

# Accounting for Merchandising Concerns



# 1) Inventory/Merchandise/Goods/Stock (Nature : Asset)

Items purchased for resale

Or

As per IAS-2:

Inventories are assets:

1. Held for sale in the ordinary course of business,
2. In the process of production for such sale or
3. In the form of materials or supplies to be consumed in the Production process or in the rendering of services.

## 2) Cost of Goods Sold (Nature : Expense):

Cost of goods that have been sold in the ordinary course of business.

### 3) Sales (Nature : Revenue):

The **price** at which the goods have been  
**sold** is 'Sales'

# Income Statement for Trading Business-Condensed

Revenue:	Rs.
Net Sales	500,000
Less: Cost of Goods Sold	<u>(350,000)</u>
Gross Profit/Loss	150,000
Less: Operating Expenses	<u>(50,000)</u>
Net Income / Loss	<u>100,000</u>

# Operating Cycle

## For Servicing Business

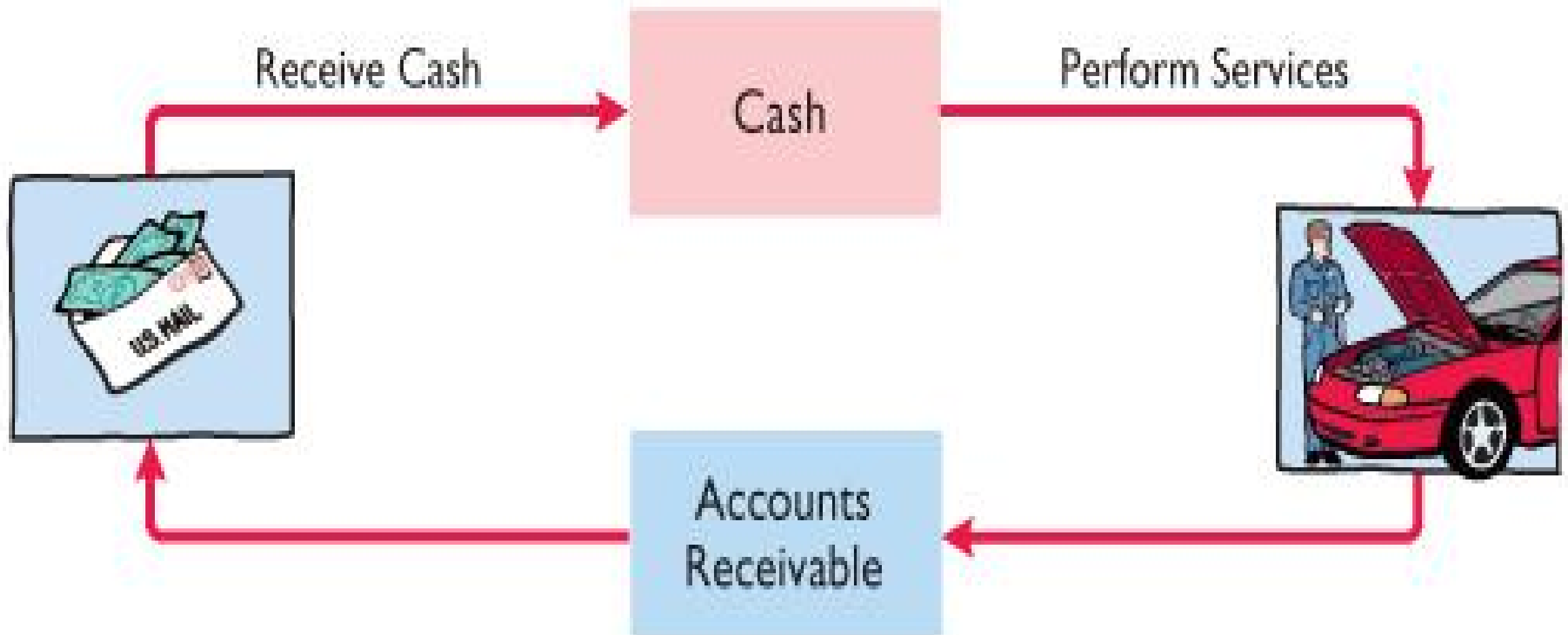
An Operating Cycle (OC) refers to the days required for a business **to render the services and collect cash** from the sale of the inventory.

## For Trading Business

An Operating Cycle (OC) refers to the days required for a business **to receive inventory, sell the inventory, and collect cash** from the sale of the inventory.

