and allowances journal* is shown in Figure 7.7.

>> 7-5. OBJECTIVE

Post sales returns and allowances.

FIGURE 7.7

Sales Returns and Allowances Journal

FIGURE 7.8

Posting a Sales Return to the Customer's Account

POSTING A SALES RETURN OR ALLOWANCE

Whether sales returns and allowances are recorded in the general journal or in a special sales returns and allowances journal, each of these transactions must be posted from the general ledger to the appropriate customer's account in the accounts receivable ledger. Figure 7.8 shows how a return of merchandise was posted from the general journal to the account of Linda Carter.

| | | | | SALES RETURNS AND | ALLO | WAN | CE | S | J | OU | RNAL | | | | PAGE | =_ | | 8 | _ |
|----|------|----|----------------------|--------------------------------|---------------|-----------------|----|----|-----|----|-------------------|-----|-----|----|------|----|-----------------------------|----|----|
| | DAT | ΓE | SALES SLIP NO. | CUSTOMER'S ACCOUNT CREDITED | POST. REF. | ACC REC C | | VΑ | BL | | SALI PA\ DI | | 3LI | | | ٩L | S RI LOV B I T | | |
| 1 | 2016 | | | | | | | | | | | | | | | | | | 1 |
| 2 | Jan. | 23 | 1105 | Fred Wu | 1 | | 1 | 6 | 2 (| 00 | | 1 | 2 | 00 | | 1 | 5 C | 00 | 2 |
| 3 | | 25 | 1106 | Linda Carter | 1 | | 4 | 8 | 6 (| 00 | | 3 | 6 | 00 | | 4 | 5 C | 00 | 3 |
| 4 | | | | | | | | Т | | | | Γ | Г | | | | | | 4 |
| | | | | | | | | | | | | | | | | | | | |
| 17 | | 31 | | Totals | | 3 | 2 | 4 | 0 (| 00 | ž | 2 4 | 0 | 00 | 3 | 0 | 00 | 00 | 17 |
| 18 | | | | | | | (1 | 1 | 1) | | (| 23 | 1) |) | | (4 | 51 |) | 18 |
| 19 | | | | | | | | | | | | | | | | | | | 19 |

| | | | | | | GENERAL J | OURNAL | | | | | | P/ | AGE | ≣_ | | 1 | _ |
|----|------|----|-------------|--------|-------|-----------------|---------------|--------------|----|-----|----|------|----|-----|-----|----|------|----|
| | DATE | ≣ | | DESC | RIPT | TION | POST. REF. | | DI | ЕΒΙ | Т | | | CF | REC | ΙT | | |
| 1 | 2016 | | | | | | | | | | | | | | | | | 1 |
| | | | | | | | | | | | | | | L | L | | | |
| 6 | Jan. | 25 | Sales Retur | ns a | nd A | llowances | 451 | | 4 | 5 | 0 | 00 | | L | L | | | 6 |
| 7 | | | Sales Tax P | ayab | le | | 231 | | | 3 | 6 | 00 | | | L | | | 7 |
| 8 | | | Accounts | Rec., | /Lin | da Carter | 111 | | | | | | | 4 | 8 | 6 | 00 | 8 |
| 9 | | | Accept | ed a | retu | ırn of | | | | | | | | | | | | 9 |
| 10 | | | defect | ive n | nercl | handise, | | | | | | | | | | | | 10 |
| 11 | | | Credit | Мет | orar | ndum 102; | | | | | | | | | | | | 11 |
| 12 | | | origina | al sai | le m | ade on Sales | | | Г | | | | | Т | Г | | | 12 |
| 13 | | | Slip 1: | 106 d | of Ja | inuary 21. | | | | | | | | | | | | 13 |
| 14 | | | | | | | | | | | | | | | | | | 14 |
| 15 | | | NAME | _ Li | nda | Carter | | 11 | | | | | | | | | | |
| 16 | | | ADDF | | 1 | 819 Belt Line F | Road, Dalla | s, Texi | 75 | 75. | 26 | 7-63 | 18 | | | | | |
| | | | | DATE | | DESCRIP | TION | POST REF. | | | ı | DEBI | Т | | | С | REDI | Т |
| | | | 2016 | | | | | | T | | | | | Т | | | | |
| | | | Jan | | 1 | Balance | | 1 | Т | | | | | T | | | | |

S1

J1

48600

21 Sales Slip 1106

25 CM 102

5 4 0 00

5 4 00

48600

Because the credit amount in the general journal entry for this transaction requires two postings, the account number 111 and a check mark are entered in the Posting Reference column of the journal. The 111 indicates that the amount was posted to the *Accounts Receivable* account in the general ledger, and the check mark indicates that the amount was posted to the customer's account in the accounts receivable ledger. Notice that a diagonal line was used to separate the two posting references.

Refer to Figure 7.7, which shows a special sales returns and allowances journal instead of a general journal. The account numbers at the bottom of each column are the posting references for the three general ledger accounts: *Accounts Receivable*, *Sales Tax Payable*, and *Sales Returns and Allowances*. The check marks in the Posting Reference column show that the credits were posted to individual customer accounts in the accounts receivable subsidiary ledger.

Remember that a business can use the general journal or special journals for transactions related to credit sales. A special journal is an efficient option for recording and posting large numbers of transactions.

Figure 7.9 shows the accounts receivable ledger after posting is completed.

REPORTING NET SALES

At the end of each accounting period, the balance of the *Sales Returns and Allowances* account is subtracted from the balance of the *Sales* account in the Revenue section of the income statement. The resulting figure is the **net sales** for the period.

For example, assume the *Sales Returns and Allowances* account contains a balance of \$600 at the end of January. Also assume the *Sales* account has a balance of \$25,700 at the end of January. The Revenue section of the firm's income statement will appear as follows.

| Maxx-Out Sporting God Income Statement (Part Month Ended January 31, | ial) |
|--|----------|
| Revenue | |
| Sales | \$25,700 |
| Less Sales Returns and Allowances | 600 |
| Net Sales | \$25,100 |

NAME _ Ann Anh 8913 South Hampton Road, Dallas, Texas 75232-6002 POST. REF. CREDIT DATE DESCRIPTION DEBIT BALANCE 2016 Jan. 1 Balance 4 3 2 00 3 Sales Slip 1101 S1 70200 1 1 3 4 00 CR1 70200 4 3 2 00 31 Sales Slip 1110 9 7 2 00 S1 27000 NAME Cathy Ball 7517 Woodrow Wilson Lane, Dallas, Texas 75267-6205 ADDRESS DATE DESCRIPTION DEBIT CREDIT BALANCE 2016 6 4 8 00 S1 6 4 8 00 Лап. 8 Sales Slip 1102

ABOUT ACCOUNTING

Investing in Ethics

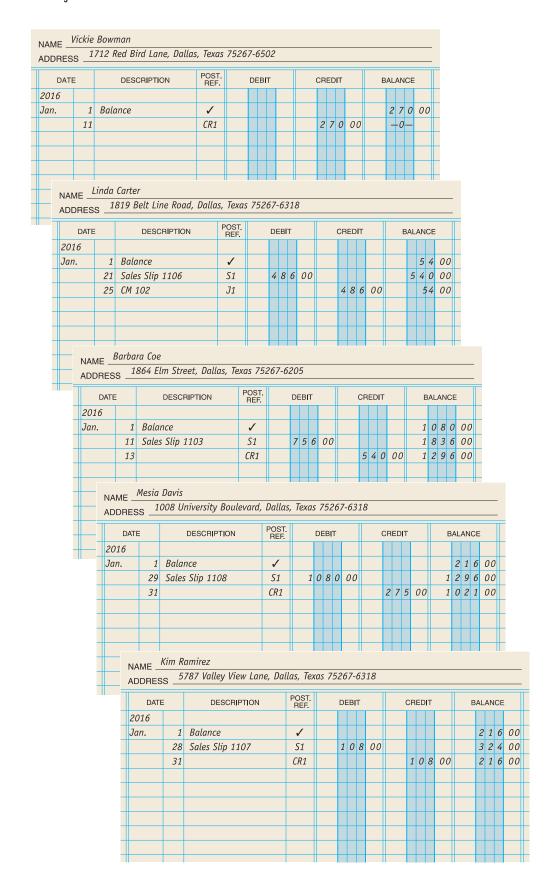
Are ethical companies — those with a strong internal enforcement policy — really more profitable? Yes, such companies are listed among the top 100 financial performers twice as often as those without an ethics focus, according to a study by Curtis Verschoor at DePaul University.

