

Accounting 252
QuickBooks Instructor Notes
Chapter 6—Sales and Receivables—Merchandising Business (10/12/16)

1. Comparison with service business (Chapter 2)

A. Merchandising businesses differ from service businesses because they stock merchandise inventory. Their business cycle is longer.

- (1) Most things merchandising businesses sell are those that are kept in stock until sold.



Merchandise Inventory is an Asset. Appears on the Balance Sheet.

When sold, the cost of the Merchandise Inventory sold goes to Cost of Goods Sold (COGS). Subtracted from Net Sales on the Income Statement to yield Gross Profit.

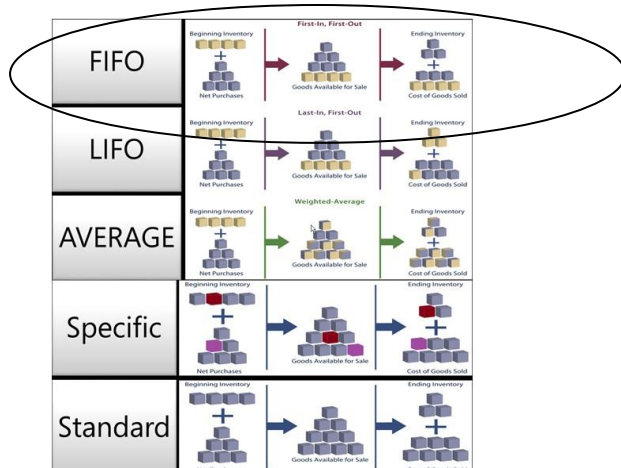
<https://www.koofers.com/flashcards/actg-chapter-5/review>

- (1) Other revenue sources for a merchandising business may not involve Merchandise Inventory.

If not, then costs of generating those revenues may not be very well coordinated or “matched” with the revenue. They may even be recorded in a different accounting period, unless special manual procedures are performed.

B. QuickBooks uses a FIFO inventory system

When an item of inventory is sold, Merchandise Inventory is automatically reduced, and the costs of the oldest inventory item on hand automatically go to Cost of Goods Sold. That means the newest inventory item costs are what make up ending inventory.



[https://msdn.microsoft.com/en-us/library/hh997373\(v=nav.90\).aspx](https://msdn.microsoft.com/en-us/library/hh997373(v=nav.90).aspx)

C. Sales may be for cash, or on account.

When Merchandise Inventory is sold, there are a minimum of four (4) accounts in the Journal Entry. Five (5) when Sales Tax is recorded using the Sales Tax function in QB.

(1) Sales Receipt

Cash, check, or credit card is a “cash sale”

Generic Account titles	Debit	Credit
Undeposited Funds	Selling price + Sales Tax	
Cost of Goods Sold	Our FIFO cost	
Sales		Selling price
Merchandise Inventory		Our FIFO cost
SalesTax Payable		Sales Tax

(2) Sales Invoice

Is a “sale on account”

Generic Account titles	Debit	Credit
Accounts Receivable – Customer name	Selling price + Sales Tax	
Cost of Goods Sold	Our FIFO cost	
Sales		Selling price
Merchandise Inventory		Our FIFO cost
SalesTax Payable		Sales Tax

2. Integration has to occur among QB “centers” and with General Ledger (G/L) accounts for a merchandising business

A. The different “centers” in QB communicate with each other.

Customer center, Vendor center, and (in the background) the inventory-related functions (Items, have to communicate automatically with each other. They have to know what G/L accounts to post transaction amounts to.

In larger Accounting Information Systems (AIS), these are called “Modules” of the accounting program. All of them working together is called “Integration.” How transactions from the different modules are related to G/L accounts may be specified in a “G/L Interface table.”

3. QuickBooks “Items” are the key to coordinating between all the centers and General Ledger accounts involved.

A. Per QB’s Help menu, an “Item” is:

- (1)** “...anything that your company buys, sells, or resells in the course of business, such as products, shipping and handling charges, discounts, and sales tax (if applicable). You can think of an item as something that shows up as a line on an invoice or other sales form.”