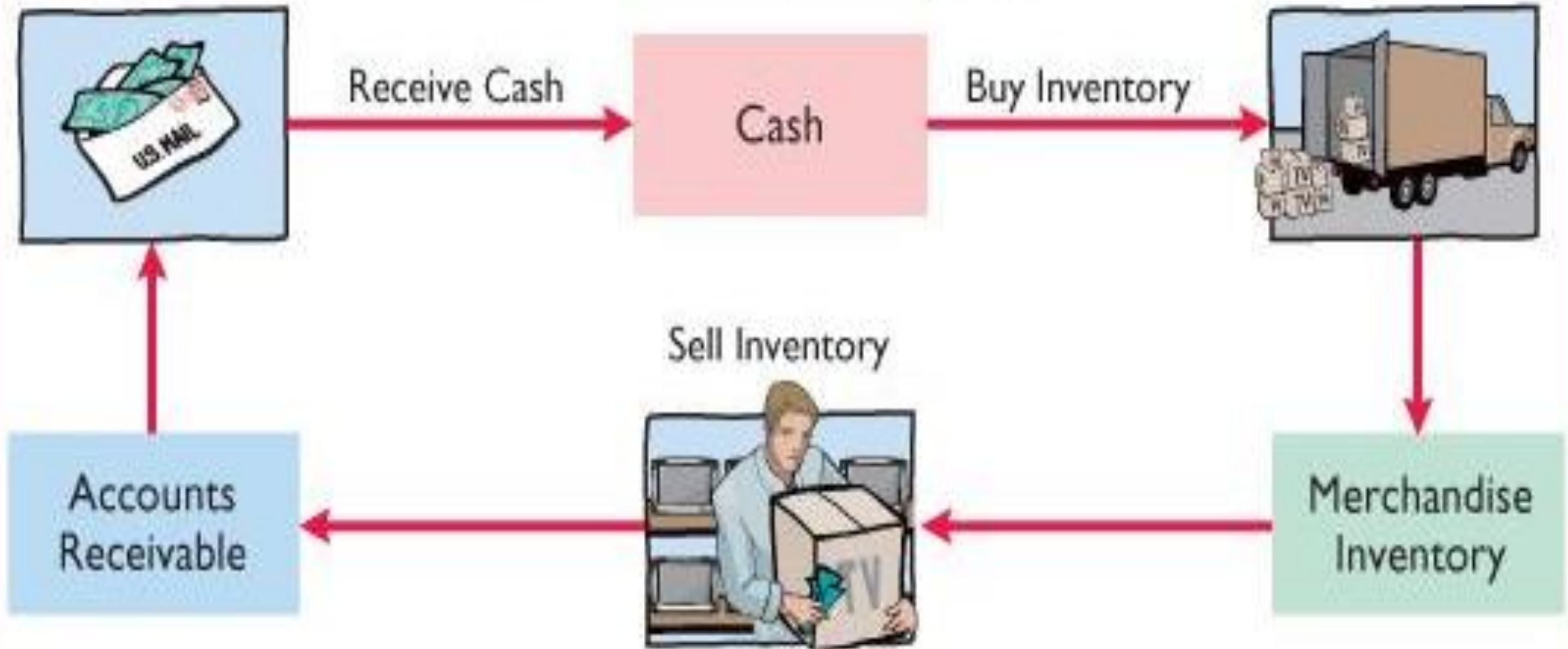
# Operating Cycle-Servicing Business

## Service Company



# Operating Cycle-Trading Business

## Merchandising Company





# Operating Cycle-Trading Business

```
graph TD; A[Operating Cycle-Trading Business] --> B[Accounting for Purchase of Inventory]; A --> C[Accounting for Sale of Inventory]; A --> D[Accounting for Receivables];
```

Accounting for  
Purchase of  
Inventory

Accounting for Sale  
of Inventory

Accounting for  
Receivables

# Cost Flow

Cost flow in trading business refers to the **manner** in which **cost** is **moved from inventory account to cost of goods sold account.**

# Cost Flow

*On Mar 5, 2022, inventory of Rs.200,000 was sold for Rs.300000.*

General Ledger Inventory					
2022 Jan 1	Cash	100,000	2022 Mar 5	Cost of Goods Sold	200,000
Feb 5	Accounts Payable	300,000			
Cost of Goods Sold					
2022 Mar 5	Inventory	200,000			

Sales					
			2022 Mar 5	Cash	300,000

# Inventory Valuation Systems

```
graph TD; A[Inventory Valuation Systems] --> B[Perpetual Inventory System]; A --> C[Periodic Inventory System];
```

Perpetual Inventory  
System

Periodic Inventory  
System

# Inventory Valuation Systems

## Perpetual Inventory System

## Periodic Inventory System

High cost goods

Low cost goods

Cost of inventory can be traced any time

Cost of inventory cannot be traced any time. For knowing the cost of inventory, physical inventory is counted and cost.

Costs of inventory sold and unsold are known entire accounting year.

Costs of inventory sold and unsold are not known entire year. In order to know the cost of inventory sold, unsold inventory is counted and cost and the cost of unsold inventory is deducted from total inventory to know cost of inventory sold

# Inventory Valuation Systems

## Perpetual Inventory System

Profit can be calculated any time during the year.

Financial reporting can be performed any time during the year.

## Periodic Inventory System

Profit cannot be calculated any time during the year. For profit calculation, cost of inventory sold is to be known and for that physical inventory is to be taken.

Financial reporting cannot be performed any time during the year without physical counting.