

Accounting for Purchases and Accounts Payable

Williams-Sonoma www.williams-sonoma.com

Williams-Sonoma began in 1956, when Chuck Williams opened a small specialty cookware shop in Sonoma, California. By offering French kitchen equipment most Americans had never seen before, the store gained popularity among home cooks and professional chefs from across the country. Since its humble beginnings in the late 1950s, Williams-Sonoma has evolved into a multibillion-dollar corporation.

Part of this success has been keeping track of the items that customers want most and making sure that those items are in stock. To combat challenging economic conditions, not only has it lowered prices on some of its high-ticket items, but has also ramped up its e-mail marketing efforts and increased focus on new product lines and exclusive merchandise to gain new customers.

Since the company buys its products from so many different suppliers, it records all of its purchases made on account, in a special journal. By keeping detailed records of who it owes and how soon payment is due, the company is better able to monitor its cash payment needs.

These strategies seem to be paying off—the company recently reported that net earnings increased by 15 percent in the year ended January 29, 2012, compared to the prior year.



thinking critically

Do you think that companies such as Williams-Sonoma pay their bills at the last possible minute? Why or why not?

LEARNING OBJECTIVES	NEW TERMS	
<p>8-1. Record purchases of merchandise on credit in a three-column purchases journal.</p> <p>8-2. Post from the three-column purchases journal to the general ledger accounts.</p> <p>8-3. Post credit purchases from the purchases journal to the accounts payable subsidiary ledger.</p> <p>8-4. Record purchases returns and allowances in the general journal and post them to the accounts payable subsidiary ledger.</p> <p>8-5. Prepare a schedule of accounts payable.</p> <p>8-6. Compute the net delivered cost of purchases.</p> <p>8-7. Demonstrate a knowledge of the procedures for effective internal control of purchases.</p> <p>8-8. Record purchases, sales, and returns using the perpetual inventory system.</p> <p>8-9. Define the accounting terms new to this chapter.</p>	<p>accounts payable ledger</p> <p>cash discount</p> <p>cost of goods sold</p> <p>Freight In account</p> <p>periodic inventory system</p> <p>perpetual inventory system</p> <p>purchase allowance</p> <p>purchase invoice</p> <p>purchase order</p> <p>purchase requisition</p>	<p>purchase return</p> <p>Purchases account</p> <p>purchases discount</p> <p>purchases journal</p> <p>receiving report</p> <p>sales discount</p> <p>sales invoice</p> <p>schedule of accounts payable</p> <p>Transportation In account</p>

Section 1

SECTION OBJECTIVES	TERMS TO LEARN
<p>>> 8-1. Record purchases of merchandise on credit in a three-column purchases journal.</p> <p>WHY IT'S IMPORTANT Most merchandisers purchase goods on credit, and the use of a special journal improves efficiency when recording these transactions.</p> <p>>> 8-2. Post from the three-column purchases journal to the general ledger accounts.</p> <p>WHY IT'S IMPORTANT Summary postings from the purchases journal minimize repetitive tasks.</p>	<p>cash discount cost of goods sold <i>Freight In</i> account purchase invoice purchase order purchase requisition <i>Purchases</i> account purchases discount purchases journal receiving report sales discount sales invoice <i>Transportation In</i> account</p>

Merchandise Purchases

In this chapter, you will learn how Maxx-Out Sporting Goods manages its purchases of goods for resale and its accounts payable.

Accounting for Purchases

Most merchandising businesses purchase goods on credit under open-account arrangements. A large firm usually has a centralized purchasing department that is responsible for locating suppliers, obtaining price quotations, negotiating credit terms, and placing orders. In small firms, purchasing activities are handled by a single individual, usually the owner or manager.

PURCHASING PROCEDURES

When a sales department needs goods, it sends the purchasing department a purchase requisition (Figure 8.1). A **purchase requisition** lists the items to be ordered. It is signed by someone with the authority to approve requests for merchandise, usually the manager of the sales department. The purchasing department selects a supplier who can furnish the goods at a competitive price and then issues a purchase order (Figure 8.2). The **purchase order** specifies the exact items, quantity, price, and credit terms. It is signed by someone with authority to approve purchases, usually the purchasing agent.

When the goods arrive at the business, they are inspected. A **receiving report** is prepared to show the quantity and condition of the goods received. The purchasing department receives a copy of the receiving report and compares it to the purchase order. If defective goods or the wrong quantity of goods are received, the purchasing department contacts the supplier and settles the problem.

Figure 8.3 shows the invoice, or **bill**, for items ordered and shipped. The customer, Maxx-Out Sporting Goods, calls it a **purchase invoice**. The supplier, International Sportsman, calls it a **sales invoice**. The customer's accounting department compares the invoice to copies of the purchase order and receiving report. The accounting department checks the quantities, prices, and math on the invoice and then records the purchase. It is important to record purchases in the accounting records as soon as the invoice is verified. Shortly before the due date of the invoice, the accounting department issues a check to the supplier and records the payment.

The purchasing department for The Home Depot, Inc., purchases 30,000 to 40,000 different kinds of home improvement supplies, building materials, and lawn and garden products.

Maxx-Out Sporting Goods
 2007 Trendsetter Lane
 Dallas, TX 75268-0967

PURCHASE REQUISITION
 No. 325

DEPARTMENT Men's DATE OF REQUEST January 2, 2016
 ADVISE ON DELIVERY Max Ferraro DATE REQUIRED January 25, 2016

QUANTITY	DESCRIPTION
10	Assorted colors men's sweatsuits

APPROVED BY _____ REQUESTED BY _____

FOR PURCHASING DEPARTMENT USE ONLY

PURCHASE ORDER 9001 ISSUED TO: International Sportsman
 DATE January 5, 2016 1718 Sherry Lane
Denton, TX 75267-6205

FIGURE 8.1
 Purchase Requisition

Maxx-Out Sporting Goods
 2007 Trendsetter Lane
 Dallas, TX 75268-0967

PURCHASE ORDER

To
International Sportsman
1718 Sherry Lane
Denton, TX 75267-6205
 Date: January 5, 2016
 Order No: 9001
 Terms: n/30
 FOB: Denton

QUANTITY	ITEM	UNIT PRICE	TOTAL
10	Assorted colors men's sweatsuits	55.00	550.00

APPROVED BY Max Ferraro

FIGURE 8.2
 Purchase Order

International Sportsman INVOICE NO. 7985
 1718 Sherry Lane
 Denton, TX 75267-6205

SOLD TO: Maxx-Out Sporting Goods DATE: January 23, 2016
 2007 Trendsetter Lane ORDER NO.: 9001
 Dallas, TX 75268-0967 SHIPPED BY: Metroplex Express
 TERMS: n/30

YOUR ORDER NO.	SALESPERSON	TERMS	
9001		n/30	
DATE SHIPPED	SHIPPED BY	FOB	
January 23, 2016	Metroplex Express	Denton	
QUANTITY	DESCRIPTION	UNIT PRICE	TOTAL
10	Assorted colors men's sweatsuits	55 00	550 00
	Freight		50 00
	Total		600 00

FIGURE 8.3
 Invoice

THE PURCHASES ACCOUNT

The purchase of merchandise for resale is a cost of doing business. The purchase of merchandise is debited to the **Purchases account**. **Purchases** is a temporary account classified as a cost of goods sold account. The **cost of goods sold** is the actual cost to the business of the merchandise sold to customers.

Cost of goods sold accounts follow the debit and credit rules of expense accounts. The **Purchases** account is increased by debits and decreased by credits. Its normal balance is a debit. In the chart of accounts, the cost of goods sold accounts appear just before the expense accounts.

Walmart purchases private-label products from suppliers and markets these as Walmart brands. Products such as Ol'Roy™ dog food and EverStart® batteries are purchased at lower costs than nationally known brands. Thus, Walmart can sell these items at a lower price to its customers.

FREIGHT CHARGES FOR PURCHASES

Sometimes the buyer pays the freight charge—the cost of shipping the goods from the seller's warehouse to the buyer's location. There are two ways to handle the freight charges paid by the buyer:

- The buyer is billed directly by the transportation company for the freight charge. The buyer issues a check directly to the freight company.
- The seller pays the freight charge and includes it on the invoice. The invoice includes the price of the goods and the freight charge.

The freight charge is debited to the **Freight In** or **Transportation In account**. This is a cost of goods sold account showing transportation charges for merchandise purchased. The buyer enters three elements in the accounting records:

Price of goods (debit Purchases)	\$550.00
Freight charge (debit Freight In)	50.00
Total invoice (credit Accounts Payable)	\$600.00

Purchases		Freight In		Accounts Payable	
Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
+	—	+	—	—	+
550		50			600

THE PURCHASES JOURNAL

For most merchandising businesses, it is not efficient to enter purchases of goods in the general journal. Instead, credit purchases of merchandise are recorded in a special journal called the **purchases journal**.

The following illustrates how credit purchases appear in a general journal. Each entry involves a debit to **Purchases** and **Freight In** and a credit to **Accounts Payable** plus a detailed explanation.

These 4 general journal entries require 12 separate postings to general ledger accounts: 4 to **Purchases**, 4 to **Freight In**, and 4 to **Accounts Payable**. As you can see from the ledger accounts that follow, it takes a great deal of time and effort to post these entries.

important!