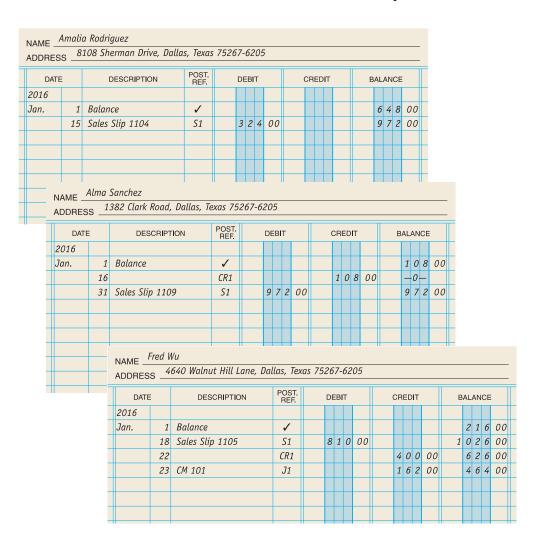
FIGURE 7.9

Accounts Receivable Ledger

(continued)

(continued)





(concluded)

Schedule of Accounts Receivable

The use of an accounts receivable ledger does not eliminate the need for the *Accounts Receivable* account in the general ledger. This account remains in the general ledger and continues to appear on the balance sheet at the end of each fiscal period. However, the *Accounts Receivable* account is now considered a control account. A **control account** serves as a link between a subsidiary ledger and the general ledger. Its balance summarizes the balances of its related accounts in the subsidiary ledger.

At the end of each month, after all the postings have been made from the sales journal, the cash receipts journal, and the general journal to the accounts receivable ledger, the balances in the accounts receivable ledger must be proved against the balance of the *Accounts Receivable* general ledger account. First a **schedule of accounts receivable**, which lists the subsidiary ledger account balances, is prepared. The total of the schedule is compared with the balance of the *Accounts Receivable* account. If the two figures are not equal, errors must be located and corrected.

On January 31, the accounts receivable ledger at Maxx-Out Sporting Goods contains the accounts shown in Figure 7.9. To prepare a schedule of accounts receivable, the names of all customers with account balances are listed with the amount of their unpaid balances. Next the figures are added to find the total owed to the business by its credit customers.

>> 7-6. OBJECTIVE

Prepare a schedule of accounts receivable.

Schedule of Accounts Receivable and the Accounts Receivable Accounts

| | | | Maxx-Out | | | | | | la. | | | | | | | | | | | | | | | |
|------------------|------|----|-------------------------------|--------|------|----|-----|----|-----|---|--------------|-----|---|-----|-----|-----|-----|----|-----|------|----|-----|-----|--|
| | | | Schedule of <i>I</i> Janua | ary 31 | | | eiv | au | ie | | | | | | | | | | | | | | | |
| Ann Anh | | | | | | | | | | | Т | | | | 9 7 | 2 | 00 | וו | | | | | | |
| Cathy Ball | | | | | | | | | | | † | | | _ | _ | - | 00 | - | _ | | | | | |
| Linda Carter | | | | | | | | | | | t | | | | _ | - | 00 | - | | | | | | |
| Barbara Coe | | | | | | | | | | | Ħ | | | 1 2 | _ | - | 00 | - | | | | | | |
| Mesia Davis | | | | | | | | | | | Ħ | | | | _ | - | 00 | - | | | | | | |
| Kim Ramirez | | | | | | | | | | | t | | | 2 | | - | 00 | | | | | | | |
| Amalia Rodriguez | | | | | | | | | | | t | | | _ | _ | - | 00 |) | | | | | | |
| Alma Sanchez | | | | | | | | | | | Ħ | | | 9 | 9 7 | 2 | 00 |) | | | | | | |
| Fred Wu | | | | | | | | | | | Ħ | | | 4 | _ | _ | 00 |) | | | | | | |
| Total | | | | | | | | | | | T | | | 6 6 | 5 1 | 5 | 00 |) | | | | | | |
| | | | | | | | | | | | r | | | | П | Ī | | 1 | | | | | | |
| | ACCC | UN | T_Accounts | Receiv | able | | | | | | | | | | | | _ / | ٩C | COL | JNT | NO | | 111 | |
| | | | | POST. | | | | | | | | | | | | | | | BAL | ANCE | | | | |
| | DAT | Έ | DESCRIPTION | REF. | | DI | EBI | T | | ' | CR | EDI | Т | | | С | EE | ΙT | | | CF | RED | IT | |
| | 2016 | | | | | | | | | | | | | | | | | | | | | | | |
| | Jan. | 1 | Balance | 1 | | | | | | | | | 1 | | | 3 2 | | | | - | | | | |
| | | 23 | | J1 | | | | | | | 1 | - | _ | 00 | | | | 8 | | - | | | | |
| | | 25 | | J1 | | L | | | | | 4 | 8 | 6 | 00 | | 2 5 | | | | - | | | | |
| | | 31 | | S1 | 6 | 1 | 5 | 6 | 00 | | | | | | | | | 8 | | - | | | | |
| | | 31 | | CR1 | | | | | | 2 | 1 | 3 . | 3 | 00 | | 5 6 | 5 1 | 5 | 00 | | | | | |
| | | | | | | | | | | | | | | | | | | | | | | | | |

A comparison of the total of the schedule of accounts receivable prepared at Maxx-Out Sporting Goods on January 31 and the balance of the *Accounts Receivable* account in the general ledger shows that the two figures are the same, as shown in Figure 7.10. The posting reference CR1 refers to the cash receipts journal, which is discussed in Chapter 9.

In addition to providing a proof of the subsidiary ledger, the schedule of accounts receivable serves another function. It reports information about the firm's accounts receivable at the end of the month. Management can review the schedule to see exactly how much each customer owes.

Section 2 Self Review

QUESTIONS

- 1. What are net sales?
- 2. What is a sales return? What is a sales allowance?
- Which accounts are kept in the accounts receivable ledger?

EXERCISES

- 4. Where would you report net sales?
 - a. sales general ledger account
 - b. general journal
 - c. income statement
 - d. sales journal

- Which of the following general ledger accounts would appear in a sales returns and allowances journal?
 - a. Sales Returns and Allowances, Sales Tax Payable, Accounts Receivable
 - b. Sales Returns and Allowances, Sales, Accounts Receivable
 - c. Sales Returns, Sales Allowances, Sales

ANALYSIS

6. Draw a diagram showing the relationship between the accounts receivable ledger, the schedule of accounts receivable, and the general ledger.

(Answers to Section 2 Self Review are on page 233.)

Section 3

| SE | CTION OBJECTIVES | TERMS TO LEARN |
|----------------------|---|---|
| >> 7-7. | Compute trade discounts. WHY IT'S IMPORTANT Trade discounts allow for flexible pricing structures. | charge-account sales invoice list price |
| >> 7-8. | Record credit card sales in appropriate journals. WHY IT'S IMPORTANT Credit cards are widely used in merchandising transactions. | net price open-account credit trade discount wholesale business |
| >> 7-9. | Prepare the state sales tax return. WHY IT'S IMPORTANT Businesses are legally responsible for accurately reporting and remitting sales taxes. | |

Special Topics in Merchandising

Merchandisers have many accounting concerns. These include pricing, credit, and sales taxes.

Credit Sales for a Wholesale Business

The operations of Maxx-Out Sporting Goods are typical of those of many retail businesses—businesses that sell goods and services directly to individual consumers. In contrast, a **wholesale business** is a manufacturer or distributor of goods that sells to retailers or large consumers such as hotels and hospitals. The basic procedures used by wholesalers to handle sales and accounts receivable are the same as those used by retailers. However, many wholesalers offer cash discounts and trade discounts, which are not commonly found in retail operations.

The procedures used in connection with cash discounts are examined in Chapter 9. The handling of trade discounts is described here.

COMPUTING TRADE DISCOUNTS

A wholesale business offers goods to trade customers at less than retail prices. This price adjustment is based on the volume purchased by trade customers and takes the form of a **trade discount**, which is a reduction from the **list price**—the established retail price. There may be a single trade discount or a series of discounts for each type of goods. The **net price** (list price less all trade discounts) is the amount the wholesaler records in its sales journal.

The same goods may be offered to different customers at different trade discounts, depending on the size of the order and the costs of selling to the various types of customers.

Single Trade Discount Suppose the list price of goods is \$1,500 and the trade discount is 40 percent. The amount of the discount is \$600, and the net price to be shown on the invoice and recorded in the sales journal is \$900.

| Invoice price | \$ 900 |
|---|---------|
| Less 40% discount (\$1,500 \times 0.40) | 600 |
| List price | \$1,500 |

>> 7-7. **OBJECTIVE**

Compute trade discounts.

important!

Trade Discounts

The amount of sales revenue recorded is the list price minus the trade discount.

important!

Special Journal Format Special journals such as the sales journal can vary in format from company to company.

Series of Trade Discounts If the list price of goods is \$1,500 and the trade discount is quoted in a series such as 25 and 15 percent, a different net price will result.

| \$1,500.00 |
|------------|
| 375.00 |
| \$1,125.00 |
| 168.75 |
| \$ 956.25 |
| |

USING A SALES JOURNAL FOR A WHOLESALE BUSINESS

Since sales taxes apply only to retail transactions, a wholesale business does not need to account for such taxes. Its sales journal may therefore be as simple as the one illustrated in Figure 7.11. This sales journal has a single amount column. The total of this column is posted to the general ledger at the end of the month as a debit to the Accounts Receivable account and a credit to the Sales account (Figure 7.12). During the month, the individual entries in the sales journal are posted to the customer accounts in the accounts receivable ledger.

Wholesale businesses issue invoices. An **invoice** is a customer billing for merchandise bought on credit. Copies of the invoices are used to enter the transactions in the sales journal.

