



Università
Cattaneo

Management & Principles of Accounting

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Recording purchases

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Source: E-Book: (Basic accounting - how to prepare and analyze financial statements)
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Wolters Kluwer

E-Book

After this lesson you should be able to:


- Explain the recording of purchases

Example of Purchase Invoice

Please identify:

1. Invoice number
2. Seller
3. Invoice date
4. Purchaser
5. Saleperson
6. Credit Terms*
7. Good purchased: catalog numer, description, quantity, price per unit
8. Total invoice amount

INVOICE NO. 731



PW AUDIO SUPPLY, INC.
 27 CIRCLE DRIVE
 HARDING, MICHIGAN 48281

S
O
L
D
T
O

Firm Name Sauk Stereo

Attention of James Hoover, Purchasing Agent

Address 125 Main Street

Chelsea Illinois 60918
City State Zip

| | | | | | | | |
|--|---------------------------------|-------------|--------|----------|------------|--------------------|---------|
| Date | 5/4/14 | Salesperson | Malone | Terms | 2/10, n/30 | FOB Shipping Point | |
| Catalog No. | Description | | | Quantity | Price | Amount | |
| X572Y9820 | Printed Circuit Board-prototype | | | 1 | 2,300 | \$2,300 | |
| A2547Z45 | Production Model Circuits | | | 5 | 300 | 1,500 | |
| IMPORTANT: ALL RETURNS MUST BE MADE WITHIN 10 DAYS | | | | | | TOTAL | \$3,800 |

* Terms: 2/10 n. 30: 2% discount if paid within 10 days, otherwise net amount due within 30 days.

Recording purchases: cash vs. accounts payable

- When we buy goods paying cash we make the following entry:

| | | |
|--|----------|-------|
| Inventory (A) | 3.500 | |
| | Cash (A) | 3.500 |
| <i>Purchase of inventory, cost 3.500</i> | | |

- If we buy something “on account” we first record the debt and later the payment:

| | | |
|---|----------------------|-------|
| Furniture (A) | 6.000 | |
| | Accounts payable (L) | 6.000 |
| <i>Purchase of furniture, cost 6.000, to be paid in one month</i> | | |

| | | |
|--|----------|-------|
| Accounts payable (L) | 6.000 | |
| | Cash (A) | 6.000 |
| <i>Purchase of the debt related to the purchase of furniture</i> | | |

Recording purchases: notes payable

- The seller may ask to issue a “note payable”, that is a formal promise to pay a definite sum at a specific date in the future, including also the promise that the creditor may claim certain assets (collateral) if the debtor fails to pay the amount due. In this case we record, for example:

| | | |
|------------|------------------|-------|
| Plants (A) | 3.500 | |
| | Note payable (L) | 3.500 |

Purchase of a plant. Issued a note payable.

- At maturity we'll record:

| | | |
|-------------------|----------|-------|
| Notes payable (L) | 3.500 | |
| | Cash (A) | 3.500 |

Payment of the note payable

Note Payable - Example

Promissory note

For value received, the undersigned promises to pay to the order of BancZone, Inc.

the sum of: *****Ten-Thousand and no/100 Dollars***** (\$10,000.00)

Along with annual interest of 8% on the unpaid balance. This note shall mature and be payable, along with accrued interest, on June 30, 2008.

January 1, 2008 Olivia Zavala
Issue Date Maker signature

Source: Google

Recording purchases: notes payable

- The seller may also ask for interests in case of delayed payment. This interests are paid at maturity. Using the same example:

| | | |
|----------------------|-------|-------|
| Notes payable (L) | 3.500 | |
| Interest expense (E) | 350 | |
| | | |
| Cash (A) | | 3.850 |

Payment of the note payable + interest for 350 euros

Recording purchases: advance payment

- If we pay our supplier in advance, that is before receiving the goods or services purchased, we have to record an asset (a receivable), representing the right to receive something in the future:

| | | |
|------------------------------------|-------|----------------|
| Advance to supplier receivable (A) | 1.500 | |
| | | Cash (A) 1.500 |

Paid in advance to the supplier for the purchase of the furniture.

- When we receive the goods or services and we pay for what is left:

| | | |
|---------------|-------|---|
| Furniture (A) | 3.500 | |
| | | Advances to suppliers receiv. (A) 1.500 |
| | | Cash (A) 2.000 |

Received the furniture, total cost 3.500, paid cash the remaining amount

Recording purchases: returns, allowances and discounts

- If we return part of the goods purchased or ask for an allowance (reduction in price) we record:

| | | |
|---------------------|-----|-------------------|
| Account payable (L) | 300 | |
| | | Inventory (A) 300 |

Returned (or received an allowance of) 300 euros of goods previously bought

- Sometimes, if we pay before the agreed deadline, we benefit from a cash discount:

| | | |
|---------------------|-------|-----------------------------------|
| Account payable (L) | 3.500 | |
| | | Cash discounts on purchase (R) 70 |
| | | Cash (A) 3.430 |

Paid 3.500 euros to our supplier in advance, received a cash discount of 70

Recording purchases: sales tax receivable

- In some countries (like Italy) there are taxes on sales (e.g. VAT, value added tax). In most cases, if we are a business and we are buying goods or services for our business activity, we pay for the taxes to our supplier but we are reimbursed for the taxes paid by the government.

| | | |
|----------------------|-------|-------|
| Inventory (A) | 1.500 | |
| VAT receivable (A) | 330 | |
| Accounts payable (L) | | 1.830 |

Purchase of goods, cost 1.500+VAT 22%. Payment postponed.

- Who bears the cost of sales taxes like VAT is only the “final consumer” of the goods or services sold, that is the person who uses them for his own consumption and not to produce any other good or service

Recording purchases: Summary

| TRANSACTIONS | | PERPETUAL INVENTORY SYSTEM | |
|--------------|-----------------------------------|------------------------------------|-------|
| MAY 4 | Purchase of merchandise on credit | Inventory (A) | 3.500 |
| | | Account Payable (L) | 3.500 |
| MAY 6 | Advance payment | Advance to supplier receivable (A) | 1.500 |
| | | Cash (L) | 1.500 |
| MAY 8 | Purchase returns and allowances | Account Payable (L) | 300 |
| | | Inventory (A) | 300 |
| MAY 12 | Purchase discounts | Account Payable (L) | 3.500 |
| | | Cash (A) | 3.430 |
| | | Cash discounts on purchase (R) | 70 |

Review Questions

Review Question

A company makes a credit sale of € 750 on June 13 terms 2/10 n.30 What amount is received on June 23?

Review Question

What is a purchase discount?