Credit Purchases

The purchases journal is used to record only credit purchases of merchandise for resale. Credit purchases of other items used in the business are recorded in the general journal.

GENERAL JOURNAL						PAGE <u>1</u>
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT		
2016					1	
Jan. 3	Purchases	501	2 675 00		2	
	Freight In	502	190 00		3	
	Accounts Payable	205		2 865 00	4	
	Purchased merchandise from					
	Active Designs, Invoice 5879,					
	dated January 2, 2016,					
	terms 2/10, n/30					
					9	
5	Purchases	501	3 880 00		10	
	Freight In	502	175 00		11	
	Accounts Payable	205		4 055 00	12	
	Purchased merchandise from					
	The Sports Warehouse, Invoice 633,					
	dated January 3, 2016,					
	terms n/30					
					17	
6	Purchases	501	2 900 00		18	
	Freight In	502	240 00		19	
	Accounts Payable	205		3 140 00	20	
	Purchased merchandise from					
	The Modern Sportsman,					
	Invoice 8011, dated					
	January 4, 2016, terms n/30					
					25	
7	Purchases	501	3 675 00		26	
	Freight In	502	260 00		27	
	Accounts Payable	205		3 935 00	28	
	Purchased merchandise from					
	World of Sports, Invoice 4321,					
	dated January 4, 2016,					
	terms 2/10, n/30					

ACCOUNT Accounts Payable ACCOUNT NO. 205

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE	
					DEBIT	CREDIT
2016						
Jan. 1	Balance	✓				10 800 00
3	J1			2 865 00		13 665 00
5	J1			4 055 00		17 720 00
6	J1			3 140 00		20 860 00
7	J1			3 935 00		24 795 00

ACCOUNT Purchases ACCOUNT NO. 501

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE	
					DEBIT	CREDIT
2016						
Jan. 3	J1		2 675 00		2 675 00	
5	J1		3 880 00		6 555 00	
6	J1		2 900 00		9 455 00	
7	J1		3 675 00		13 130 00	

>> **8-1. OBJECTIVE**

Record purchases of merchandise on credit in a three-column purchases journal.

ACCOUNT <i>Freight In</i>						ACCOUNT NO. <u>502</u>					
DATE	DESCRIPTION	POST. REF.	DEBIT			CREDIT			BALANCE		
									DEBIT	CREDIT	
2016											
Jan. 3		J1	1	9	00			1	9	00	
5		J1	1	7	50			3	6	50	
6		J1	2	4	00			6	0	50	
7		J1	2	6	00			8	6	50	

Figure 8.4 shows the purchases journal for Maxx-Out Sporting Goods. Remember that the purchases journal is only for credit purchases of merchandise for resale to customers. Notice how the columns efficiently organize the data about the credit purchases. The purchases journal makes it possible to record each purchase on a single line. In addition, there is no need to enter account names and descriptions.

RECORDING TRANSACTIONS IN A PURCHASES JOURNAL

Use the information on the purchase invoice to make the entry in the purchases journal:

1. Enter the date, supplier name, invoice number, invoice date, and credit terms.
2. In the Accounts Payable Credit column, enter the total owed to the supplier.
3. In the Purchases Debit column, enter the price of the goods purchased.
4. In the Freight In Debit column, enter the freight amount.

The total of the Purchases Debit and Freight In Debit columns must equal the amount entered in the Accounts Payable Credit column.

The invoice date and credit terms determine when payment is due. The following credit terms often appear on invoices:

- *Net 30 days* or *n/30* means that payment in full is due 30 days after the date of the invoice.
- *Net 10 days EOM*, or *n/10 EOM*, means that payment in full is due 10 days after the end of the month in which the invoice was issued.
- *2% 10 days, net 30 days*, or *2/10, n/30* means that if payment is made within 10 days of the invoice date, the customer can take a 2 percent discount. Otherwise, payment in full is due in 30 days.

The 2 percent discount is a **cash discount**; it is a discount offered by suppliers to encourage quick payment by customers. To the customer it is known as a **purchases discount**. To the supplier it is known as a **sales discount**.

FIGURE 8.4 Purchases Journal

PURCHASES JOURNAL									PAGE <u>1</u>
DATE	PURCHASED FROM	INVOICE NUMBER	INVOICE DATE	TERMS	POST. REF.	ACCOUNTS PAYABLE CREDIT	PURCHASES DEBIT	FREIGHT IN DEBIT	
2016									
Jan. 3	Active Designs	5879	01/02/16	2/10, n/30		2 865 00	2 675 00	190 00	
5	The Sports Warehouse	633	01/03/16	n/30		4 055 00	3 880 00	175 00	
6	The Modern Sportsman	8011	01/04/16	n/30		3 140 00	2 900 00	240 00	
7	World of Sports	4321	01/04/16	2/10, n/30		3 935 00	3 675 00	260 00	
19	Athletic Equipment, Inc.	8997	01/15/16	2/10, n/30		4 200 00	3 860 00	340 00	
23	International Sportsman	7985	01/22/16	n/30		600 00	550 00	50 00	
31						18 795 00	17 540 00	1 255 00	

FIGURE 8.5 Posting to the General Ledger

PURCHASES JOURNAL									PAGE
DATE	CUSTOMER'S NAME	INVOICE NUMBER	INVOICE DATE	TERMS	POST. REF.	ACCOUNTS PAYABLE CREDIT	PURCHASES DEBIT	FREIGHT IN DEBIT	1
2016									
Jan. 3	Active Designs	5879	01/02/16	2/10, n/30	✓	2 865 00	2 675 00	190 00	
5	The Sports Warehouse	633	01/03/16	n/30	✓	4 055 00	3 880 00	175 00	
6	The Modern Sportsman	8011	01/04/16	n/30	✓	3 140 00	2 900 00	240 00	
7	World of Sports	4321	01/04/16	2/10, n/30	✓	3 035 00	3 675 00	260 00	
19	Athletic Equipment, Inc.	8997	01/15/16	2/10, n/30	✓	4 200 00	3 860 00	340 00	
23	International Sportsman	7985	01/22/16	n/30	✓	600 00	550 00	50 00	
31						18 795 00	17 540 00	1 255 00	
						(205)	(501)	(502)	

ACCOUNT <i>Accounts Payable</i>						ACCOUNT NO. 205
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE	
					DEBIT	CREDIT
2016						
Jan. 1	Balance	✓			10 800 00	
31		P1		18 795 00	29 595 00	

ACCOUNT <i>Purchases</i>						ACCOUNT NO. 501
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE	
					DEBIT	CREDIT
2016						
Jan. 31		P1	17 540 00		17 540 00	

ACCOUNT <i>Freight In</i>						ACCOUNT NO. 502
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE	
					DEBIT	CREDIT
2016						
Jan. 31		P1	1 255 00		1 255 00	

POSTING TO THE GENERAL LEDGER

The purchases journal simplifies the posting process. Summary amounts are posted at the end of the month. Refer to Figure 8.5 as you learn how to post from the purchases journal to the general ledger accounts.

Total the Accounts Payable Credit, the Purchases Debit, and the Freight In Debit columns. Before posting, prove the equality of the debits and credits recorded in the purchases journal.

>> 8-2. OBJECTIVE

Post from the three-column purchases journal to the general ledger accounts.

Proof of Purchases Journal	
Debits	
Purchases Debit column	\$17,540.00
Freight In Debit column	1,255.00
	<u>\$18,795.00</u>
Credits	
Accounts Payable Credit column	<u>\$18,795.00</u>

important!

Cash Discounts

In the purchases journal, record the amount shown on the invoice. The cash discount is recorded when the payment is made.

After the equality of debits and credits is verified, rule the purchases journal. The steps to post the column totals to the general ledger follow:

1. Locate the *Accounts Payable* ledger account.
2. Enter the date.
3. Enter the posting reference, P1. The **P** is for purchases journal. The **1** is the purchases journal page number.
4. Enter the amount from the Accounts Payable Credit column in the purchases journal in the Credit column of the *Accounts Payable* ledger account.
5. Compute the new balance and enter it in the Balance Credit column.
6. In the purchases journal, enter the *Accounts Payable* ledger account number (205) under the column total.
7. Repeat the steps for the *Purchases* Debit and *Freight In* Debit columns.

During the month, the individual entries in the purchases journal are posted to the creditor accounts in the accounts payable ledger. The check marks in the purchases journal in Figure 8.5 indicate that these postings have been completed. This procedure is discussed later in this chapter.

ADVANTAGES OF A PURCHASES JOURNAL

Every business has certain types of transactions that occur over and over again. A well-designed accounting system includes journals that permit efficient recording of such transactions. In most merchandising firms, purchases of goods on credit take place often enough to make it worthwhile to use a purchases journal.

A special journal for credit purchases of merchandise saves time and effort when recording and posting purchases. The use of a purchases journal and other special journals allows for the division of accounting work among different employees. The purchases journal strengthens the audit trail. All credit purchases are recorded in one place, and each entry refers to the number and date of the invoice.

Section 1 Self Review

QUESTIONS

1. What activities does a purchasing department perform?
2. What type of transaction is recorded in the purchases journal?
3. What are the advantages of using a purchases journal?