B. Items can involve from zero to several G/L accounts

- (1) A "Subtotal" Item has no value by itself, so no G/L accounts are associated with it.
- (2) The Item used for a sale of merchandise would use four G/L accounts (plus a separate Item and G/L account for sales tax), as listed in journal entries above.
- (3) The sale of an Item "Bundle" could involve multiple Inventory Asset, multiple Sales and multiple Cost of Goods Sold G/L accounts.

4. Various Item types are available:

A. A typical Item type, for the sale of merchandise inventory, matches the item's cost with its related revenue.

Each of these has links to an Inventory Asset, Sales, Cost of Goods Sold, and Sales Taxes G/L accounts.

- Inventory – Usually a single item sold by itself.
- Bundle – Usually a "kit" or collection of several existing Inventory Part Items that are often sold together. e.g. simply grouping them together in a package.

B. Some Item types for sales do not directly match costs to revenue.

This type goes directly to an expense or fixed asset account (NOT merchandise inventory) when purchased. When sold, it only shows up as Revenue – No Cost of Goods Sold (COGS).

- Non-Inventory Parts

This type has no directly related costs at any time. It is usually matched only with Operating Expenses for the period. When a sale is made, it only shows up as Revenue.

- Services

If you change a Services to an Inventory item, you can never change it back to Services. You would have to create a new Services item in order to restore it.

C. Additional information on Item types:

<https://community.intuit.com/articles/1145670-inventory-overview-and-setup>

5. Problem areas in A/R for merchandising companies

A. Items list can get messy

- (1) New Items may be added to the Item List "on the fly".

This opens the possibility for accidentally duplicating Items already on the list. Be sure to go through the Item List entirely before adding a

new Item.

Consider Group and Assembly if what you want to add includes several existing Items.

B. Discounts applied only to immediately preceding line

- (1) To apply to the whole invoice or several Items, Subtotal Item is required.

Discount must immediately follow. You need to plan out the order of items on the invoice.

C. Discount Items on the invoice are NOT the same as Sales Discounts (or Cash Discounts, or Early Payment Discounts).

- (1) Discount Item on the invoice body:

This is an Item known as Trade Discount or Quantity Discount.

This discount theoretically should just reduce the invoice amount, reduce the debit to A/R, and reduce the credit to the Sales G/L accounts at the time the invoice is created.

- (2) Discount recorded when payment received is called a Sales Discount or Cash Discount. Sales Discounts is a Contra Revenue account reserved for prompt payment based discounts. Recording it is a two-step process:

- a. Modify the invoice to show the discount. Make sure the discount appears BEFORE sales tax, or the wrong amount of tax will be computed.
- b. Click Receive Payment button from within the invoice, via the Plus sign, or in the Customer Center. Make sure the payment amount agrees with the invoice amount.
- c. Accounting impact

In most other accounting systems, the discount would be recorded along with the cash receipt at the time of collection, and the invoice total would be unaffected by the discount. But not in QBO.

Generic Account titles	Debit	Credit
<i>Undeposited Funds</i>	Selling price - Discount	
Accounts Receivable – Customer name		Same as Cash

In QBO, the only reason why this JE works, is because the Invoice total has already been manually reduced by the accountant.

Hopefully, QBO will change this procedure. It is very non-standard, and extremely clunky.

6. Credits, Refunds and NSF's

A. Credit Memos

- (1) Click the Refunds & Credits icon to prepare a Credit Memo

a. Accounting impact

The credit memo reverses the original sale. Most businesses would prefer to isolate these instances into a Sales Return account so they can make sure it doesn't get out of hand, but that option is impractical in QBO.

Generic Account titles	Debit	Credit
Sales	Selling price	
Merchandise Inventory	Our FIFO cost	
Sales Tax Payable	Sales Tax	
Accounts Receivable – Customer name		Selling price + Sales Tax
Cost of Goods Sold		Our FIFO cost

- b. Must eventually be “applied” to make the related Accounts Receivable invoice balance “clear”. This can be applied immediately upon creating credit memo, by issuing a refund, or by applying later.

