Lesson Blueprint

Computerized Accounting with QuickBooks® 2019

# Chapter 5: Inventory

## Introduction

* QuickBooks allows you to track inventory transactions.
* Inventory is ready-made merchandise that is sold to customers for a profit.
* Before you can enter inventory transactions, you must establish a file for each inventory item.
* Inventory item files are included in the Item List (Lists/Centers).
* Once you establish an inventory item file, transactions for the item (Activities) can be entered in the following activity windows in much the same manner as was done in prior chapters:
  + Enter Bills
  + Write Checks
  + Create Invoices
  + Enter Sales Receipts
  + Adjust Quantity/Value on Hand
* Every time the company receives merchandise for resale, sells merchandise, or adjusts the inventory because of loss or damage, QuickBooks will record that information in the Item List.
* This allows you to accurately determine inventory quantity, value, and profit on sales.
* In addition, QuickBooks automatically changes balance sheet and income statement accounts based on the inventory information on the Item List (Reports).
* In this chapter the sample company, Kristin Raina Interior Designs, begins to purchase and sell decorative accessories to clients in addition to providing design and decorating services.
* Kristin Raina must now be concerned with keeping an inventory

## QuickBooks versus Manual Accounting: Inventory Transactions

* As discussed in previous chapters, in a manual accounting system, purchases on account are recorded in a purchases journal, while sales on account are recorded in a sales journal.
  + This is true whether the purchase or sale is for services or for merchandise.
* Cash transactions are recorded in the cash receipts or cash payments journals, again for both inventory and non-inventory items.
* In QuickBooks, the Item List serves as an inventory subsidiary ledger for the company.
  + The Item List includes all items the company sells, both inventory and service items.
  + Relevant information for each inventory item, such as name/number, type, description, cost, sales price, and related general ledger accounts, is entered at the time the item file is created and updated as necessary.
* When the company purchases an inventory item from a vendor on account, the transaction is recorded in the Enter Bills activity window in much the same manner as non-inventory purchases were recorded.
* When the inventory items are sold on account, the invoice will be recorded in the Create Invoices activity window in a manner similar to that done for other sales.
  + When you enter these transactions, QuickBooks updates the Chart of Accounts (general ledger) and at the same time updates each vendor and customer file.
  + In addition, it updates the Item List to reflect the purchase and sale of the inventory items.
* Cash purchases of inventory items are recorded in the Write Checks activity window, while cash sales of inventory are recorded in the Enter Sales Receipts activity window.
* Changes in inventory not due to a sale or purchase are recorded in the Adjust Quantity/Value on Hand window.
* In all instances where inventory items are purchased, sold, or adjusted, the Item List is updated to reflect the new inventory quantity and value.
* Below is a comparison of manual accounting ledger and journals with QuickBooks functions:

|  |  |
| --- | --- |
| **Manual Accounting System** | **QuickBooks Pro** |
| Inventory Subsidiary Ledger | Item List (inventory part items) |

## Accounting for Inventory Transactions

* There are two types of inventory systems: periodic and perpetual.
* Under the periodic inventory system, separate records are not maintained for inventory items and no attempt is made to adjust the inventory account for purchases and sales.
  + Inventory is counted periodically to determine inventory quantity, value, cost of goods sold, and gross profit.
  + The periodic system was often used by businesses that sold high-volume, low-cost goods, for which keeping individual inventory records was not practical.
* Under the perpetual inventory system, accounting records are maintained that continuously show the current inventory quantity and value.
  + When inventory is purchased, the inventory (asset) account is increased.
  + When inventory is sold, the inventory account is reduced.
  + In addition, the cost of goods sold is simultaneously computed in order to arrive at gross profit.
* Prior to the availability of low-cost computer hardware and software, only businesses with low-volume, high-cost goods used the perpetual system.
* Now, with computers pervasive in business, most companies are now able to use a perpetual inventory system.
* QuickBooks, like almost all general ledger accounting software programs, utilizes the perpetual system because it allows the user to know the current inventory quantity and value at any given moment and also calculates the cost of goods sold and gross profit after each sale without the need for a periodic physical inventory count.