EXERCISES

4. When the sales department needs goods, what document is sent to the purchasing department?
 - a. Purchase invoice
 - b. Purchase order

- c. Purchase requisition
 - d. Sales requisition
5. What form is sent to the supplier to order goods?
 - a. Purchase invoice
 - b. Purchase order
 - c. Purchase requisition
 - d. Sales invoice

ANALYSIS

6. An invoice dated March 15 for \$4,000 shows credit terms 2/10, n/30. What do the credit terms mean?

(Answers to Section 1 Self Review are on page 268.)

Section 2

SECTION OBJECTIVES	TERMS TO LEARN
<p>>> 8-3. Post credit purchases from the purchases journal to the accounts payable subsidiary ledger.</p> <p>WHY IT'S IMPORTANT Up-to-date records allow prompt payment of invoices.</p> <p>>> 8-4. Record purchases returns and allowances in the general journal and post them to the accounts payable subsidiary ledger.</p> <p>WHY IT'S IMPORTANT For unsatisfactory goods received, an allowance or return is reflected in the accounting records.</p> <p>>> 8-5. Prepare a schedule of accounts payable.</p> <p>WHY IT'S IMPORTANT This schedule provides a snapshot of amounts owed to suppliers.</p> <p>>> 8-6. Compute the net delivered cost of purchases.</p> <p>WHY IT'S IMPORTANT This is an important component in measuring operational results.</p> <p>>> 8-7. Demonstrate a knowledge of the procedures for effective internal control of purchases.</p> <p>WHY IT'S IMPORTANT Businesses try to prevent fraud, errors, and holding excess inventory.</p> <p>>> 8-8. Record purchases, sales, and returns using the perpetual inventory system.</p> <p>WHY IT'S IMPORTANT Larger businesses require up-to-date information about inventories on hand and use the perpetual system.</p>	<p>accounts payable ledger periodic inventory system perpetual inventory system purchase allowance purchase return schedule of accounts payable</p>

Accounts Payable

Businesses that buy merchandise on credit can conduct more extensive operations and use financial resources more effectively than if they paid cash for all purchases. It is important to pay invoices on time so that the business maintains a good credit reputation with its suppliers.

The Accounts Payable Ledger

Businesses need detailed records in order to pay invoices promptly. The **accounts payable ledger** provides information about the individual accounts for all creditors. The accounts payable ledger is a subsidiary ledger; it is separate from and subordinate to the general ledger. The accounts payable ledger contains a separate account for each creditor. Each account shows purchases, payments, and returns and allowances. The balance of the account shows the amount owed to the creditor.

Figure 8.6 on the next page shows the accounts payable ledger account for International Sportsman. Notice that the Balance column does not indicate whether the balance is a debit or a credit. The form assumes that the balance will be a credit because the normal balance of liability accounts is a credit. A debit balance may exist if more than the amount owed was paid to the creditor or if returned goods were already paid for. If the balance is a debit, circle the amount to show that the account does not have the normal balance.

Small businesses like Maxx-Out Sporting Goods arrange the accounts payable ledger in alphabetical order. Large businesses and businesses that use computerized accounting systems assign an account number to each creditor and arrange the accounts payable ledger in numeric order.

>> **8-3. OBJECTIVE**

Post credit purchases from the purchases journal to the accounts payable subsidiary ledger.

POSTING A CREDIT PURCHASE

To keep the accounting records up to date, invoices are posted to the accounts payable subsidiary ledger every day. Refer to Figure 8.6 as you learn how to post to the accounts payable ledger.

1. Locate the accounts payable ledger account for the creditor International Sportsman.
2. Enter the date.
3. In the Description column, enter the invoice number and date.
4. In the Posting Reference column, enter the purchases journal page number.
5. Enter the amount from the *Accounts Payable* Credit column in the purchases journal in the Credit column of the accounts payable subsidiary ledger.
6. Compute and enter the new balance in the Balance column.
7. In the purchases journal (Figure 8.5 on page 241), enter a check mark (✓) in the Posting Reference column. This indicates that the transaction is posted in the accounts payable subsidiary ledger.

POSTING CASH PAID ON ACCOUNT

When the transaction involves cash paid on account to a supplier, the payment is first recorded in a cash payments journal. (The cash payments journal is discussed in Chapter 9.) The cash payment is then posted to the individual creditor’s account in the accounts payable ledger. Figure 8.7 shows a posting for cash paid to a creditor on January 27.

>> **8-4. OBJECTIVE**

Record purchases returns and allowances in the general journal and post them to the accounts payable subsidiary ledger.

Purchases Returns and Allowances

When merchandise arrives, it is examined to confirm that it is satisfactory. Occasionally, the wrong goods are shipped, or items are damaged or defective. A **purchase return** is when the business returns the goods. A **purchase allowance** is when the purchaser keeps the goods but receives a reduction in the price of the goods. The supplier issues a credit memorandum for the return or allowance. The credit memorandum reduces the amount that the purchaser owes.

Purchases returns and allowances are entered in the *Purchases Returns and Allowances* account, not in the *Purchases* account. The *Purchases Returns and Allowances* account is a complete record of returns and allowances. Business managers analyze this account to identify problem suppliers.

Purchases Returns and Allowances is a contra cost of goods sold account. The normal balance of cost of goods sold accounts is a debit. The normal balance of *Purchases Returns and Allowances*, a contra cost of goods sold account, is a credit.

RECORDING PURCHASES RETURNS AND ALLOWANCES

Maxx-Out Sporting Goods received merchandise from International Sportsman on January 23. Some goods were damaged, and the supplier granted a \$100 purchase allowance. Maxx-Out Sporting Goods recorded the full amount of the invoice, \$600, in the purchases journal. The purchase allowance was recorded separately in the general journal.

recall

Subsidiary Ledger

The total of the accounts in the subsidiary ledger must equal the control account balance.

FIGURE 8.6

Accounts Payable Ledger Account

NAME		International Sportsman		TERMS		n/30	
ADDRESS		1718 Sherry Lane, Dallas, Texas 75267-6205					
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		
2016							
Jan.	1 Balance	✓			1 6 0 0 00		
	23 Invoice 7985, 01/23/16	P1		6 0 0 0 00	2 2 0 0 00		

NAME <u>International Sportsman</u>		TERMS <u>n/30</u>			
ADDRESS <u>1718 Sherry Lane, Dallas, Texas 75267-6205</u>					
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE
2016					
Jan. 1	Balance	✓			1 6 0 0 00
23	Invoice 7985, 01/23/16	P1		6 0 0 00	2 2 0 0 00
27		CP1	1 0 0 0 00		1 2 0 0 00

FIGURE 8.7

Posting a Payment Made on Account

BUSINESS TRANSACTION

On January 30, Maxx-Out Sporting Goods received a credit memorandum for \$100 from International Sportsman as an allowance for damaged merchandise.

International Sportsman

1718 Sherry Lane
Dallas, TX 75267-6205

TO: Maxx-Out Sporting Goods
2007 Trendsetter Lane
Dallas, TX 75268-0967

CREDIT MEMORANDUM

NUMBER: 103
DATE: January 30, 2016

ORIGINAL INVOICE: 7985
INVOICE DATE: January 23, 2016
DESCRIPTION: Credit for damaged merchandise: \$100.00

ANALYSIS

The liability account, **Accounts Payable**, is decreased by \$100. The contra cost of goods sold account, **Purchases Returns and Allowances**, is increased by \$100.

DEBIT-CREDIT RULES

DEBIT Decreases to liabilities are debits. Debit **Accounts Payable** for \$100.

CREDIT Increases to contra cost of goods sold accounts are recorded as credits. Credit **Purchases Returns and Allowances** for \$100.

T-ACCOUNT PRESENTATION

Accounts Payable		Purchases Returns and Allowances	
-	+	-	+
100			100

GENERAL JOURNAL ENTRY

GENERAL JOURNAL					PAGE <u>1</u>
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	
15 Jan. 30	Accounts Payable/International Sportsman		100 00		15
16	Purchases Returns and Allowances			100 00	16
17	Received Credit Memo 103 for				17
18	damaged merchandise returned;				18
19	original Invoice 7985,				19
20	January 23, 2016				20

THE BOTTOM LINE

Purchase Allowance

Income Statement

Contra Cost of Goods Sold	↑ 100
Net Income	↑ 100

Balance Sheet

Liabilities	↓ 100
Equity	↑ 100

FIGURE 8.8

Posting to a Creditor's Account

recall

Contra Accounts

The **Purchases Returns and Allowances** account is a contra account. Contra accounts have normal balances that are the opposite of related accounts.

GENERAL JOURNAL							PAGE <u>1</u>
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT			
1	2016					1	
15	Jan. 30	Accounts Payable/International Sportsman	205 ✓	1 0 0 0 0		16	
16		Purchases Returns and Allowances	503		1 0 0 0 0	17	
17		Received Credit Memo 103 for				18	
18		damaged merchandise				19	
19		returned; original				20	
20		Invoice 7985, January 23, 2016				21	
21						22	
22							

NAME <u>International Sportsman</u>		TERMS <u>n/30</u>	
ADDRESS <u>1718 Sherry Lane, Dallas, Texas 75267-6205</u>			

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE
2016					
Jan. 1	Balance	✓			1 6 0 0 0 0
23	Invoice 7985, 01/23/16	P1		6 0 0 0 0	2 2 0 0 0 0
27		CP1	1 0 0 0 0 0		1 2 0 0 0 0
30	CM 103	J1	1 0 0 0 0		1 1 0 0 0 0

Notice that this entry includes a debit to **Accounts Payable** and a credit to **Purchases Returns and Allowances**. In addition, there is a debit to the creditor's account in the accounts payable subsidiary ledger. Businesses that have few returns and allowances use the general journal to record these transactions. Businesses with many returns and allowances use a special journal for purchases returns and allowances.