The next merchandising topic, credit policies, applies to both wholesalers and retailers. The discussion in this textbook focuses on credit policies and accounting for retail firms.

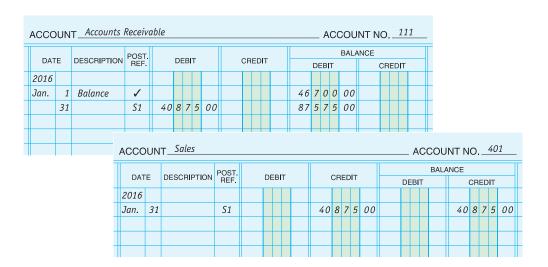
FIGURE 7.11

Wholesaler's Sales Journal

| | | | | SALES JOURNAL | | PAGE | | 1 | _ |
|----|------|----|----------------|----------------------------|---------------|------|------------------|-------|------|
| | DAT | E | INVOICE NO. | CUSTOMER'S ACCOUNT DEBITED | POST. REF. | RECE | OUN VAB ES | LE DE | ₹. |
| 1 | 2016 | | | | | | | | 1 |
| 2 | Jan. | 3 | 7099 | Gabbert's Hardware Company | | 18 | 60 | 0 0 |) 2 |
| 3 | | | | | | | | | 3 |
| Ξ, | | | | | | | | | |
| 25 | | 31 | 7151 | Neal's Department Store | | 4 | 20 | 0 0 | 25 |
| 26 | | 31 | | Total | | 40 | 87 | 5 0 | 26 |
| 27 | | | | | | (1: | 1/ | 401 |) 27 |
| 28 | | | | | | | | | 28 |

FIGURE 7.12

General Ledger Accounts



Credit Policies

The use of credit is considered to be one of the most important factors in the rapid growth of modern economic systems. Sales on credit are made by large numbers of wholesalers and retailers of goods and by many professional people and service businesses. The assumption is that the volume of both sales and profits will increase if buyers are given a period of a month or more to pay for the goods or services they purchase.

However, the increase in profits a business expects when it grants credit will be realized only if each customer completes the transaction by paying for the goods or services purchased. If payment is not received, the expected profits become actual losses and the purpose for granting the credit is defeated. Business firms try to protect against the possibility of such losses by investigating a customer's credit record and ability to pay for purchases before allowing any credit to the customer.

Professional people such as doctors, lawyers, architects, and owners of small businesses like Maxx-Out Sporting Goods usually make their own decisions about granting credit. Such decisions may be based on personal judgment or on reports available from credit bureaus, information supplied by other creditors, and credit ratings supplied by national firms such as Dun & Bradstreet.

Dun & Bradstreet is a leader in providing credit information. For the year ended December 31, 2012, the company reported revenues of \$1.6 billion.

Larger businesses maintain a credit department to determine the amounts and types of credit that should be granted to customers. In addition to using credit data supplied by institutions, the credit department may obtain financial statements and related reports from customers who have applied for credit. This information is analyzed to help determine the maximum amount of credit that may be granted and suitable credit terms for the customer. Financial statements that have been audited by certified public accountants are used extensively by credit departments.

Even though the credit investigation is thorough, some accounts receivable become uncollectible. Unexpected business developments, errors of judgment, incorrect financial data, and many other causes may lead to defaults in payments by customers. Experienced managers know that some uncollectible accounts are to be expected in normal business operations and that limited losses indicate that a firm's credit policies are sound. Provisions for such limited losses from uncollectible accounts are usually made in budgets and other financial projections.

Each business must develop credit policies that achieve maximum sales with minimum losses from uncollectible accounts:

- A credit policy that is too tight results in a low level of losses at the expense of increases in sales volume.
- A credit policy that is too lenient may result in increased sales volume accompanied by a high level of losses.

Good judgment based on knowledge and experience must be used to achieve a well-balanced credit policy.

Different types of credit have evolved with the growing economy and changing technology. The different types of credit require different accounting treatments.

ACCOUNTING FOR DIFFERENT TYPES OF CREDIT SALES

The most common types of credit sales are:

- open-account credit,
- business credit cards,
- bank credit cards.
- cards issued by credit card companies.

Open-Account Credit The form of credit most commonly offered by professional people and small businesses permits the sale of services or goods to the customer with the understanding that the amount is to be paid at a later date. This type of arrangement is called **open-account credit.** It is usually granted on the basis of personal acquaintance or knowledge of the customer. However, formal credit checks may also be used. The amount involved in each transaction is usually small, and payment is expected within 30 days or on receipt of a monthly statement. Open-account sales are also referred to as **charge-account sales**.

Maxx-Out Sporting Goods uses the open-account credit arrangement. Sales transactions are recorded as debits to the *Accounts Receivable* account and credits to the *Sales* account. Collections on account are recorded as debits to the *Cash* account and credits to the *Accounts Receivable* account.

Business Credit Cards Many retail businesses, especially large ones such as department store chains and gasoline companies, provide their own credit cards (sometimes called charge cards) to customers who have established credit. Whenever a sale is completed using a business credit card, a sales slip is prepared in the usual manner. Then the sales slip and the credit card are placed in a mechanical device that prints the customer's name, account number, and other data on all copies of the sales slip. Many companies use computerized card readers and sales registers that print out a sales slip with the customer information and a line for the customer's signature. Some businesses require that the salesclerk contact the credit department by telephone or computer terminal to verify the customer's credit status before completing the transaction.

Business credit card sales are similar to open-account credit sales. A business credit card sale is recorded as:

- a debit to *Accounts Receivable*,
- a credit to a revenue account such as *Sales*.

A customer payment is recorded as:

- a debit to Cash,
- a credit to *Accounts Receivable*.

Bank Credit Cards Retailers can provide credit while minimizing or avoiding the risk of losses from uncollectible accounts by accepting bank credit cards. The most widely accepted bank credit cards are MasterCard and Visa. Many banks participate in one or both of these credit card programs, and other banks have their own credit cards. Bank credit cards are issued to consumers directly by banks.

A business may participate in these credit card programs by meeting conditions set by the bank. Banks review such factors as:

- The business's financial history.
- The industry in which the business operates.
- The type of business, online, physical store, or both.
- Any past merchant account history.

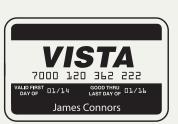
When a sale is made to a cardholder, the sale is processed using a magnetic swipe machine (see Figure 7.13). Most businesses use an online credit card processing terminal. This type of terminal transmits information to the bank using an Internet connection.

When a business makes a sale to a customer using a bank credit card, it acquires an asset that can be converted into cash immediately without responsibility for later collection from the customer. In most cases, the bank deposits the cash from the sale into the business's bank account the same day.

Banks charge the business a fee, called a *discount*, for processing the sale. The discount is usually between 1.5 and 4 percent of the amount charged. Depending on the arrangements that have been made, the bank will deduct the discount and immediately credit the depositor's checking account with the net amount of the sale, or it will credit the depositor's checking account for the full amount of the sale and deduct the discount at the end of the month. If the second procedure is used, the total discount for the month's sales will appear on the bank statement.

The bank is responsible for collecting from the cardholder. If any amounts are uncollectible, the bank sustains the loss. For the retailer, bank credit card sales are like cash sales. The accounting procedures for such sales are therefore quite similar to the accounting procedures





Credit Card Reader

MAXX-OUT SPORTING GOODS DALLAS, TX

| ****** | ****** |
|-----------|----------|
| SWEATSUIT | \$125.00 |
| SALES TAX | \$10.00 |
| TOTAL | \$135.00 |
| | |

NAME:

CONNORS/JAMES

TYPE:

PURCHASED SWIPED

VISTA

*******222

INVOICE # 08789798234
AUTH CODE : 12345
DATE : 01/28/16
TIME 17:02

James Connors

Signature:

for cash sales, which will be discussed in Chapter 9. If the business is billed once each month for the bank's discount, the total amount involved in the daily deposit of the credit card sales slips is debited to *Cash* and credited to *Sales*.

Credit Card Companies Credit cards such as American Express and Diners Club are issued by business firms or subsidiaries of business firms that are operated for the special purpose of handling credit card transactions. The potential cardholder must submit an application and pay an annual fee to the credit card company. If the credit references are satisfactory, the credit card is issued. It is normally reissued at one-year intervals so long as the company's credit experience with the cardholder remains satisfactory.

Hotels, restaurants, airline companies, many types of retail stores, and a wide variety of other businesses accept these credit cards. When making sales to cardholders, sellers usually prepare their own sales slip or bill and then complete a special sales slip required by the credit card company (see Figure 7.14). As with the sales slips for bank credit cards, the forms must be imprinted with the identifying data on the customer's card and signed by the customer. Such sales slips are sometimes referred to as *sales invoices*, *sales drafts*, or *sales vouchers*. The term used varies from one credit card company to another.

The seller acquires an account receivable from the credit card company rather than from the customer. At approximately one-month intervals, the credit card company bills the cardholders for all sales slips it has acquired during the period. It is the responsibility of the credit card company to collect from the cardholders.

FIGURE 7.14

Credit Card Receipt

>> 7-8. OBJECTIVE

Record credit card sales in appropriate journals.