## Chapter Problem

* In this chapter inventory transactions are tracked for Kristin Raina Interior Designs, which has decided to begin selling decorative inventory items in addition to providing decorating and design services.
* Information for inventory items has been entered in the Item List.
* This information along with the March 1, 2021 beginning balances is contained in the company file CH5 Kristin Raina Interior Designs.
* See text for steps to open CH5 Kristin Raina Interior Designs.
* See text for steps to make a backup copy and restore the company file.
  + Use the file name EX5 [*Your Name*] Kristin Raina Interior Designs.
* See text for steps to change company name.
  + EX5 [*Your Name*] Kristin Raina Interior Designs

## Lists: The Item List

* Recall from Chapter 1 that the second level of operation in QuickBooks is to record background information in Lists /Centers.
* The Item List contains a file for each type of service or inventory item sold by the company.
* If the item sold is an inventory product, QuickBooks calls it an inventory part as opposed to a service item.
* You should enter the information for each inventory item in the Item List prior to recording transactions.
  + It makes the Activities function run more smoothly.
  + If you inadvertently omit an item, you can add that item during the Activities level of operation with a minimum of disruption.
* The Item List contains important information on each product, such as
  + type of item
  + number
  + description
  + cost
  + general ledger posting accounts for inventory asset, cost of goods sold, and sales
  + preferred vendor
  + sales tax status
* All products or services sold by the company should be included in the Item List.
* These files will need to be updated as products are added or discontinued, or background information changes.
* Kristin Raina has entered information for various inventory items in the Item List.
* See text for steps to review the Item List.
* Note the following fields in the Edit Item window:

|  |  |
| --- | --- |
| **TYPE** | If this is an inventory item, select *Inventory Part.* |
| Other selections include: |
| *Services* for service revenue items  *Non-inventory Part* for products sold that are not maintained in inventory  *Inventory Assembly*  *Other Charges* |
| **Item Name/Number** | Used to assign an identifying name or number to each item. |
| **Subitem of** | Used if item is a component of another item, such as in a construction or manufacturing company. |
| **Description on Purchase Transactions/ Description on Sales Transactions** | Used to enter a description of the item for sales activity windows. |
| **Cost** | Used to enter the typical unit cost for the item. |
| This amount will appear in the purchase activity window as the default cost amount. |
| Override as needed. |
| **COGS Account** | Lists the default general ledger posting account for cost of goods sold when the item is sold. |
| Override this account as needed. |
| **Sales Price** | This is the default unit-selling price that will appear in sales activity windows. |
| override this entry as needed. |
| **Tax Code** | Used to indicate if the item is taxable or nontaxable for sales tax purposes. |
| **Income Account** | This is the default general ledger posting account for revenue when the item is sold. |
| Override this account as needed. |
| **Asset Account** | This is the default general ledger posting account for the inventory balance sheet account when items are purchased. |
| Override this entry as needed. |

* Item List needs to be revised periodically when
  + new inventory items need to be added
  + inventory items not used in the business need to be deleted
  + when modifications need to be made as a result of inventory items changes
* These adjustments to the inventory item files are referred to as *updating* the Item List.

### Adding an Item

* Kristin Raina has decided to sell a line of modern lamps to clients and needs to add this inventory item to the Item List.
* See text for steps for adding an item.

### Deleting an Item

* Kristin Raina wishes to delete tapestries from the Item List because the company has decided not to sell this product.
* See text for steps for deleting an item.
* You cannot delete an item with a balance or an item that has been part of a transaction for the period.
* If you delete the wrong item, click Edit and then *Undo Delete Item* immediately after deleting the item.
* If you do not do this immediately, you will not be able to undo the deletion.

### Editing an Item

* Kristin Raina needs to edit the file for Draperies because the unit cost has increased to $125 and the sales price to $250.
* See text for steps for editing an item.
* Another way to access the Edit Item window is to select the item, click the Item button, and then click *Edit*.
* See text for practice exercise.