POSTING A PURCHASES RETURN OR ALLOWANCE

Whether recorded in the general journal or in a special journal, it is important to promptly post returns and allowances to the creditor's account in the accounts payable ledger. Refer to Figure 8.8 to learn how to post purchases returns and allowances to the supplier's account.

1. Enter the date.
2. In the Description column, enter the credit memorandum number.
3. In the Posting Reference column, enter the general journal page number.
4. Enter the amount of the return or allowance in the Debit column.
5. Compute the new balance and enter it in the Balance column.
6. In the general journal, enter a check mark (✓) to show that the transaction was posted to the creditor's account in the accounts payable subsidiary ledger.

After the transaction is posted to the general ledger, enter the **Purchases Returns and Allowances** ledger account number in the Posting Reference column.

>> 8-5. OBJECTIVE

Prepare a schedule of accounts payable.

Schedule of Accounts Payable

The total of the individual creditor accounts in the subsidiary ledger must equal the balance of the **Accounts Payable** control account. To prove that the control account and the subsidiary ledger are equal, businesses prepare a **schedule of accounts payable**—a list of all balances owed to creditors. Figure 8.9 shows the accounts payable subsidiary ledger for Maxx-Out Sporting Goods on January 31.

Figure 8.10 on page 248 shows the schedule of accounts payable for Maxx-Out Sporting Goods. Notice that the accounts payable control account balance is \$20,245. This equals the total on the schedule of accounts payable. If the amounts are not equal, it is essential to locate and correct the errors.

FIGURE 8.9

The Accounts Payable Ledger

NAME Active Designs TERMS 2/10, n/30
 ADDRESS 2313 Belt Line Road, Dallas, Texas 75267-6205

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE
2016					
Jan. 1	Balance	✓			2 2 0 0 00
3	Invoice 5879, 01/02/16	P1		2 8 6 5 00	5 0 6 5 00
13		CP1	3 2 0 0 00		1 8 6 5 00
30		CP1	8 0 0 0 00		1 0 6 5 00

NAME Athletic Equipment, Inc. TERMS 2/10, n/30
 ADDRESS 1027 St James Avenue, Dallas, Texas 75267-6205

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE
2016					
Jan. 19	Invoice 8997, 01/15/16	P1		4 2 0 0 00	4 2 0 0 00

NAME International Sportsman TERMS n/30
 ADDRESS 1718 Sherry Lane, Dallas, Texas 75267-6205

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE
2016					
Jan. 1	Balance	✓			1 6 0 0 00
23	Invoice 7985, 01/23/16	P1		6 0 0 0 00	2 2 0 0 00
27		CP1	1 0 0 0 00		1 2 0 0 00
30	CM 103	J1	1 0 0 0 00		1 1 0 0 00

NAME The Modern Sportsman TERMS n/30
 ADDRESS 2860 Jackson Drive, Dallas, Texas 75267-6205

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE
2016					
Jan. 1	Balance	✓			1 6 0 0 00
6	Invoice 8011, 01/04/16	P1		3 1 4 0 00	4 7 4 0 00

NAME The Sports Warehouse TERMS n/30
 ADDRESS 1313 Sunset Drive, Dallas, Texas 75267-6205

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE
2016					
Jan. 1	Balance	✓			2 4 0 0 00
5	Invoice 633, 01/03/16	P1		4 0 5 5 00	6 4 5 5 00
17		CP1	4 2 5 0 00		2 2 0 5 00

NAME World of Sports TERMS 2/10, n/30
 ADDRESS 1729 Parker Road, Dallas, Texas 75267-6205

DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE
2016					
Jan. 1	Balance	✓			3 0 0 0 00
7	Invoice 4321, 01/04/16	P1		3 9 3 5 00	6 9 3 5 00

FIGURE 8.10

Schedule of Accounts Payable and the Accounts Payable Account

Maxx-Out Sporting Goods	
Schedule of Accounts Payable	
January 31, 2016	
Active Designs	1 0 6 5 00
Athletic Equipment, Inc.	4 2 0 0 00
International Sportsman	1 1 0 0 00
The Modern Sportsman	4 7 4 0 00
The Sports Warehouse	2 2 0 5 00
World of Sports	6 9 3 5 00
Total	2 0 2 4 5 00

ACCOUNT <i>Accounts Payable</i>				ACCOUNT NO. <i>205</i>			
DATE	DESCRIPTION	POST. REF.	DEBIT	CREDIT	BALANCE		
					DEBIT	CREDIT	
2016							
Jan. 1	Balance					10 8 0 0 00	
30		J1	1 0 0 00			10 7 0 0 00	
31		P1		18 7 9 5 00		29 4 9 5 00	
31		CP1	9 2 5 0 00			20 2 4 5 00	

>> 8-6. OBJECTIVE

Compute the net delivered cost of purchases.

Determining the Cost of Purchases

The **Purchases** account accumulates the cost of merchandise bought for resale. The income statement of a merchandising business contains a section showing the total cost of purchases. This section combines information about the cost of the purchases, freight in, and purchases returns and allowances for the period. Maxx-Out Sporting Goods has the following general ledger account balances at January 31:

Purchases	\$17,540
Freight In	1,255
Purchases Returns and Allowances	100

The net delivered cost of purchases for Maxx-Out Sporting Goods for January is calculated as follows:

Purchases	\$17,540
Freight In	<u>1,255</u>
Delivered Cost of Purchases	\$18,795
Less Purchases Returns and Allowances	<u>100</u>
Net Delivered Cost of Purchases	<u>\$18,695</u>

For firms that do not have freight charges, the amount of net purchases is calculated as follows:

Purchases	\$17,540
Less Purchases Returns and Allowances	<u>100</u>
Net Purchases	<u>\$17,440</u>

In Chapter 13, you will see how the complete income statement for a merchandising business is prepared. You will learn about the Cost of Goods Sold section and how the net delivered cost of purchases is used in calculating the results of operations.

Internal Control of Purchases

Internal controls are the company's policies and procedures in place to safeguard assets, ensure reliability of accounting data, and promote compliance with management policies and applicable laws. Because of the large amount of money spent to purchase goods, businesses should develop careful procedures to control purchases and payments. A business should ensure its control process includes sufficient safeguards to:

- create written proof that purchases and payments are authorized;
- ensure that different people are involved in the process of buying goods, receiving goods, and making payments.

Separating duties among employees provides a system of checks and balances. In a small business with just a few employees, it might be very difficult to separate duties. This means the owner must be involved in daily operations. Even a small business, however, should design a set of control procedures as effective as resources allow. Effective systems for small businesses should have the following controls in place:

1. All purchases should be made only after proper authorization has been given in writing.
2. Goods should be carefully checked when received. They should then be compared with the purchase order and with the invoice received from the supplier.
3. The purchase order, receiving report, and invoice should be checked to confirm that the information on the documents is in agreement.
4. The computations on the invoice should be checked for accuracy.
5. Authorization for payment should be made by someone other than the person who ordered the goods.
6. Another person should write the check for payment.
7. Prenumbered forms should be used for purchase requisitions, purchase orders, and checks. The numbers on the documents issued should be verified periodically to make sure all forms can be accounted for.

Medium- and large-sized businesses often use the voucher system. As a business grows, the owner finds it increasingly difficult to be involved in all the firm's transactions. The owner cannot personally approve or sign all checks. That's when the internal controls provided by the voucher system become increasingly important.

Controls built into a voucher system include the following:

- All liabilities are authorized. For example, a properly approved purchase order is required for each purchase of merchandise on account.
- All payments are made by check.
- All checks are issued based on a properly approved voucher.
- Vouchers are used to cover bills and invoices received from outside parties.
- All bills and invoices are verified before they are approved for payment.
- Only experienced and responsible employees are allowed to approve bills and invoices for payment.
- Invoices are attached to the vouchers to provide supporting documentation.
- Different employees approve the vouchers, record the vouchers and payments, and sign and mail the checks.
- All paid vouchers, including supporting documentation, are kept on file for a specified period of time.

>> 8-7. OBJECTIVE

Demonstrate a knowledge of the procedures for effective internal control of purchases.



ABOUT ACCOUNTING

Employee Fraud

According to the U.S. Chamber of Commerce, businesses lose billions of dollars each year to employee fraud. The best defense against fraud is to use good internal controls: Have multiple employees in contact with suppliers and screen employees and vendors to reduce fraud opportunities.

>> 8-8. OBJECTIVE

Record purchases, sales, and returns using the perpetual inventory system.

The Perpetual Inventory System

The accounting for sales and purchases discussed in Chapter 7 and so far in Chapter 8 has assumed use of the **periodic inventory system**. When the periodic system is used, the inventory records are only updated when a physical inventory is taken. A physical inventory is an actual count of units on hand. This system is adequate for smaller businesses.