ACCOUNTING FOR CREDIT CARD SALES

The procedure used to account for credit card sales is similar to the procedure for recording open-account credit sales. However, the account receivable is with the credit card company, not with the cardholders who buy the goods or services.

There are two basic methods of recording these sales. Businesses that have few transactions with credit card companies normally debit the amounts of such sales to the usual *Accounts Receivable* account in the general ledger and credit them to the same *Sales* account that is used for cash sales and other types of credit sales. An individual account for each credit card company is set up in the accounts receivable subsidiary ledger. This method of recording sales is shown in Figure 7.15.

Payment from a credit card company is recorded in the cash receipts journal, a procedure discussed in Chapter 9. Fees charged by the credit card companies for processing these sales are debited to an account called *Discount Expense on Credit Card Sales*. For example, assume that American Express charges a 7 percent discount fee on the sale charged by Wilson Davis on January 3 and remits the balance to the firm. This transaction would be recorded in the cash receipts journal by debiting *Cash* for \$502.20, debiting *Discount Expense on Credit Card Sales* for \$37.80, and crediting *Accounts Receivable* for \$540.00.

Firms that do a large volume of business with credit card companies may debit all such sales to a special *Accounts Receivable from Credit Card Companies* account in the general ledger, thus separating this type of receivable from the accounts receivable resulting from open-account credit sales. A special account called *Sales—Credit Card Companies* is credited for the revenue from these transactions. Figure 7.16 shows how the necessary entries are made in the sales journal.

FIGURE 7.15

Recording Credit Card Company Sales

| | | | | SALES | JOUR | NAL | | | | | | | | PAGE | _ | 1 | 17 | _ |
|----|------|----|----------------------|----------------------------|---------------|-----------------|-----|----|----|-----------------|---|------------|----|------|-----|---|----|----|
| | DAT | | SALES SLIP NO. | CUSTOMER'S ACCOUNT DEBITED | POST. REF. | ACC REC E | | AB | | SAL PA CF | | BL | E | | ALI | | | |
| 1 | 2016 | | | | | | | | | | | | | | | | | 1 |
| 2 | Jan. | 3 | 533 | American Express | | | 5 4 | 60 | 00 | | 4 | <i>4</i> 0 | 00 | | 5 (| 0 | 00 | 2 |
| 3 | | | | (Wilson Davis) | | | | Г | | | T | | | | П | | | 3 |
| | | | | | | | | | | | | | | | | | | |
| 26 | | 11 | 651 | MasterCard | | | 2 1 | 6 | 00 | | 1 | ! 6 | 00 | | 20 | 0 | 00 | 26 |
| 27 | | | | (Teresa Logan) | | | | | | | | | | | | | | 27 |
| 28 | | | | | | | 1 | | | | I | | | | | | | 28 |

FIGURE 7.16 Recording Sales for Accounts Receivable from Credit Card Companies

| | SALES JOURNAL PAGE 7 | | | | | | | | | | | | | |
|----|----------------------|----|----------------------|-------------------------------|---------------|-----|-----------------------|-----|--|--------------------------------|-----------------|--|------|--|
| | DA ⁻ | TE | SALES SLIP NO. | CUSTOMER'S ACCOUNT DEBITED | POST. REF. | REC | COUN EIVA DEBIT | BLE | ACCT. REC.— CREDIT CARD COMPANIES DEBIT | SALES TAX PAYABLE CREDIT | SALES CREDIT | SALES— CREDIT CARD COMPANIES CREDIT | | |
| 1 | 2016 | | | | | | Ш | | | | | | 1 | |
| 2 | Jan. | 3 | | Summary of credit card sales/ | | | Ш | | | | | | 2 | |
| 3 | | | | American Express | | | | | 972000 | 72000 | | 900000 |) з | |
| | | | | | | | | | | | | | | |
| 5 | | | | | | | | | | | | | 5 | |
| 16 | | 11 | | Summary of credit card sales/ | | | Ш | | 5 4 0 0 00 | 40000 | | 500000 |) 16 | |
| 17 | | | | MasterCard | | | | | | | | | 17 | |
| | | | | | | | | | | | | | | |
| 29 | | 31 | | Totals | | | | | 48 6 0 0 00 | 3 6 0 0 00 | | 45 0 0 0 00 | 29 | |
| 30 | | | | | | | | | (114) | (231) | | (404) | 30 | |
| 31 | | | | | | | | | | | | | 31 | |

Sales Taxes

Many cities and states impose a tax on retail sales. Sales taxes imposed by city and state governments vary. However, the procedures used to account for these taxes are similar.

A sales tax may be levied on all retail sales, but often certain items are exempt. In most cases, the amount of the sales tax is stated separately and then added to the retail price of the merchandise.

In November 2012, California voters approved an initiative to raise the state sales tax by .25%.

The retailer is required to collect sales tax from customers, make periodic (usually monthly) reports to the taxing authority, and pay the taxes due when the reports are filed. The government may allow the retailer to retain part of the tax as compensation for collecting it.

PREPARING THE STATE SALES TAX RETURN

At the end of each month, after the accounts have all been posted, Maxx-Out Sporting Goods prepares the sales tax return. The information required for the monthly return comes from the accounting data of the current month. Three accounts are involved: *Sales Tax Payable, Sales*, and *Sales Returns and Allowances*. In some states, the sales tax return is filed quarterly rather than monthly.

The procedures to file a sales tax return are similar to those used by Maxx-Out Sporting Goods on February 7 when it filed the monthly sales tax return for January with the state tax commissioner. The firm's sales are subject to an 8 percent state sales tax. To highlight the data needed, the January postings are shown in the ledger accounts in Figure 7.17.

>> 7-9. OBJECTIVE

Prepare the state sales tax return.

| ACCC | DUN | T <u>Sales Tax</u> | Payabl | е | | | | | | | | | | | Α | C | cou | NT N | Ю. | | 23 | 1 | |
|------|-----|--------------------|---------------|---|----|-----|---|----|---|----|----|----|----|----|-----|---|------|------|----|-----|----------|------|----|
| DAT | ΓE | DESCRIPTION | POST. REF. | | DE | ΞBΙ | Т | | | CR | ED | ΙT | | DI | ΞВΙ | Т | BALA | | CF | RED | OIT | | |
| 2016 | | | | | | | | | | | | | | | | | | | | | | | Π |
| Jan. | 1 | Balance | 1 | | | | | | | | | | | | | | | | 7 | 5 | 6 | 00 | |
| | 11 | | CP1 | | 7 | 5 | 6 | 00 | | | | | | | | | | | - | 0 | \vdash | | |
| | 23 | | J1 | | | 1 | 2 | 00 | | | | | | | 1 | 2 | 00 | | | | | | |
| | 25 | | J1 | | | 3 | 6 | 00 | | | | | | | 4 | 8 | 00 | | | Г | | | П |
| | 31 | | S1 | | | | | | | 4 | 5 | 6 | 00 | | | | | | 4 | 0 | 8 | 00 | Π |
| | 31 | | CR1 | | | | | | 1 | 8 | 0 | 0 | 00 | | | | | 2 | 2 | 0 | 8 | 00 | Π |
| | | | | | | | | | | | | | | | | | | | | | | | Π |
| | | ACCOUNT. | Sales | | | | | | | | | | | | | | | A(| CC | Ю | UN | IT N | Ο. |

| ACCC | UN. | T_Sales Retu | ırns an | d Allo | W | an | ce. | S | | | | | _ | Α | C | COU | NT N | 1C |) | 45 | 51 | - |
|------|-----|--------------|---------|--------|----|----|-----|----|-----|----|---|--|----|-----|---|------|------|----|-----|-----|----|---|
| DAT | _ | DESCRIPTION | POST. | | DI | ΞВ | | | CD. | ED | | | | | | BALA | NCE | | | | | |
| DAI | _ | DESCRIPTION | REF. | | Di | =D | " | | CR | ED | " | | DE | ΞBΙ | Т | | | CI | REI | DIT | | |
| 2016 | | | | | | | | | | | | | | | | | | Г | П | | | |
| Jan. | 23 | | J1 | | 1 | 5 | 0 | 00 | | | | | 1 | 5 | 0 | 00 | | Τ | Т | Г | | |
| | 25 | | J1 | | 4 | 5 | 0 | 00 | | | | | 6 | 0 | 0 | 00 | | T | | Т | | |
| | | | | | | | Г | | | | | | Г | | | | | Т | Т | Т | | |

FIGURE 7.17

Ledger Account Postings for Sales Tax THE BOTTOM LINE **Retail Sales Income Statement**

Balance Sheet

27,600

29,808.00

27,600.00

2,208.00

1 27,600

Revenue

Assets

Equity

Liabilities

Net Income

Using these figures as a basis, the amount of the firm's taxable gross sales for January is determined as follows:

| Cash Sales | \$22,500 |
|-----------------------------------|----------|
| Credit Sales | 5,700 |
| Total Sales | \$28,200 |
| Less Sales Returns and Allowances | 600 |
| Taxable Gross Sales for January | \$27,600 |

The 8 percent sales tax on the gross sales of \$27,600 amounts to \$2,208.00. Note that the firm's increase in assets (Cash and Accounts Receivable) is equal to sales revenue plus the sales tax liability on that revenue.