### Inventory Center

* similar to Vendor Center and Customer Center
* contains a file for each inventory item
* The Inventory Center duplicates the information contained in the Item List, but it does not contain a file for non-inventory part items.
* Many procedures reviewed in this chapter such as adding, editing, or deleting an item can be accomplished through the Inventory Center.

## Activities: Purchasing Inventory

* Recall from Chapter 1 that the third level of operation in QuickBooks is Activities, during which you record the daily business activities.
* Activities identified as purchases of inventory items on account are recorded in the Enter Bills window.
* Activities identified as purchases of inventory items for cash are recorded in the Write Checks window.
* use of purchase order is explained in Appendix D

### Recording Inventory Purchases Using the Enter Bills Window

* In Chapter 2 you used the Enter Bills activity window when goods and services were purchased on account from a vendor.
* There are two tabs in the Enter Bills window: Expenses and Items
* When you chose Enter Bills from the Vendor pull-down menu, the Enter Bills window would open with the Expenses tab as the active tab.
* When a company uses the inventory feature, the Vendors menu offers an additional choice of *Receive Items and Enter Bill.*
* When you click Receive Items and Enter Bill, the Enter Bills window is opened, but the Items tab is the active tab.
* In the Enter Bills window, the Items tab is similar to the Expenses tab but provides for additional fields that relate to inventory.
* In addition, you will find buttons that can be used when purchase orders are utilized in the purchase of inventory.
* In some instances, items will be received before the vendor forwards a bill.
* If this occurs, a different procedure is employed to record the transactions.
* For this chapter, it is assumed that a bill from the vendor accompanies the receipt of the inventory item and that you will record the transaction on the Enter Bills window–Items tab by clicking Vendor and then *Receive Items and Enter Bill*.
* Enter Bills window–Items tab contains the following new fields:

|  |  |
| --- | --- |
| **ITEM** | Click the inventory item purchased from the drop-down list. |
| Once an item is chosen, the *Description* and *Unit Cost* fields will automatically be filled based on information in the Item file. |
| **QTY** | Enter the quantity purchased. |
| QuickBooks multiplies the quantity purchased by the unit cost to arrive at the *Amount* and *Amount Due* figures. You can enter the quantity amount even with the Inventory Current Availability icon in the *Qty* field. |

* Notice that a field for the general ledger accounts is not displayed.
* Recall that when you entered items in the Items List, the general ledger accounts for the purchase (inventory asset account) and sale (income account and COGS account) of inventory items were indicated.
* QuickBooks uses the information in the Item List and the information entered in the Enter Bills window to adjust the correct accounts automatically.
* The Enter Bills window–Items tab is designed for purchases of inventory items on account.
* Default accounts are the Inventory asset account and the Accounts Payable account.
* QuickBooks uses the information on the Item List to correctly record the amount and account for the inventory asset.
* The transaction is recorded as follows:

|  |  |  |
| --- | --- | --- |
| Inventory | XXX |  |
| Accounts Payable |  | XXX |

### Recording a Purchase and Receipt of an Inventory Item on Account

* See text for steps for recording a purchase and receipt of an inventory item on account.
* If you click *Enter Bills* instead of *Receive Items and Enter Bill*, simply click the Items tab in the Enter Bills window.

### Recording Inventory Purchases Using the Write Checks Window

* Like the Enter Bills window, the Write Checks window has an Expenses tab and an Items tab.
* For purchase of inventory items for cash, switch to the Items tab after opening the Write Checks window.
* The fields to enter information for inventory items on the Write Checks window–Items tab are similar to those on the Enter Bill window–Items tab.
* The Write Checks window–Items tab is designed for purchases of inventory items for cash.
* The default accounts are the Inventory asset account and the Cash account.
* QuickBooks uses the information on the Item List to correctly record the amount and account for the inventory asset.
* The transaction is recorded as follows:

|  |  |  |
| --- | --- | --- |
| Inventory | XXX |  |
| Cash |  | XXX |

### Recording a Purchase and Receipt of an Inventory Item for Cash

* See text for steps for recording a purchase and receipt of an inventory item for cash.
* See text for practice exercise.