Larger businesses require up-to-date information of inventories on hand, and use the **perpetual inventory system**. The perpetual inventory system updates both the general ledger merchandise inventory account and inventory items in the inventory ledger with each purchase, sale, and return. Using a perpetual inventory system requires a substantial investment in point-of-sale cash registers, scanning devices, and computer software.

Perpetual inventory management systems give management more control over the company's inventory. Management can use computers to access inventory records to know exactly how much of each item in inventory is on hand. This assists management in inventory control and purchasing activities. The perpetual inventory system also allows for cycle counts of inventory. A cycle count is an inventory management procedure in which only certain inventory items are counted and compared with the perpetual inventory records. Shortages of inventory on hand can be investigated and corrective actions taken.

When the perpetual inventory system is used, an account called *Merchandise Inventory* replaces the *Purchases*, *Purchases Returns*, and *Freight In* accounts used in the periodic inventory system. Merchandise Inventory is an asset account whose balance represents the cost of merchandise inventory on hand.

Additionally, perpetual inventory accounting requires a second entry when sales are made. This entry debits the *Cost of Goods Sold* account and credits the *Merchandise Inventory* account. The *Cost of Goods Sold* account shows the actual cost of the merchandise sold to customers, and is classified as an expense in a perpetual inventory system. If a sales return is processed, an additional entry to debit *Merchandise Inventory* and credit *Cost of Goods Sold* is made.

Figure 8.11 presents the general journal entries for the purchase, sales, and return transactions in Chapters 7 and 8 using both the periodic system and the perpetual system.

FIGURE 8.11

Journal Entries Using Both the Periodic and Perpetual Inventory Systems

Journal Entry to Record Transaction, Using the:					
Transaction	Periodic System			Perpetual System	
June 20: Purchased merchandise inventory for \$2,050 plus freight of \$120 from Holtz Industries, Invoice 5027; the terms are 2/10, n/30.	Purchases	2,050		Merchandise Inventory	2,170
	Freight In	120		Accounts Payable/Holtz Industries	
	Accounts Payable/Holtz Industries		2,170		2,170
June 22: Received Credit Memorandum 110 for \$150 from Holtz Industries for defective product returned; they were originally purchased on Invoice 5027, dated June 20.	Accounts Payable/Holtz Industries	150		Accounts Payable/Holtz Industries	150
	Purchases Returns and Allowances		150	Merchandise Inventory	150
July 1: Sold merchandise on credit to Cervantes Company; issued Invoice 109 for \$1,250, terms 2/10, n/30. The cost of the merchandise sold was \$800.	Accounts Receivable/Cervantes Company	1,250		Accounts Receivable/Cervantes Company	1,250
	Sales		1,250	Sales	1,250
				Cost of Goods Sold	800
				Merchandise Inventory	800
July 3: Issued Credit Memorandum 138 for \$50 to Cervantes Company for defective product returned; they were originally purchased Invoice 109, dated July 1. The cost of the merchandise returned was \$32.	Sales Returns and Allowances	50		Sales Returns and Allowances	50
	Accounts Receivable/Cervantes Company		50	Accounts Receivable/Cervantes Company	50
				Merchandise Inventory	32
				Cost of Goods Sold	32

MANAGERIAL IMPLICATIONS <<

ACCOUNTING FOR PURCHASES

- Management and the accounting staff need to work together to make sure that there are good internal controls over purchasing.
- A carefully designed system of checks and balances protects the business against fraud, errors, and excessive investment in merchandise.
- The accounting staff needs to record transactions efficiently so that up-to-date information about creditors is available.
- Using the purchases journal and the accounts payable subsidiary ledger improves efficiency.
- To maintain a good credit reputation with suppliers, it is important to have an accounting system that ensures prompt payment of invoices.

- A well-run accounting system provides management with information about cash: cash required to pay suppliers, short-term loans needed to cover temporary cash shortages, and cash available for short-term investments.
- Separate accounts for recording purchases, freight charges, and purchases returns and allowances make it easy to analyze the elements in the cost of purchases.

THINKING CRITICALLY

As a manager, what internal controls would you put in your accounting system?

Section 2 Self Review

QUESTIONS

1. What is the purpose of the schedule of accounts payable?
2. A firm has a debit balance of \$62,450 in its *Purchases* account and a credit balance of \$2,875 in its *Purchases Returns and Allowances* account. Calculate net purchases for the period.
3. A firm receives an invoice that reflects the price of goods as \$1,375 and the freight charge as \$92. How is this transaction recorded?
4. In the accounts payable ledger, a supplier's account has a beginning balance of \$4,800. A transaction of \$1,600 is posted from the purchases journal. What is the balance of the supplier's account?
 - a. \$3,200 debit
 - b. \$3,200 credit
 - c. \$6,400 debit
 - d. \$6,400 credit

EXERCISES

4. The net delivered cost of purchases for the period appears on the:
 - a. balance sheet

ANALYSIS

6. In the general ledger, the *Accounts Payable* account has a balance of \$15,500. The schedule of accounts payable lists accounts totaling \$20,500. What could cause this error?

(Answers to Section 2 Self Review are on page 268.)

8

Chapter

REVIEW

Chapter Summary

In this chapter, you have learned about the accounting journals and ledgers required for the efficient processing of purchases for a business. Businesses with strong internal controls establish and follow procedures for approving requests for new merchandise, choosing suppliers, placing orders with suppliers, checking goods after they arrive, identifying invoices, and approving payments.

Learning Objectives

8-1 Record purchases of merchandise on credit in a three-column purchases journal.

Purchases and payments on account must be entered in the firm's accounting records promptly and accurately. Most merchandising businesses normally purchase goods on credit. The most efficient system for recording purchases on credit is the use of a special purchases journal. With this type of journal, only one line is needed to enter all the data.

The purchases journal is used only to record the credit purchase of goods for resale. General business expenses are not recorded in the purchases journal.

8-2 Post from the three-column purchases journal to the general ledger accounts.

The use of the three-column purchases journal simplifies the posting process because nothing is posted to the general ledger until the month's end. Then, summary postings are made to the *Purchases*, *Freight In*, and *Accounts Payable* accounts.

8-3 Post credit purchases from the purchases journal to the accounts payable subsidiary ledger.

An accounts payable subsidiary ledger helps a firm keep track of the amounts it owes to creditors. Postings are made to this ledger on a daily basis.

- Each credit purchase is posted from the purchases journal to the accounts payable subsidiary ledger.
- Each payment on account is posted from the cash payments journal to the accounts payable subsidiary ledger.

8-4 Record purchases returns and allowances in the general journal and post them to the accounts payable subsidiary ledger.

Returns and allowances on purchases of goods are credited to an account called *Purchases Returns and*

Allowances. These transactions may be recorded in the general journal or in a special purchases returns and allowances journal. Each return or allowance on a credit purchase is posted to the accounts payable subsidiary ledger.

8-5 Prepare a schedule of accounts payable.

At the month's end, a schedule of accounts payable is prepared. The schedule lists the balances owed to the firm's creditors and proves the accuracy of the subsidiary ledger. The total of the schedule of accounts payable is compared with the balance of the *Accounts Payable* account in the general ledger, which acts as a control account. The two amounts should be equal.

8-6 Compute the net delivered cost of purchases.

The net delivered cost of purchases is computed by adding the cost of purchases and freight in, then subtracting any purchases returns and allowances. Net delivered cost of purchases is reported in the Cost of Goods Sold section of the income statement.

8-7 Demonstrate a knowledge of the procedures for effective internal control of purchases.

Purchases and payments should be properly authorized and processed with appropriate documentation to provide a system of checks and balances. A division of responsibilities within the purchases process ensures strong internal controls.

8-8 Record purchases, sales, and returns using the perpetual inventory system.

Perpetual inventory systems give management more control over the company's inventory, and assist management in inventory control and purchasing activities.

8-9 Define the accounting terms new to this chapter.

Glossary

Accounts payable ledger (p. 243) A subsidiary ledger that contains a separate account for each creditor

Cash discount (p. 240) A discount offered by suppliers for payment received within a specified period of time

Cost of goods sold (p. 238) The actual cost to the business of the merchandise sold to customers

Freight In account (p. 238) An account showing transportation charges for items purchased

Periodic inventory system (p. 250) An inventory system in which the merchandise inventory balance is only updated when a physical inventory is taken

Perpetual inventory system (p. 250) An inventory system in which merchandise inventory is updated for each purchase, sale, and return

Purchase allowance (p. 244) A price reduction from the amount originally billed

Purchase invoice (p. 236) A bill received for goods purchased

Purchase order (p. 236) An order to the supplier of goods specifying items needed, quantity, price, and credit terms

Purchase requisition (p. 236) A list sent to the purchasing department showing the items to be ordered

Purchase return (p. 244) Return of unsatisfactory goods

Purchases account (p. 238) An account used to record cost of goods bought for resale during a period

Purchases discount (p. 240) A cash discount offered to the customer for payment within a specified period

Purchases journal (p. 238) A special journal used to record the purchase of goods on credit

Receiving report (p. 236) A form showing quantity and condition of goods received

Sales discount (p. 240) A cash discount offered by the supplier for payment within a specified period

Sales invoice (p. 236) A supplier's billing document

Schedule of accounts payable (p. 246) A list of all balances owed to creditors

Transportation In account (p. 238) See Freight In account

Comprehensive Self Review

1. What type of account is *Purchases Returns and Allowances*?
2. What is a cash discount and why is it offered?
3. What is the purpose of the *Freight In* account?
4. What is the purpose of a purchase requisition? A purchase order?
5. What is the difference between a receiving report and an invoice?