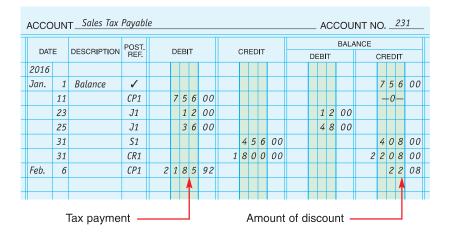
In the state where Maxx-Out Sporting Goods is located, a retailer who files the sales tax return (see Figure 7.19 on the next page) on time and who pays the tax when it is due is entitled to a discount. The discount is intended to compensate the retailer, at least in part, for acting as a collection agent for the government. The discount rate depends on the amount of tax to be paid. For amounts over \$1,000, the rate is 1 percent of the total tax due. For Maxx-Out Sporting Goods, the discount for January is determined as follows:

| Taxable Gross Sales for January | \$27,600.00 |
|---------------------------------|-------------|
| 8% Sales Tax Rate | × 0.08 |
| Sales Tax Due | \$ 2,208.00 |
| 1% Discount Rate | × 0.01 |
| Discount | \$22.08 |
| Sales Tax Due | \$ 2,208.00 |
| Discount | (22.08) |
| Net Sales Tax Due | \$ 2,185.92 |
| | |

The firm sends a check for the net sales tax due with the sales tax return. The accounting entry made to record this payment includes a debit to Sales Tax Payable and a credit to Cash (for \$2,185.92 in this case). After the amount of the payment is posted, the balance in the *Sales* Tax Payable account should be equal to the discount, as shown in Figure 7.18. Slight differences can arise because the tax collected at the time of the sale is determined by a tax bracket method that can give results slightly more or less than the final computations on the tax return.

FIGURE 7.18

Effect of Paying Sales Tax



SALES TAX RETURN **STATE TAX COMMISSION** LICENSE NUMBER ALWAYS REFER TO THIS NUMBER WHEN WRITING THE DIVISION SALES AND USE TAX DIVISION 217539 DRAWER 20 -IMPORTANT-CAPITAL CITY, STATE 78711 ANY CHANGE IN OWNERSHIP RETURN REQUESTED REQUIRES A NEW LICENSE: NOTIFY THIS DIVISION IMMEDIATELY. This return DUE on the 1st day of month following period covered by the return, and becomes DELINQUENT on the 21st day. January 31, 2016 37-9462315 - 4 7 7 7 8 FED. E.I. NO. OR S.S NO. —Sales for period ending— OWNER'S NAME AND LOCATION MAKE ALL REMITTANCES

PAYABLE TO STATE TAX COMMISSIOIN DO NOT SEND CASH STAMPS NOT ACCEPTED Maxx-Out Sporting Goods 2007 Trendsetter Lane Dallas, Texas 75268-0967

| COMPUTATION OF SALES TAX | For Taxpayer's Use | Do Not Use This Column |
|--|-----------------------|---------------------------|
| 1. TOTAL Gross proceeds of sales or Gross Receipts (to include rentals) | 27,600.00 | |
| Add cost of personal property purchased on a RETAIL LICENSE FOR RESALE but USED BY YOU or YOUR EMPLOYEES, including GIFTS and PREMIUMS | -0- | |
| USE TAX—Add cost of personal property purchased outside of STATE for your use, storage, or consumption | -0- | |
| 4. Total (Lines 1, 2, and 3) | 27,600.00 | |
| 5. LESS ALLOWABLE DEDUCTIONS (Must be itemized on reverse side) | -0- | |
| 6. Net taxable total (Line 4 minus Line 5) | 27,600.00 | |
| 7. Sales and Use Tax Due (8% of Line 6) | 2,208.00 | |
| LESS TAXPAYER'S DISCOUNT—(Deductible only when amount of TAX due is not delinquent at time of payment) | 22.08 | |
| IF LINE 7 IS LESS THAN \$100.00 —DEDUCT 3% IF LINE 7 IS \$100 BUT LESS THAN \$1,000.00 —DEDUCT 2% IF LINE 7 IS \$1,000.00 OR MORE —DEDUCT 1% | | |
| 9. NET AMOUNT OF TAX PAYABLE (Line 7 minus Line 8) | 2,185.92 | |
| Add the following penalty and interest if return or remittance is late. 10. Specific Penalty: 25% of tax \$ 11. Interest: 1/2 of 1% per month from due date until paid. \$ | | |
| 12. TOTAL TAX, PENALTY AND INTEREST | 2,185.92 | |
| 13. Subtract credit memo No. | | |
| 14. TOTAL AMOUNT DUE (IF NO SALES MADE SO STATE) | 2,185.92 | |

I certify that this return, including the accompanying schedules or statements, has been examined by me and to the best of my knowledge and belief, a true and complete return, made in good faith, for the period stated, pursuant to the provisions of the Code of Laws, 20-, and Acts Amendatory Thereto.

URGENT—SEE THAT LICENSE NUMBER IS ON RETURN

| Max | Division Use Only | |
|--|-------------------|--|
| SIGN | | |
| | | |
| Owner | February 7, 2016 | |
| Owner, partner or title | | |
| Return must be signed by owner or if corporation | | |
| | | |

FIGURE 7.19

State Sales Tax Return

If there is a balance in the *Sales Tax Payable* account after the sales tax liability is satisfied, the balance is transferred to an account called *Miscellaneous Income* by a general journal entry. This entry consists of a debit to *Sales Tax Payable* and a credit to *Miscellaneous Income*.

RECORDING SALES TAX IN THE SALES ACCOUNT

In some states, retailers can credit the entire sales price plus tax to the *Sales* account. At the end of each month or quarter, they must remove from the *Sales* account the amount of tax included and transfer that amount to the *Sales Tax Payable* account. Assume that during January a retailer whose sales are all taxable sells merchandise for a total price of \$20,250, which includes an 8 percent tax. The entry to record these sales is summarized in general journal form shown here.

| | GENERAL JOURNAL PAGE 4 | | | | | | | | | | | | | | |
|---|------------------------|----|----------------------------|---------------|----|----|-----|---|----|--------|---|---|---|----|---|
| | DATE | Ξ | DESCRIPTION | POST. REF. | | DE | ЕΒΙ | Т | | CREDIT | | | | | |
| 1 | 2016 | | | | | | | | | | | | | | 1 |
| 2 | Jan. | 31 | Accounts Receivable | 111 | 20 | 2 | 5 | 0 | 00 | | | | | | 2 |
| 3 | | | Sales | 401 | | | | | | 20 | 2 | 5 | 0 | 00 | 3 |
| 4 | | | To record total sales and | | | | | | | | | | | | 4 |
| 5 | | | sales tax collected during | | | | | | | | | | | | 5 |
| 6 | | | the month | | | | | | | | | | | | 6 |
| 7 | | | | | | | | | | | | | | | 7 |
| 7 | | | | | | | | | | | | | | | |

At the end of the month, the retailer must transfer the sales tax from the *Sales* account to the *Sales Tax Payable* account. The first step in the transfer process is to determine the amount of tax involved. The sales tax payable is computed as follows on the next page.

CREDIT SALES

- Credit sales are a major source of revenue in many businesses, and accounts receivable represent a major asset.
- Management needs up-to-date and correct information about both sales and accounts receivable in order to monitor the financial health of the firm.
- Special journals save time and effort and reduce the cost of accounting work.
- In a retail firm that must handle sales tax, the sales journal and the cash receipts journal provide a convenient method of recording the amounts owed for sales tax
 - When the data is posted to the Sales Tax Payable account in the general ledger, the firm has a complete and systematic record that speeds the completion of the periodic sales tax return.
 - The firm has detailed proof of its sales tax figures in the case of a tax audit.
- An accounts receivable subsidiary ledger provides management and the credit department with up-to-date information about the balances owed by all customers.
 - This information is useful in controlling credit and collections.

MANAGERIAL IMPLICATIONS

- Detailed information helps in evaluating the effectiveness of credit policies.
- Management must keep a close watch on the promptness of customer payments because much of the cash needed for day-to-day operations usually comes from payments on accounts receivable.
- A well-balanced credit policy helps increase sales volume but also keeps losses from uncollectible accounts at an acceptable level.
- Retailers are liable for any undercollection of sales taxes. This situation can be avoided with an efficient control system.

THINKING CRITICALLY

What are some possible consequences of out-of-date accounts receivable records?

Sales + tax = \$20,250100% of sales + 8% of sales = \$20,250108% of sales = \$20,250 Sales = \$20,250/1.08Sales = \$18,750

Tax $= $18,750 \times 0.08 = $1,500$

The firm then makes the following entry to transfer the liability from the Sales account.

| | | | GENERAL J | OURNAL | | | | | | PA | GE | = _ | | 4 | |
|----|------|----|--------------------------|---------------|---|----|-----|---|----|--------|----|-----|---|----|----|
| | DATI | Ē | DESCRIPTION | POST. REF. | | DE | ЕΒΙ | Т | | CREDIT | | | | | |
| 1 | 2016 | | | | | | | | | | | | | | 1 |
| | | | | | | | | | | | | | | | |
| 8 | Jan. | 31 | Sales | 401 | 1 | 5 | 0 | 0 | 00 | | | | | | 8 |
| 9 | | | Sales Tax Payable | 231 | | | | | | 1 | 5 | 0 | 0 | 00 | 9 |
| 10 | | | To transfer sales tax | | | | | | | | | | | | 10 |
| 11 | | | payable from the Sales | | | | | | | | | | | | 11 |
| 12 | | | account to the liability | | | | | | | | | | | | 12 |
| 13 | | | account | | | | | | | | | | | | 13 |
| 14 | | | | | | | | | | | | | | | 14 |
| 15 | | | | | | | | | | | | | | | 15 |

The retailer in this example originally recorded the entire sales price plus tax in the Sales account. The sales tax was transferred to the Sales Tax Payable account at the end of the month.