## Sales Tax

* When a company sells a product to a customer, it will usually be required to collect sales tax on the sale.
  + The sales tax amount charged is added to the invoice price of the product.
  + At a later date, the retailer will remit the tax collected from customers to the appropriate state sales tax collection agency.
* Rules for applying and collecting sales tax are complex and beyond the scope of this text.
* QuickBooks, like most general ledger software programs, is equipped to track sales-taxable transactions and to facilitate the collection and payment of taxes due.
* In this chapter Kristin Raina Interior Designs will be selling decorative accessories to her customers.
  + All sales of these products are subject to a sales tax charge of 7%, which is added to the invoice total.
  + The tax will be payable to the Minnesota Department of Revenue at the end of each month.
* Sales tax will not be collected on services (decorating and design) in this text because services generally are not subject to sales tax.
  + Note, however, that in some communities, services also are subject to sales tax.
* As you know from Chapter 3, a sale on account is recorded in the Create Invoices window and a sale for cash is recorded in the Enter Sales Receipts window.
  + The default account in the Create Invoices window is a debit to Accounts Receivable.
  + The default account in the Enter Sales Receipts window is a debit to Cash or Undeposited Funds.
* When sales tax is charged on the sale of an item, a default Sales Tax Payable account is credited in both the Create Invoices and Enter Sales Receipts windows.
* The sale of taxable products for either cash or on account results in the following general ledger posting:

|  |  |  |
| --- | --- | --- |
| Accounts Receivable/Cash or  Undeposited Funds | XXX |  |
| Sales |  | XXX |
| Sales Tax Payable |  | XXX |

## Activities: Sale of Inventory

* Activities identified as sales of inventory items on account are recorded in the Create Invoices window.
* Activities identified as sales of inventory items for cash are recorded in the Enter Sales Receipts window.
* Activities recorded in these windows are similar to those in Chapter 3, but additional fields in the window are used that relate to inventory.

### Inventory Sales on Account in the Create Invoices Window

* When you record the sale of inventory items in the Create Invoices window, you use a template to access the additional fields needed for inventory items.
  + In Chapter 3, for the sale of services, you used the Intuit Service Invoice Template.
  + For the sale of inventory items on account, you use the Intuit Product Invoice Template.
* The Intuit Product Invoice is designed for the sale of inventory items on account.
  + The default accounts are Accounts Receivable, Cost of Goods Sold, Inventory, Sales Tax Payable, and Sales.
* QuickBooks uses the inventory Item List to determine the correct amount and account for the Cost of Goods Sold, Inventory, and Sales accounts.
* If an item is marked as taxable, QuickBooks uses the Item List to determine the correct amount of sales tax to be recorded in the Sales Tax Payable account.
* The transaction is recorded as follows:

|  |  |  |
| --- | --- | --- |
| Accounts Receivable | XXX |  |
| Cost of Goods Sold | XXX |  |
| Inventory Asset |  | XXX |
| Sales Tax Payable |  | XXX |
| Sales |  | XXX |

### Recording a Sale of an Inventory Item on Account

* See text for steps for recording a sale of an inventory item on account.
* You may need to press the Tab key to move to additional lines in the Create Invoice window.
* If you miss an item, click Edit and then *Insert Line*.
* If you wish to erase a line, click Edit and then *Delete Line*.