(Answers to Comprehensive Self Review are on page 268.)

Discussion Questions

1. Why are the invoice date and terms recorded in the purchases journal?
2. What major safeguards should be built into a system of internal control for purchases of goods?
3. What is the purpose of a credit memorandum?
4. What is a purchase allowance?
5. What is a purchase return?
6. What is a schedule of accounts payable? Why is it prepared?
7. What is the relationship of the *Accounts Payable* account in the general ledger to the accounts payable subsidiary ledger?
8. What type of accounts are kept in the accounts payable ledger?
9. Why is it useful for a business to have an accounts payable ledger?
10. How is the net delivered cost of purchases computed?
11. What journals can be used to enter various merchandise purchase transactions?
12. What is the difference between a purchase invoice and a sales invoice?
13. What is the normal balance of the *Purchases* account?

14. On what financial statement do the accounts related to purchases of merchandise appear? In which section of this statement are they reported?
15. Why is the use of a *Purchases Returns and Allowances* account preferred to crediting these transactions to *Purchases*?
16. What do the following credit terms mean?
 - a. n/30
 - b. 2/10, n/30
 - c. n/10 EOM
 - d. n/20
 - e. 1/10, n/20
 - f. 3/5, n/30
 - g. n/15 EOM
17. A business has purchased some new equipment for use in its operations, not for resale to customers. The terms of the invoice are n/30. Should this transaction be entered in the purchases journal? If not, where should it be recorded?
18. What account is debited for the purchase of merchandise inventory when (a) the periodic system is used and (b) the perpetual inventory system is used?
19. What account is credited for the return of merchandise inventory when (a) the periodic system is used and (b) the perpetual inventory system is used?
20. What account is debited for freight charges on merchandise inventory purchases when (a) the periodic system is used and (b) the perpetual inventory system is used?

APPLICATIONS

Exercises connect[™] | ACCOUNTING

Exercise 8.1 Objective 8-1

▶ Identifying the journals used to record purchases and related transactions.

The accounting system of Shoe City includes the following journals. Indicate which journal is used to record each transaction.

JOURNALS

Cash receipts journal
 Cash payments journal
 Purchases journal
 Sales journal
 General journal

TRANSACTIONS

1. Purchased merchandise for \$3,000; the terms are 2/10, n/30.
2. Returned damaged merchandise to a supplier and received a credit memorandum for \$800.
3. Issued a check for \$3,600 to a supplier as a payment on account.
4. Purchased merchandise for \$2,000 plus a freight charge of \$140; the supplier's invoice is payable in 30 days.
5. Received an allowance for merchandise that was damaged but can be sold at a reduced price; the supplier's credit memorandum is for \$475.
6. Purchased merchandise for \$3,500 in cash.

Identifying journals used to record purchases and related transactions.

The following transactions took place at Extreme Bikers. Indicate the general ledger account numbers that would be debited and credited to record each transaction.

GENERAL LEDGER ACCOUNTS

- 101 Cash
- 205 Accounts Payable
- 501 Purchases
- 502 Freight In
- 503 Purchases Returns and Allowances

TRANSACTIONS

1. Purchased merchandise for \$1,500; the terms are 2/10, n/30.
2. Returned damaged merchandise to a supplier and received a credit memorandum for \$300.
3. Issued a check for \$800 to a supplier as a payment on account.
4. Purchased merchandise for \$2,400 plus a freight charge of \$260; the supplier's invoice is payable in 30 days.
5. Received an allowance for merchandise that was damaged but can be sold at a reduced price; the supplier's credit memorandum is for \$400.
6. Purchased merchandise for \$4,200 in cash.

Recording credit purchases.

The following transactions took place at Cerritos Auto Parts and Custom Shop during the first week of July. Indicate how these transactions would be entered in a purchases journal like the one shown in this chapter.

DATE	TRANSACTIONS
July 1	Purchased batteries for \$2,060 plus a freight charge of \$132 from Auto Parts Corporation; received Invoice 6812, dated June 27, which has terms of n/30.
3	Purchased mufflers for \$3,250 plus a freight charge of \$89 from Aplex Company; received Invoice 441, dated June 30, which has terms of 1/10, n/60.
5	Purchased car radios for \$2,470 plus freight of \$127 from The Custom Sounds Shop, Inc.; received Invoice 5601, dated July 1, which has terms of 2/10, n/30.
10	Purchased truck tires for \$4,270 from Specialty Tire Company; received Invoice 1102, dated July 8, which has terms of 2/10, n/30.

Recording a purchase return.

On February 9, Sophisticated Kitchens, a retail store, received Credit Memorandum 244 for \$4,320 from M & J Appliance Corporation. The credit memorandum covered a return of damaged trash compactors originally purchased on Invoice 4101 dated January 3. Prepare the general journal entry that Sophisticated Kitchens would make for this transaction.

Recording a purchase allowance.

On March 17, All-Star Appliances was given an allowance of \$1,175 by Uptown Kitchens, which issued Credit Memorandum 112. The allowance was for scratches on stoves that were originally purchased on Invoice 911 dated February 20. Prepare the general journal entry that All-Star Appliances would make for this transaction.

◀ **Exercise 8.2**
Objective 8-1

◀ **Exercise 8.3**
Objective 8-1

◀ **Exercise 8.4**
Objective 8-4

◀ **Exercise 8.5**
Objective 8-4

Exercise 8.6**Objective 8-4**▶ **Determining the cost of purchases.**

On June 30 the general ledger of Bentleys New York, a clothing store, showed a balance of \$53,495 in the *Purchases* account, a balance of \$2,875 in the *Freight In* account, and a balance of \$5,220 in the *Purchases Returns and Allowances* account. What was the delivered cost of the purchases made during June? What was the net delivered cost of these purchases?

Exercise 8.7**Objectives 8-1, 8-4**▶ **Errors in recording purchase transactions.**

The following errors were made in recording transactions in posting from the purchases journal. How will these errors be detected?

- A credit of \$2,000 to Thomastown Furniture Company account in the accounts payable ledger was posted as \$200.
- The Accounts Payable column total of the purchases journal was understated by \$200.
- An invoice of \$1,680 for merchandise from Johnson Company was recorded as having been received from Baxton Company, another supplier.
- A \$500 payment to Baxton Company was debited to Johnson Company.

Exercise 8.8**Objective 8-4**▶ **Determining the cost of purchases.**

Complete the following schedule by supplying the missing information.

Net Delivered Cost of Purchases	Case A	Case B
Purchases	(a)	95,570
Freight In	4,275	(c)
Delivered Cost of Purchases	97,750	(d)
Less Purchases Returns and Allowances	(b)	3,930
Net Delivered Cost of Purchases	<u>93,825</u>	<u>97,920</u>

Exercise 8.9**Objective 8-8**▶ **Recording transactions using the perpetual inventory system.**

The following transactions took place at Fine Fashions Outlet during July 2016. Fine Fashions Outlet uses a perpetual inventory system. Record the transactions in a general journal. Use 8 as the page number for the general journal. Omit descriptions.

DATE	TRANSACTIONS
July 3	Purchased dresses for \$3,500 plus a freight charge of \$120 from Fashion Expo, Invoice 101, dated July 1; the terms are net 30 days.
5	Sold two dresses on account to Alice Chu, terms net 30 days; issued Sales Slip 788 for \$600. The cost of the dresses sold was \$400.
7	Received Credit Memorandum 210 for \$550 from Fashion Expo for damaged dresses returned; the goods were purchased on Invoice 101 dated July 1.
9	Accepted a return of a dress from Alice Chu; the dress was originally sold on Sales Slip 788 of July 5; issued Credit Memorandum 89 for \$200. The cost of the returned dress was \$135.

PROBLEMS

Problem Set A



Journalizing credit purchases and purchases returns and allowances and posting to the general ledger.

Digital World is a retail store that sells cameras and photography supplies. The firm's credit purchases and purchases returns and allowances transactions for June 2016 appear below, along with the general ledger accounts used to record these transactions. The balance shown in *Accounts Payable* is for the beginning of June.

INSTRUCTIONS

1. Open the general ledger accounts and enter the balance of *Accounts Payable* for June 1, 2016.
2. Record the transactions in a three-column purchases journal and in a general journal. Use 14 as the page number for the purchases journal and 38 as the page number for the general journal.
3. Post entries from the general journal to the general ledger accounts.
4. Total and rule the purchases journal as of June 30.
5. Post the column totals from the purchases journal to the proper general ledger accounts.
6. Compute the net purchases of the firm for the month of June.