Section 3 **Self Review**

QUESTIONS

- 1. What are four types of credit sales?
- What is the difference between list price and net
- 3. What account is used to record sales tax owed by a business to a city or state?

EXERCISES

4. A company that buys \$4,000 of goods from a wholesaler offering trade discounts of 20 and 10 percent will pay what amount for the goods?

- **a.** \$1,760
- **b.** \$2,800
- c. \$2,880
- d. \$2,780
- 5. If a wholesale business offers a trade discount of 35 percent on a sale of \$7,200, what is the amount of the discount?
 - **a.** \$240
 - **b.** \$252
 - c. \$2,400
 - d. \$2,520

ANALYSIS

6. What factors would you consider in deciding whether or not to extend credit to a customer?

(Answers to Section 3 Self Review are on page 233.)

Chapter

REVIEW Chapter Summary

The nature of the operations of a business, the volume of its transactions, and other factors influence the design of an accounting system. In this chapter, you have learned about the use of special journals and subsidiary ledgers suitable for a merchandising business. These additional journals and ledgers increase the efficiency of recording credit transactions and permit the division of labor.

Learning Objectives

Record credit sales in a sales journal.

The sales journal is used to record credit sales transactions, usually on a daily basis. For sales transactions that include sales tax, the sales tax liability is recorded at the time of the sale to ensure that company records reflect the appropriate amount of sales tax liability.

Post from the sales journal to the general ledger 7-2 accounts.

> At the end of each month, the sales journal is totaled, proved, and ruled. Column totals are then posted to the general ledger. Using a sales journal rather than a general journal to record sales saves the time and effort of posting individual entries to the general ledger during the month.

Post from the sales journal to the customers' 7-3 accounts in the accounts receivable subsidiary ledger.

> The accounts of individual credit customers are kept in a subsidiary ledger called the accounts receivable ledger. Daily postings are made to this ledger from the sales journal, the cash receipts journal, and the general journal or the sales returns and allowances journal. The current balance of a customer's account is computed after each posting so that the amount owed is known at all times.

Record sales returns and allowances in the 7-4 general journal.

> Sales returns and allowances are usually debited to a contra revenue account. A firm with relatively few sales returns and allowances could use the general journal to record these transactions.

7-5 Post sales returns and allowances.

> Sales returns and allowances transactions must be posted to the general ledger and to the appropriate accounts receivable subsidiary ledgers. The balance of the Sales Returns and Allowances account is subtracted from the balance of the Sales account to show net sales on the income statement.

7-6 Prepare a schedule of accounts receivable.

> Each month a schedule of accounts receivable is prepared. It is used to prove the subsidiary ledger against the Accounts Receivable account. It also reports the amounts due from credit customers.

7-7 Compute trade discounts.

> Wholesale businesses often offer goods to trade customers at less than retail prices. Trade discounts are expressed as a percentage off the list price. Multiply the list price by the percentage trade discount offered to compute the dollar amount.

7-8 Record credit card sales in appropriate journals.

> Credit sales are common, and different credit arrangements are used. Businesses that have few transactions with credit card companies normally record these transactions in the sales journal by debiting the usual Accounts Receivable account in the general ledger and crediting the same Sales account that is used for cash sales.

7-9 Prepare the state sales tax return.

> In states and cities that have a sales tax, the retailer must prepare a sales tax return and send the total tax collected to the taxing authority.

7-10 Define the accounting terms new to this chapter.

Glossary

Accounts receivable ledger (p. 197) A subsidiary ledger that contains credit customer accounts Charge-account sales (p. 208) Sales made through the use of open-account credit or one of various types of credit cards

CHAPTER 7

Contra revenue account (p. 199) An account with a debit balance, which is contrary to the normal balance for a revenue account

Control account (p. 203) An account that links a subsidiary ledger and the general ledger since its balance summarizes the balances of the accounts in the subsidiary ledger

Credit memorandum (p. 198) A note verifying that a customer's account is being reduced by the amount of a sales return or sales allowance plus any sales tax that may have been involved

Invoice (p. 206) A customer billing for merchandise bought on credit

List price (p. 205) An established retail price

Manufacturing business (p. 190) A business that sells goods that it has produced

Merchandise inventory (p. 190) The stock of goods a merchandising business keeps on hand

Merchandising business (p. 190) A business that sells goods purchased for resale

Net price (p. 205) The list price less all trade discounts

Net sales (p. 201) The difference between the balance in the *Sales* account and the balance in the *Sales Returns and Allowances* account

Open-account credit (p. 208) A system that allows the sale of services or goods with the understanding that payment will be made at a later date

Retail business (p. 190) A business that sells directly to individual consumers

Sales allowance (p. 198) A reduction in the price originally charged to customers for goods or services

Sales journal (p. 190) A special journal used to record sales of merchandise on credit

Sales return (p. 198) A firm's acceptance of a return of goods from a customer

Sales Returns and Allowances (p. 199) A contra revenue account where sales returns and sales allowances are recorded; sales returns and allowances are subtracted from sales to determine net sales

Schedule of accounts receivable (p. 203) A listing of all balances of the accounts in the accounts receivable subsidiary ledger

Service business (p. 190) A business that sells services

Special journal (p. 190) A journal used to record only one type of transaction

Subsidiary ledger (p. 190) A ledger dedicated to accounts of a single type and showing details to support a general ledger account

Trade discount (p. 205) A reduction from list price

Wholesale business (p. 205) A business that manufactures or distributes goods to retail businesses or large consumers such as hotels and hospitals

Comprehensive **Self Review**

- 1. Name the two different time periods usually covered in sales tax returns.
- **2.** What is a control account?
- **3.** Why does a small merchandising business usually need a more complex set of financial records and statements than a small service business?
- **4.** Why is it useful for a firm to have an accounts receivable ledger?
- 5. Explain how service, merchandising, and manufacturing businesses differ from each other.

(Answers to Comprehensive Self Review are on page 234.)

Discussion Questions

- 1. How are the net sales for an accounting period determined?
- **2.** What purposes does the schedule of accounts receivable serve?
- 3. How do retail and wholesale businesses differ?

- 4. Why is a sales return or allowance usually recorded in a special Sales Returns and Allowances account rather than being debited to the Sales account?
- **5.** How is a multicolumn special journal proved at the end of each month?
- 6. What kind of account is Sales Returns and Allowances?
- 7. The sales tax on a credit sale is not collected from the customer immediately. When is this tax usually entered in a firm's accounting records? What account is used to record this tax?
- 8. In a particular state, the sales tax rate is 5 percent of sales. The retailer is allowed to record both the selling price and the tax in the same account. Explain how to compute the sales tax due when this method is used.
- 9. What two methods are commonly used to record sales involving credit cards issued by credit card companies?
- 10. What procedure does a business use to collect amounts owed to it for sales on credit cards issued by credit card companies?
- 11. When a firm makes a sale involving a credit card issued by a credit card company, does the firm have an account receivable with the cardholder or with the credit card company?
- 12. What is the discount on credit card sales? What type of account is used to record this item?
- 13. Why are bank credit card sales similar to cash sales for a business?
- **14.** What is open-account credit?
- **15.** What is a trade discount? Why do some firms offer trade discounts to their customers?

APPLICATIONS





Exercise 7.1

Objective 7-1

Identifying the journal to record transactions.

The accounting system of Healthy Focus Natural Foods includes the journals listed below. Indicate the specific journal in which each of the transactions listed below would be recorded.

JOURNALS

| Cash receipts journal | Sales journal | Purchases journal |
|-----------------------|-----------------|-------------------|
| Cash payments journal | General journal | |

| DAT | E | TRANSACTIONS |
|-----|---|--|
| May | 1 | Sold merchandise on credit. |
| | 2 | Accepted a return of merchandise from a credit customer. |
| | 3 | Sold merchandise for cash. |
| | 4 | Purchased merchandise on credit. |
| | 5 | Gave a \$400 allowance for damaged merchandise. |
| | 6 | Collected sums on account from credit customers. |
| | 7 | Received an additional cash investment from the owner. |
| | 8 | Issued a check to pay a creditor on account. |

Identifying the accounts used to record sales and related transactions.

Exercise 7.2 Objective 7-1

The transactions below took place at Outdoor Adventures, a retail business that sells outdoor clothing and camping equipment. Indicate the numbers of the general ledger accounts that would be debited and credited to record each transaction.