B. Refunds

- (1) Click the Refunds & Credits icon to prepare a Credit Memo. Click “Use credit to give refund” button.

a. Accounting impact

Same JE as Credit Memo, except A/R replaced by Cash.

C. Non Sufficient Funds (NSF) check

- (1) In order to match transactions appearing on bank statement, the best approach is to create an NSF item. The original deposit of the check (before it was dishonored) will match our books. We need to create a new substitute Invoice to apply that Payment to that will allow you to turn the original Invoice back into unpaid status.

Since the deposit containing the bad check has already been made, you need to temporarily remove the invoice payment you recorded from the deposit in the Deposit window.

Then, you must un-apply the Payment from the original Invoice.

Then, you must create your Bad Check item charge as an Invoice, and apply the original payment to this new invoice.

As a result, the original Invoice will now be in unpaid status, showing from all the way back in time when it was first created.

- (2) Accounting impact of NSF itself, “NSF Check” Item.

Once you have a bad check, you now have to chase down the customer to really receive your payment.

Generic Account titles	Debit	Credit
Accounts Receivable – Customer name	X	
Checking		X

- (3) We must also pass through to the customer the debit for the dishonored check the bank will make to our account. And most businesses will also charge the customer a separate fee for the inconvenience of dealing with the NSF check. Any amount we charge the customer as a pass-through of bank charge and as a company service charge should go to revenue.

- a. Accounting impact of service charge to customer, “NSF Charges” Item.

This means the customer owes us the amount of the bad check AND the bad check fee we are now assessing.

Generic Account titles	Debit	Credit
Accounts Receivable – Customer name	X	
Fees Billed (Bank Special Handling fee + Our company’s NSF handling fee)		X

7. Advanced topics

A. QB’s Sales Tax function does not match the way Hawaii General Excise Tax (GET) works.

- (1) In QB, the Sales Tax is computed on the sale amount, not the total amount collected.

This will result in underreported income for GET purposes. For GET purposes, the total amount collected (including the GET) must be reported as GET Taxable. The GET is then computed at 4.5% (depending on County) on the gross amount. This is why some businesses charge 4.71%. They are collecting the tax on the tax.

- (2) Two common possible approaches to fixing the underreported income:

- a. Collect the tax on the tax. Add tax collected to Revenue.

Charge GET at 4.71% using QB’s built-in Sales Tax function. When calculating GET Taxable income, add net credits less debits in the Sales Tax Payable account to regular Revenue. The Sales Tax

Payable was recorded when the invoice was made. This approach has no Income Statement effect.

- b. Create a revenue Item called General Excise Tax and use it on Invoices and Sales Receipts instead of QB's built-in Sales Tax function

Subtotal invoices before charging GET. Charge GET as a Revenue Item on the invoice at either 4.71% or 4.5%. When calculating GET Taxable income, use only regular Revenue accounts. Record the total GET cost as GET Expense & GET Payable in a month-end accrual AJE. On the Income Statement, the Revenue Item included in Sales and the GET Expense net to zero Net Income effect.

B. A Sales Estimate is not a Sale

- (1) To bill customer and update inventory, you must actually create invoices from Estimates. Otherwise you may send a Sales Estimate to a customer, and they might pay you, but you would have no invoice to apply the payment to.

Creating an Invoice from the Estimate will turn it from a pending sale into an actual sale. Otherwise, nothing will be recorded in A/R subsidiary ledger or in the G/L.

- (2) To enable converting Estimates to Invoices:

Go to Gear > Account and Settings > Advanced > Automation. Once there, check to see that Copy estimates to invoices is On.

Click on the setting category Automation and a more detailed view will appear.

Change the dropdown box Copy accepted estimates only to Copy pending and accepted estimates

Then, under Customers > Estimates make your estimate.

To turn it into an invoice, click to view the Estimate and in the Estimate window click the Start Invoice button.

Once in the create new invoice view, click on the estimate information you want in the Add to invoice panel