GENERAL LEDGER ACCOUNTS

205	Accounts Payable, \$14,404 Cr.
501	Purchases
502	Freight In
503	Purchases Returns and Allowances

DATE	TRANSACTIONS
June 1	Purchased instant cameras for \$2,050 plus a freight charge of \$230 from Pro Photo Equipment, Invoice 4241, dated May 27; the terms are 60 days net.
8	Purchased film for \$1,394 from Photo Supplies, Invoice 1102, dated June 3, net payable in 45 days.
12	Purchased lenses for \$916 from Nano Glass, Invoice 7282, dated June 9; the terms are 1/10, n/60.
18	Received Credit Memorandum 110 for \$400 from Pro Photo Equipment for defective cameras that were returned; they were originally purchased on Invoice 4241, dated May 27.
20	Purchased color film for \$1,200 plus freight of \$75 from Photo Supplies, Invoice 1148, dated June 15, net payable in 45 days.
23	Purchased camera cases for \$1,956 from Hi-Qual Case, Invoice 3108, dated June 18, net due and payable in 45 days.
28	Purchased lens filters for \$2,470 plus freight of \$120 from Holtz Spectrum, Invoice 5027, dated June 24; the terms are 2/10, n/30.
30	Received Credit Memorandum 1108 for \$310 from Hi-Qual Case; the amount is an allowance for damaged but usable goods purchased on Invoice 3108, dated June 18.

(Note: Save your working papers for use in Problem 8.2A.)

Analyze: What total purchases were posted to the *Purchases* general ledger account for June?

◀ **Problem 8.1A**
Objectives 8-1,
8-2, 8-3

Sage 50
Complete Accounting



Problem 8.2A

Objectives 8-4, 8-6

CONTINUING >>>
Problem**Posting to the accounts payable ledger and preparing a schedule of accounts payable.**

This problem is a continuation of Problem 8.1A.

INSTRUCTIONS

1. Set up an accounts payable subsidiary ledger for Digital World. Open an account for each of the creditors listed below and enter the balances as of June 1, 2016. Arrange the accounts payable ledger in alphabetical order.
2. Post the individual entries from the purchases journal and the general journal prepared in Problem 8.1A.
3. Prepare a schedule of accounts payable for June 30.
4. Check the total of the schedule of accounts payable against the balance of the *Accounts Payable* account in the general ledger. The two amounts should be equal.

Creditors		
Name	Terms	Balance
Photo Supplies	n/45	\$10,580
Hi-Qual Case	n/45	1,300
Pro Photo Equipment	n/60	
Nano Glass	1/10, n/60	2,524
Holtz Spectrum	2/10, n/30	

Analyze: What amount is owed to Nano Glass on June 30?

Problem 8.3AObjectives 8-1, 8-2,
8-3, 8-4, 8-5, 8-6Sage 50
Complete Accounting**Journalizing credit purchases and purchases returns and allowances, computing the net delivered cost of goods, posting to the general ledger, posting to the accounts payable ledger, and preparing a schedule of accounts payable.**

The English Garden Shop is a retail store that sells garden equipment, furniture, and supplies. Its credit purchases and purchases returns and allowances for July are listed on the next page. The general ledger accounts used to record these transactions are also provided. The balance shown is for the beginning of July 2016.

INSTRUCTIONS**PART I**

1. Open the general ledger accounts and enter the balance of *Accounts Payable* for July 1.
2. Record the transactions in a three-column purchases journal and in a general journal. Use 8 as the page number for the purchases journal and 20 as the page number for the general journal.
3. Post the entries from the general journal to the proper general ledger accounts.
4. Total, prove, and rule the purchases journal as of July 31.
5. Post the column totals from the purchases journal to the proper general ledger accounts.
6. Compute the net delivered cost of the firm's purchases for the month of July.

GENERAL LEDGER ACCOUNTS

205	Accounts Payable, \$35,980 Cr.	502	Freight In
501	Purchases	503	Purchases Returns and Allowances

DATE	TRANSACTIONS
July 1	Purchased lawn mowers for \$9,310 plus a freight charge of \$259 from Brown Corporation, Invoice 1011, dated June 26, net due and payable in 60 days.
5	Purchased outdoor chairs and tables for \$4,470 plus a freight charge of \$562 from Brooks Garden Furniture Company, Invoice 639, dated July 2, net due and payable in 45 days.
9	Purchased grass seed for \$1,590 from Lawn and Gardens Supply, Invoice 8164, dated July 5; the terms are 30 days net.
16	Received Credit Memorandum 110 for \$700 from Brooks Garden Furniture Company; the amount is an allowance for scratches on some of the chairs and tables originally purchased on Invoice 639, dated July 2.
19	Purchased fertilizer for \$1,300 plus a freight charge of \$266 from Lawn and Gardens Supply, Invoice 9050, dated July 15; the terms are 30 days net.
21	Purchased hoses from Cameron Rubber Company for \$3,780 plus a freight charge of \$234, Invoice 1785, dated July 17; terms are 1/15, n/60.
28	Received Credit Memorandum 223 for \$530 from Cameron Rubber Company for damaged hoses that were returned; the goods were purchased on Invoice 1785, dated July 17.
31	Purchased lawn sprinkler systems for \$10,410 plus a freight charge of \$288 from Wilson Industrial Products, Invoice 8985, dated July 26; the terms are 2/10, n/30.

INSTRUCTIONS

PART II

- Set up an accounts payable subsidiary ledger for The English Garden Shop. Open an account for each of the creditors listed below and enter the balances as of July 1.
- Post the individual entries from the purchases journal and the general journal prepared in Part I.
- Prepare a schedule of accounts payable for July 31, 2016.
- Check the total of the schedule of accounts payable against the balance of the *Accounts Payable* account in the general ledger. The two amounts should be equal.

Creditors		
Name	Terms	Balance
Brooks Garden Furniture Company	n/45	\$11,220
Brown Corporation	n/60	18,220
Cameron Rubber Company	1/15, n/60	
Lawn and Gardens Supply	n/30	6,540
Wilson Industrial Products	2/10, n/30	

Analyze: What total freight charges were posted to the general ledger for the month of July?

Journalizing credit purchases and purchases returns and allowances, posting to the general ledger, posting to the accounts payable ledger, and preparing a schedule of accounts payable.

Office Plus is a retail business that sells office equipment, furniture, and supplies. Its credit purchases and purchases returns and allowances for September are shown on the next page. The general ledger accounts and the creditors' accounts in the accounts payable subsidiary ledger used to record these transactions are also provided. All balances shown are for the beginning of September.

◀ **Problem 8.4A**
Objectives 8-1, 8-2,
8-3, 8-4, 8-5, 8-6

Sage 50
Complete Accounting



INSTRUCTIONS

1. Open the general ledger accounts and enter the balance of *Accounts Payable* for September 1, 2016.
2. Open the creditors' accounts in the accounts payable subsidiary ledger and enter the balances for September 1.
3. Record the transactions in a three-column purchases journal and in a general journal. Use 5 as the page number for the purchases journal and 14 as the page number for the general journal.
4. Post to the accounts payable subsidiary ledger daily.
5. Post the entries from the general journal to the proper general ledger accounts at the end of the month.
6. Total and rule the purchases journal as of September 30.
7. Post the column totals from the purchases journal to the proper general ledger accounts.
8. Prepare a schedule of accounts payable and compare the balance of the *Accounts Payable* control account with the schedule of accounts payable.

GENERAL LEDGER ACCOUNTS

205	Accounts Payable, \$28,356 Cr.	502	Freight In
501	Purchases	503	Purchases Returns and Allowances

Creditors		
Name	Terms	Balance
Apex Office Machines, Inc.	n/60	\$11,060
Brown Paper Company	1/10, n/30	2,220
Dalton Office Furniture Company	n/30	9,676
Davis Corporation	n/30	
Zenn Furniture, Inc.	2/10, n/30	5,400

DATE	TRANSACTIONS
Sept. 3	Purchased desks for \$8,020 plus a freight charge of \$222 from Dalton Office Furniture Company, Invoice 4213, dated August 29; the terms are 30 days net.
7	Purchased computers for \$12,300 from Apex Office Machines, Inc., Invoice 9217, dated September 2, net due and payable in 60 days.
10	Received Credit Memorandum 511 for \$700 from Dalton Office Furniture Company; the amount is an allowance for damaged but usable desks purchased on Invoice 4213, dated August 29.
16	Purchased file cabinets for \$2,656 plus a freight charge of \$134 from Davis Corporation, Invoice 8066, dated September 11; the terms are 30 days net.
20	Purchased electronic desk calculators for \$1,100 from Apex Office Machines, Inc., Invoice 11011, dated September 15, net due and payable in 60 days.
23	Purchased bond paper and copy machine paper for \$8,500 plus a freight charge of \$100 from Brown Paper Company, Invoice 6498, dated September 18; the terms are 1/10, n/30.
28	Received Credit Memorandum 312 for \$980 from Apex Office Machines, Inc., for defective calculators that were returned; the calculators were originally purchased on Invoice 11011, dated September 15.
30	Purchased office chairs for \$3,940 plus a freight charge of \$170 from Zenn Furniture, Inc., Invoice 696, dated September 25, the terms are 2/10, n/30.

Analyze: What total amount was recorded for purchases returns and allowances in the month of September? What percentage of total purchases does this represent?

Problem Set B

Journalizing credit purchases and purchases returns and allowances and posting to the general ledger.

◀ Problem 8.1B

Objectives 8-1, 8-2, 8-3

Mountain Ski Shop is a retail store that sells ski equipment and clothing. The firm's credit purchases and purchases returns and allowances during May 2016 follow, along with the general ledger accounts used to record these transactions. The balance shown in *Accounts Payable* is for the beginning of May.