GENERAL LEDGER ACCOUNTS

| 101 | Cash | 401 | Sales |
|-----|---------------------|-----|------------------------------|
| 111 | Accounts Receivable | 451 | Sales Returns and Allowances |
| 231 | Sales Tax Payable | | |

| DAT | Έ | TRANSACTIONS |
|-----|---|--|
| May | 1 | Sold merchandise on credit; the transaction involved sales tax. |
| | 2 | Received checks from credit customers on account. |
| 3 | | Accepted a return of merchandise from a credit customer; the original sale involved sales tax. |
| | 4 | Sold merchandise for cash; the transaction involved sales tax. |
| | 5 | Gave an allowance to a credit customer for damaged merchandise; the original sale involved sales tax. |
| | 6 | Provided a cash refund to a customer who returned merchandise; the original sale was made for cash and involved sales tax. |

Recording credit sales.

The following transactions took place at Outdoor Adventures during May. Enter these transactions in a sales journal like the one shown in Figure 7.2. Use 18 as the page number for the sales journal.

| DAT | E | TRANSACTIONS |
|-----|---|--|
| Мау | 1 | Sold a tent and other items on credit to Justin Williams; issued Sales Slip 1101 for \$550 plus sales tax of \$44. |
| | 2 | Sold a backpack, an air mattress, and other items to Diane Le; issued Sales Slip 1102 for \$500 plus sales tax of \$40. |
| 3 | | Sold a lantern, cooking utensils, and other items to Richard Rodriguez; issued Sales Slip 1103 for \$575 plus sales tax of \$46. |

Recording sales returns and allowances.

Record the general journal entries for the following transactions of Luxurious Linens that occurred in June. Use 15 as the page number for the general journal.

| DATE | TRANSACTIONS |
|--------|---|
| June 5 | Accepted a return of damaged merchandise from Tiffany Monroe, a credit customer; issued Credit Memorandum 301 for \$918, which includes sales tax of \$68; the original sale was made on Sales Slip 1610 of May 31. |
| 25 | Gave an allowance to Brian Barnes, a credit customer, for merchandise that was slightly damaged but usable; issued Credit Memorandum 302 for \$1,242, which includes sales tax of \$92; the original sale was made on Sales Slip 1663 of June 17. |

Exercise 7.3

Objective 7-2

CONTINUING >>>

Exercise 7.4

Objective 7-2

Exercise 7.5

Objective 7-2

Posting from the sales journal.

The sales journal for Charleston Company is shown below. Describe how the amounts would be posted to the general ledger accounts.

| | SALES JOURNAL PAGE1_ | | | | | | | | | | | | | | | | |
|----|----------------------|----|----------------------|----------------------------|---------------|---------------------------------|-----|-----|--------------------------------|----|-----|------------|---|----|-----|----|----|
| | DATI | E | SALES SLIP NO. | CUSTOMER'S ACCOUNT DEBITED | POST. REF. | ACCOUNTS RECEIVABLE DEBIT | | | SALES TAX PAYABLE CREDIT | | | ABLE SALES | | | | | |
| 1 | 2016 | | | | | | | | | | | | | | | | 1 |
| 2 | July | 2 | 1101 | Scott Cohen | | | 5 | 40 | 00 | | 4 | 00 | | 5 | 00 | 00 | 2 |
| 3 | | 7 | 1102 | Julia Hoang | | | 8 | 5 4 | 00 | | 6 | 4 00 | | 8 | 00 | 00 | 3 |
| | | | | | | | | | | | | | | | | | |
| 11 | | 31 | 1110 | Barbara Baxter | | | 3 , | 24 | 00 | | 2 | 4 00 | | 3 | 00 | 00 | 11 |
| 12 | | 31 | | Totals | | 6 | 4 | 3 O | 00 | 4 | 48 | 00 | 6 | 0 | 00 | 00 | 12 |
| 13 | | | | | | | (1. | 11, |) | (. | 231 |) | | (4 | 01) | | 13 |
| 14 | | | | | | | | | | | | | | | | | 14 |

Exercise 7.6

Computing a trade discount.

Objective 7-7

The Alpha Wholesale Company made sales using the following list prices and trade discounts. What amount will be recorded for each sale in the sales journal?

- 1. List price of \$600 and trade discount of 10 percent
- 2. List price of \$750 and trade discount of 20 percent
- 3. List price of \$250 and trade discount of 30 percent

Exercise 7.7

Computing a series of trade discounts.

Objective 7-7

Patio Dudes, a wholesale firm, made sales using the following list prices and trade discounts. What amount will be recorded for each sale in the sales journal?

- 1. List price of \$6,250 and trade discounts of 20 and 12 percent
- 2. List price of \$4,000 and trade discounts of 30 and 10 percent
- 3. List price of \$2,500 and trade discounts of 20 and 5 percent

Exercise 7.8

Computing the sales tax due and recording its payment.

Objective 7-9

The balances of certain accounts of Vanessa Corporation on April 30, 2016, were as follows:

Sales \$230,000 Sales Returns and Allowances \$ 4,000

The firm's net sales are subject to a 6 percent sales tax. Prepare the general journal entry to record payment of the sales tax payable on April 30, 2016.

Exercise 7.9

Preparing a schedule of accounts receivable.

Objective 7-6

The accounts receivable ledger for The Old Country Barn follows on the next page.

- 1. Prepare a schedule of accounts receivable as of January 31, 2016.
- **2.** What should the balance in the *Accounts Receivable* (control) account be?

Exercise 7.10

Posting sales returns and allowances.

Objective 7-5

Post the journal entries on page 222 to the appropriate ledger accounts. Assume the following account balances as of March 1, 2016:

| Accounts Receivable (control account) | \$1,688 |
|---------------------------------------|---------|
| Accounts Receivable — Cara Fountain | 940 |
| Accounts Receivable — Sadie Palmer | 748 |

| DA | ГЕ | | DES | CRIPTI | ON | POST REF. | | DEBI | Т | | CRE | DIT | | В | ALAN | CE | | | | | | | | | | | | | | | | |
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| 016 | | | | | 1101 | | | | | | | \dashv | | | T | | | | | | | | | | | | | | | | | |
| 1. | 1 | Bala | ınce | | | 1 | | | | | | | | | 5 7 | _ | _ | | | | | | | | | | | | | | | |
| | 2 | Sale | s Slip | 1801 | | S1 | ╙ | 5 4 | 0 00 | | | 4 | 4 | 2 | 1 1 | 5 (| 00 | | | | | | | | | | | | | | | |
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| | + | | 27 | Sale | s Slip 18 | 324 | | S1 | | 1 8 ! | 9 0 | 0 | 2 | 0 / | 0.0 | | _ | | 7 | | | | | | | | | | | | | |
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| 2 | Mar. | 14 | Sales Returns and Allowances | | | 3 | 0 | 0 | 00 | | | | | | 2 |
| 3 | | | Sales Tax Payable | | | | 2 | 4 | 00 | | | | | | 3 |
| 4 | | | Accounts Rec.—Cara Fountain | | | | | | | | 3 | 2 | 4 | 00 | 4 |
| 5 | | | Accepted return on defective | | | | | | | | | | | | 5 |
| 6 | | | merchandise, Credit Memo | | | | | | | | | | | | 6 |
| 7 | | | 101; original sale of Feb. 23, | | | | | | | | | | | | 7 |
| 8 | | | Sales Slip 1101 | | | | | | | | | | | | 8 |
| 9 | | | | | | | | | | | | | | | 9 |
| 10 | | 22 | Sales Returns and Allowances | | | 1 | 0 | 0 | 00 | | | | | | 10 |
| 11 | | | Sales Tax Payable | | | | | 8 | 00 | | | | | | 11 |
| 12 | | | Accounts Rec.—Sadie Palmer | | | | | | | | 1 | 0 | 8 | 00 | 12 |
| 13 | | | Gave allowance for damaged | | | | | | | | | | | | 13 |
| 14 | | | merchandise, Credit Memo | | | | | | | | | | | | 14 |
| 15 | | | 102; original sale Mar. 15, | | | | | | | | | | | | 15 |
| 16 | | | Sales Slip 1150 | | | | | | | | | | | | 16 |

PROBLEMS

Problem Set A



Problem 7.1A

Objectives 7-1, 7-2

Sage 50 Complete Accounting

Recording credit sales and posting from the sales journal.

Best Appliances is a retail store that sells household appliances. Merchandise sales are subject to an 8 percent sales tax. The firm's credit sales for July are listed below, along with the general ledger accounts used to record these sales. The balance shown for Accounts Receivable is for the beginning of the month.

| DAT | E | TRANSACTIONS |
|------|----|--|
| July | 1 | Sold a dishwasher to Perry Martin; issued Sales Slip 501 for \$1,150 plus sales tax of \$92. |
| | 6 | Sold a washer to Cindy Han; issued Sales Slip 502 for \$2,425 plus sales tax of \$194. |
| | 11 | Sold a high-definition television set to Richard Slocomb; issued Sales Slip 503 for \$2,600 plus sales tax of \$208. |
| | 17 | Sold an electric dryer to Mary Schneider; issued Sales Slip 504 for \$1,275 plus sales tax of \$102. |
| | 23 | Sold a trash compactor to Veronica Velazquez; issued Sales Slip 505 for \$900 plus sales tax of \$72. |
| | 27 | Sold a color television set to Jeff Budd; issued Sales Slip 506 for \$1,725 plus sales tax of \$138. |
| | 29 | Sold an electric range to Michelle Ly; issued Sales Slip 507 for \$1,450 plus sales tax of \$116. |
| | 31 | Sold a double oven to Phil Long; issued Sales Slip 508 for \$625 plus sales tax of \$50. |

INSTRUCTIONS

- 1. Open the general ledger accounts and enter the balance of *Accounts Receivable* for July 1,
- 2. Record the transactions in a sales journal like the one shown in Figure 7.4. Use 8 as the journal page number.

- **3.** Total, prove, and rule the sales journal as of July 31.
- **4.** Post the column totals from the sales journal to the proper general ledger accounts.

GENERAL LEDGER ACCOUNTS

- 111 Accounts Receivable, \$34,500 Dr.
- 231 Sales Tax Payable
- 401 Sales

Analyze: What percentage of credit sales were for entertainment items?

Journalizing, posting, and reporting sales transactions.

Towncenter Furniture specializes in modern living room and dining room furniture. Merchandise sales are subject to an 8 percent sales tax. The firm's credit sales and sales returns and allowances for February 2016 are reflected below, along with the general ledger accounts used to record these transactions. The balances shown are for the beginning of the month.

| DATE | TRANCACTIONS |
|--------|---|
| DATE | TRANSACTIONS |
| Feb. 1 | Sold a living room sofa to Sun Yoo; issued Sales Slip 1615 for \$4,790 plus sales tax of \$383.20. |
| 5 | Sold three recliners to Jacqueline Moore; issued Sales Slip 1616 for \$2,350 plus sales tax of \$188. |
| 9 | Sold a dining room set to Hazel Tran; issued Sales Slip 1617 for \$6,550 plus sales tax of \$524. |
| 11 | Accepted a return of one damaged recliner from Jacqueline Moore that was originally sold on Sales Slip 1616 of February 5; issued Credit Memorandum 702 for \$1,026, which includes sales tax of \$76.00. |
| 17 | Sold living room tables and bookcases to Ann Brown; issued Sales Slip 1618 for \$9,550 plus sales tax of \$764. |
| 23 | Sold eight dining room chairs to Domingo Salas; issued Sales Slip 1619 for \$3,650 plus sales tax of \$292. |
| 25 | Gave Ann Brown an allowance for scratches on her bookcases; issued Credit Memorandum 703 for \$702, which includes sales taxes of \$52; the bookcases were originally sold on Sales Slip 1618 of February 17. |
| 27 | Sold a living room sofa and four chairs to Jose Saucedo; issued Sales Slip 1620 for \$4,225 plus sales tax of \$338. |
| 28 | Sold a dining room table to Mimi Yuki; issued Sales Slip 1621 for \$2,050 plus sales tax of \$164. |
| 28 | Sold a living room modular wall unit to Alan Baker; issued Sales Slip 1622 for \$3,900 plus sales tax of \$312. |

INSTRUCTIONS

- 1. Open the general ledger accounts and enter the balances for February 1.
- **2.** Record the transactions in a sales journal and in a general journal. Use 8 as the page number for the sales journal and 24 as the page number for the general journal.
- **3.** Post the entries from the general journal to the general ledger.
- **4.** Total, prove, and rule the sales journal as of February 28.
- **5.** Post the column totals from the sales journal.
- **6.** Prepare the heading and the Revenue section of the firm's income statement for the month ended February 28, 2016.

◄ Problem 7.2A

Objectives 7-1, 7-2, 7-4

Sage 50
Complete Accounti



GENERAL LEDGER ACCOUNTS

- 111 Accounts Receivable, \$16,636 Dr.
- 231 Sales Tax Payable, \$7,270 Cr.
- 401 Sales
- 451 Sales Returns and Allowances

Analyze: Based on the beginning balance of the *Sales Tax Payable* account, what was the amount of net sales for January? (Hint: Sales tax returns are filed and paid to the state quarterly.)

Problem 7.3A Objectives 7-1, 7-2, 7-3, 7-4, 7-6

Recording sales transactions, posting to the accounts receivable ledger, and preparing a schedule of accounts receivable.

The Elegant Table sells china, glassware, and other gift items that are subject to an 8 percent sales tax. The shop uses a general journal and a sales journal similar to those illustrated in this chapter.

| DATE | TRANSACTIONS |
|--------|---|
| Nov. 1 | Sold china to Pauline Judge; issued Sales Slip 1001 for \$1,750 plus \$140 sales tax. |
| 5 | Sold a brass serving tray to Janet Hutchison; issued Sales Slip 1002 for \$2,350 plus \$188 sales tax. |
| 6 | Sold a vase to Charles Brown; issued Sales Slip 1003 for \$950 plus \$76 sales tax. |
| 10 | Sold a punch bowl and glasses to Lisa Morgan; issued Sales Slip 1004 for \$1,950 plus \$156 sales tax. |
| 14 | Sold a set of serving bowls to Dorothy Watts; issued Sales Slip 1005 for \$800 plus \$64 sales tax. |
| 17 | Gave Lisa Morgan an allowance because of a broken glass discovered when unpacking the punch bowl and glasses sold on November 10, Sales Slip 1004; issued Credit Memorandum 102 for \$162.00, which includes sales tax of \$12. |
| 21 | Sold a coffee table to Teresa Yu; issued Sales Slip 1006 for \$3,450 plus \$276 sales tax. |
| 24 | Sold sterling silver teaspoons to Henry Okafor; issued Sales Slip 1007 for \$850 plus \$68 sales tax. |
| 25 | Gave Teresa Yu an allowance for scratches on her coffee table sold on November 21, Sales Slip 1006; issued Credit Memorandum 103 for \$378, which includes \$28 in sales tax. |
| 30 | Sold a clock to Elaine Brock; issued Sales Slip 1008 for \$4,050 plus \$324 sales tax. |

INSTRUCTIONS

- 1. Record the transactions for November in the proper journal. Use 6 as the page number for the sales journal and 16 as the page number for the general journal.
- **2.** Immediately after recording each transaction, post to the accounts receivable ledger.
- **3.** Post the amounts from the general journal daily. Post the sales journal amount as a total at the end of the month.
- **4.** Prepare a schedule of accounts receivable. Compare the balance of the *Accounts Receivable* control account with the total of the schedule.

Analyze: Which customer has the highest balance owed at November 30, 2016?

Recording sales transactions, posting to the accounts receivable ledger, and preparing a schedule of accounts receivable.

Bella Floral Designs is a wholesale shop that sells flowers, plants, and plant supplies. The transactions shown below took place during January.

| 4 | Problem 7.4A |
|----------|----------------------|
| | Objectives 7-1, 7-2, |
| | 7-3, 7-4, 7-6 |

Sage 50
Complete Accounting



| DA | TE | TRANSACTIONS |
|------|----|---|
| Jan. | 3 | Sold a floral arrangement to Thomas Florist; issued Invoice 1081 for \$600. |
| | 8 | Sold potted plants to Carter Garden Supply; issued Invoice 1082 for \$825. |
| | 9 | Sold floral arrangements to Thomasville Flower Shop; issued Invoice 1083 for \$482. |
| | 10 | Sold corsages to Moore's Flower Shop; issued Invoice 1084 for \$630. |
| | 15 | Gave Thomasville Flower Shop an allowance because of withered blossoms discovered in one of the floral arrangements sold on Invoice 1083 on January 9; issued Credit Memorandum 101 for \$60. |
| | 20 | Sold table arrangements to Cedar Hill Floral Shop; issued Invoice 1085 for \$580. |
| | 22 | Sold plants to Applegate Nursery; issued Invoice 1086 for \$780. |
| | 25 | Sold roses to Moore's Flower Shop; issued Invoice 1087 for \$437. |
| | 27 | Sold several floral arrangements to Thomas Florist; issued Invoice 1088 for \$975. |
| | 31 | Gave Thomas Florist an allowance because of withered blossoms discovered in one of the floral arrangements sold on Invoice 1088 on January 27; issued Credit Memorandum 102 for \$200. |

INSTRUCTIONS

- 1. Record the transactions in the proper journal. Use 7 as the page number for the sales journal and 11 as the page number for the general journal.
- 2. Immediately after recording each transaction, post to the accounts receivable ledger.
- **3.** Post the amounts from the general journal daily. Post the sales journal amount as a total at the end of the month.
- **4.** Prepare a schedule of accounts receivable. Compare the balance of the *Accounts Receivable* control account with the total of the schedule.

Analyze: Damaged goods decreased sales by what dollar amount? By what percentage amount?

Problem Set B

Recording credit sales and posting from the sales journal.

J&J Appliances is a retail store that sells household appliances. Merchandise sales are subject to an 8 percent sales tax. The firm's credit sales for June are listed below Instruction 4, along with the general ledger accounts used to record these sales. The balance shown for Accounts Receivable is for the beginning of the month.

INSTRUCTIONS

- 1. Open the general ledger accounts and enter the balance of *Accounts Receivable* for June 1.
- **2.** Record the transactions in a sales journal like the one shown in Figure 7.4. Use 8 as the journal page number.

Problem 7.1B
Objectives 7-1, 7-2