INSTRUCTIONS

1. Open the general ledger accounts and enter the balance of *Accounts Payable* for May 1, 2016.
2. Record the transactions in a three-column purchases journal and in a general journal. Use 15 as the page number for the purchases journal and 38 as the page number for the general journal.
3. Post the entries from the general journal to the proper general ledger accounts.
4. Total and rule the purchases journal as of May 31.
5. Post the column totals from the purchases journal to the proper general ledger accounts.
6. Compute the net purchases of the firm for the month of May.

GENERAL LEDGER ACCOUNTS

205	Accounts Payable, \$21,608 Cr.
501	Purchases
502	Freight In
503	Purchases Returns and Allowances

DATE	TRANSACTIONS
May 1	Purchased ski boots for \$6,600 plus a freight charge of \$120 from East Coast Snow Shop, Invoice 6572, dated April 28; the terms are 45 days net.
8	Purchased skis for \$12,500 from May-Day Ski Shop, Invoice 4916, dated May 2; the terms are net payable in 30 days.
9	Received Credit Memorandum 155 for \$1,050 from East Coast Snow Shop for damaged ski boots that were returned; the boots were originally purchased on Invoice 6572, dated April 28.
12	Purchased ski jackets for \$5,200 from Fashion Ski Wear, Invoice 986, dated May 11, net due and payable in 60 days.
16	Purchased ski poles for \$2,650 from May-Day Ski Shop, Invoice 5011, dated May 15; the terms are n/30.
22	Purchased ski pants for \$3,160 from Winter Sports Clothing, Invoice 4019, dated May 16; the terms are 1/10, n/60.
28	Received Credit Memorandum 38 for \$480 from May-Day Ski Shop for defective ski poles that were returned; the items were originally purchased on Invoice 5011, dated May 15.
31	Purchased sweaters for \$3,630 plus a freight charge of \$220 from Golden Skis & Clothing, Invoice 8354, dated May 27; the terms are 2/10, n/30.

(Note: Save your working papers for use in Problem 8.2B.)

Analyze: What total accounts payable were posted from the purchases journal to the general ledger for the month?

Problem 8.2B

Objectives 8-4, 8-6

CONTINUING >>>
Problem**Posting to the accounts payable ledger and preparing a schedule of accounts payable.**

This problem is a continuation of Problem 8.1B.

INSTRUCTIONS

1. Set up an accounts payable subsidiary ledger for Mountain Ski Shop. Open an account for each of the creditors listed below and enter the balances as of May 1, 2016. Arrange the accounts payable ledger in alphabetical order.
2. Post the individual entries from the purchases journal and the general journal prepared in Problem 8.1B.
3. Prepare a schedule of accounts payable for May 31.
4. Check the total of the schedule of accounts payable against the balance of the *Accounts Payable* account in the general ledger. The two amounts should be equal.

Creditors		
Name	Terms	Balance
May-Day Ski Shop	n/30	\$1,700
Fashion Ski Wear	n/60	8,720
Winter Sports Clothing	1/10, n/60	5,000
East Coast Snow Shop	n/45	6,188
Golden Skis & Clothing	2/10, n/30	

Analyze: What amount did Mountain Ski Shop owe to its supplier, East Coast Snow Shop, on May 31?

Problem 8.3BObjectives 8-1, 8-2,
8-3, 8-4, 8-5, 8-6**Journalizing credit purchases and purchases returns and allowances, computing the net delivered cost of goods, posting to the general ledger, posting to the accounts payable ledger, and preparing a schedule of accounts payable.**

The Landscape Supply Center is a retail store that sells garden equipment, furniture, and supplies. Its credit purchases and purchases returns and allowances for December are shown below. The general ledger accounts used to record these transactions are also provided. The balance shown is for the beginning of December 2016.

INSTRUCTIONS**PART I**

1. Open the general ledger accounts and enter the balance of *Accounts Payable* for December 1.
2. Record the transactions in a three-column purchases journal and in a general journal. Use 8 as the page number for the purchases journal and 20 as the page number for the general journal.
3. Post the entries from the general journal to the proper general ledger accounts.
4. Total, prove, and rule the purchases journal as of December 31.
5. Post the column totals from the purchases journal to the proper general ledger accounts.
6. Compute the net delivered cost of the firm's purchases for the month of December.

GENERAL LEDGER ACCOUNTS

205	Accounts Payable, \$13,490 Cr.
501	Purchases
502	Freight In
503	Purchases Returns and Allowances

DATE	TRANSACTIONS
Dec. 1	Purchased lawn mowers for \$5,780 plus a freight charge of \$156 from Selby Corporation, Invoice 2110, dated November 26, net due and payable in 45 days.
5	Purchased outdoor chairs and tables for \$5,700 plus a freight charge of \$100 from Patio Furniture Shop, Invoice 633, dated December 2; the terms are 1/15, n/60.
9	Purchased grass seed for \$1,148 from Spring Lawn Center, Invoice 1127, dated December 4; the terms are 30 days net.
16	Received Credit Memorandum 101 for \$400 from Patio Furniture Shop; the amount is an allowance for scratches on some of the chairs and tables originally purchased on Invoice 633, dated December 2.
19	Purchased fertilizer for \$1,600 plus a freight charge of \$156 from Spring Lawn Center, Invoice 1131, dated December 15; the terms are 30 days net.
21	Purchased garden hoses for \$760 plus a freight charge of \$76 from Delta Rubber Company, Invoice 8517, dated December 17; the terms are n/60.
28	Received Credit Memorandum 210 for \$150 from Delta Rubber Company for damaged hoses that were returned; the goods were purchased on Invoice 8517, dated December 17.
31	Purchased lawn sprinkler systems for \$3,700 plus a freight charge of \$80 from Cason Industries, Invoice 8819, dated December 26; the terms are 2/10, n/30.

INSTRUCTIONS

PART II

- Set up an accounts payable subsidiary ledger for The Landscape Supply Center. Open an account for each of the following creditors and enter the balances as of December 1.
- Post the individual entries from the purchases journal and the general journal prepared in Part I.
- Prepare a schedule of accounts payable for December 31.
- Check the total of the schedule of accounts payable against the balance of the *Accounts Payable* account in the general ledger. The two amounts should be equal.

Creditors		
Name	Terms	Balance
Cason Industries	2/10, n/30	\$2,150
Delta Rubber Company	n/60	3,850
Patio Furniture Shop	1/15, n/60	
Selby Corporation	n/45	4,842
Spring Lawn Center	n/30	2,648

Analyze: By what amount did Accounts Payable increase during the month of December?

Journalizing credit purchases and purchases returns and allowances, posting to the general ledger, posting to the accounts payable ledger, and preparing a schedule of accounts payable.

Simpson's Card and Novelty Shop is a retail card, novelty, and business supply store. Its credit purchases and purchases returns and allowances for February 2016 appear on the next page. The general ledger accounts and the creditors' accounts in the accounts payable subsidiary ledger used to record these transactions are also provided. The balance shown is for the beginning of February.

◀ **Problem 8.4B**
Objectives 8-1, 8-2,
8-3, 8-4, 8-5, 8-6

INSTRUCTIONS

1. Open the general ledger accounts and enter the balance of *Accounts Payable* for February.
2. Open the creditors' accounts in the accounts payable subsidiary ledger and enter the balances for February 1, 2016.
3. Record each transaction in the appropriate journal, purchases or general. Use page 4 in the purchases journal and page 12 in the general journal.
4. Post entries to the accounts payable subsidiary ledger daily.
5. Post entries in the general journal to the proper general ledger accounts at the end of the month.
6. Total and rule the purchases journal as of February 29.
7. Post the totals to the appropriate general ledger accounts.
8. Calculate the net delivered cost of purchases.
9. Prepare a schedule of accounts payable and compare the balance of the *Accounts Payable* control account with the schedule of accounts payable.

GENERAL LEDGER ACCOUNTS

203	Accounts Payable, \$15,200 credit balance
501	Purchases
502	Freight In
503	Purchases Returns and Allowances

Creditors		
Name	Terms	Balance
Business Forms, Inc.	n/30	\$8,000
Gifts and Holiday Cards	2/10, n/30	4,000
Packing and Mailing Supply Center	2/10, n/30	3,200
Specialty Business Cards	1/10, n/45	

DATE	TRANSACTIONS
Feb. 5	Purchased copy paper from Packing and Mailing Supply Center for \$2,000 plus \$100 shipping charges on Invoice 502, dated February 2.
8	Purchased assorted holiday cards from Gifts and Holiday Cards on Invoice 2808, \$1,900, dated February 5.
12	Purchased five boxes of novelty items from Gifts and Holiday Cards for a total cost of \$1,200, Invoice 2904, dated February 8.
13	Purchased tray of cards from Specialty Business Cards on Invoice 2013 for \$1,100, dated February 9.
19	Purchased supply of forms from Business Forms, Inc., for \$1,980 plus shipping charges of \$60 on Invoice 2019, dated February 16.
20	One box of cards purchased on February 8 from Gifts and Holiday Cards was water damaged. Received Credit Memorandum 102 for \$200.
21	Toner supplies are purchased from Specialty Business Cards for \$3,600 plus shipping charges of \$110, Invoice 1376, dated February 19.
27	Received Credit Memorandum 118 for \$240 from Gifts and Holiday Cards as an allowance for damaged novelty items purchased on February 12.