### Inventory Sales for Cash in the Enter Sales Receipts Window

* The Enter Sales Receipts window is designed for cash received for both the sale of services and the sale of inventory items for cash.
* Once an inventory item is chosen, QuickBooks uses the information from the Item List to correctly record the Cost of Goods Sold, Inventory, and Sales accounts.
* If an item is marked as taxable, QuickBooks uses the Item List to determine the correct amount of sales tax to be recorded in the Sales Tax Payable account.
* The transaction is recorded as follows:

|  |  |  |
| --- | --- | --- |
| Cash or Undeposited Funds | XXX |  |
| Cost of Goods Sold | XXX |  |
| Inventory Asset |  | XXX |
| Sales Tax Payable |  | XXX |
| Sales |  | XXX |

### Recording a Sale of an Inventory Item for Cash

* See text for steps for recording a sale of an inventory item for cash.
* If you miss an item, click *Insert Line* from the Edit menu.
* If you wish to erase a line, click *Delete Line* from the Edit menu.
* See text for practice exercise.

### Sales Discounts

* Sales discounts are offered to customers to encourage early payment of outstanding invoices.
* Generally, companies provide for a 1% or 2% reduction of the invoice amount if the payment is made within 10 days of the invoice date.
* See text for steps for recording a receipt of payment within the discount period.
* The Automatic Payments window warning appears because in the company preferences for payments, the Automatically calculate payments option has been selected.
  + - This option can be found in the Preferences window. At the main menu bar click Edit, click Preferences, click the Payments icon, and click the Company Preferences tab.
* If the correct date does not appear in the *Discount Date* field, complete the following steps.
  + Exit the Receive Payments window without saving.
  + Open the Create Invoices window and use the Previous arrow to locate the correct invoice.
  + Check the date, click the *Terms* field, and then click Save & Close.
  + Reopen the Receive Payments window; the *Discount Date* field should be corrected.
  + If you make an error on the payment, you can correct changes and resave, or click Edit and then *Delete Payment* and start over.
* If you forget to record the discount and go back to edit the transaction, after choosing Done in the Discounts and Credits window, you must correct the amount in the *Amount* field—it is not corrected automatically.
* See text for practice exercise.

## Activities: The Adjust Quantity/Value on Hand Window

* In QuickBooks, you use the Adjust Quantity/Value on Hand activity window to record changes in the inventory from events other than a purchase or sale.
* If inventory items are lost, stolen, damaged, or spoiled, the resulting change in the inventory quantity and/or value will be recorded in this window as an inventory adjustment.
  + The reduction is considered a loss/expense with a corresponding reduction in the inventory asset account.
  + The account that will be used to record the reduction to inventory is the Inventory Adjustment account.
  + This account is a cost of goods sold account and will be included in the cost of goods sold section of the income statement.
* Activities identified as adjustments to inventory are recorded in the Adjust Quantity/Value on Hand window.
* All transactions entered in this window result in a debit to the Inventory Adjustment account and a credit to the appropriate inventory asset account.
* QuickBooks records the transaction as follows:

|  |  |  |
| --- | --- | --- |
| Inventory Adjustment (Loss/Cost of Goods Sold) | XXX |  |
| Inventory (Asset) |  | XXX |

* See text for steps to record an inventory adjustment.
  + If the inventory adjustment was a result of a change in value only, without a change in quantity, *Total Value* should be chosen from the Adjustment Type drop-down list; this allows you to adjust the value without changing the quantity.
* If you make an error in this window, click Edit and then *Delete Inventory Adjustment* and redo the transaction.

## Activities: The Pay Sales Tax Window

* In QuickBooks, the Pay Sales Tax window is used to record the remittance to the proper tax agency of sales tax charged to customers.
* QuickBooks uses the default accounts Sales Tax Payable and Cash.
* QuickBooks records the transaction as follows:

|  |  |  |
| --- | --- | --- |
| Sales Tax Payable | XXX |  |
| Cash |  | XXX |

* See text for steps to pay the sales tax collected.

## Activities: Make Deposits

* Recall from Chapter 3 that Kristin Raina Interior Designs deposits all funds collected from customers at the end of the month.
* Before reviewing the reports for the month, the deposits should be recorded.
* See text for practice exercise.

## Reports: Inventory Items and financial reports

* Recall from Chapter 1 that Reports, the fourth level of operation, reflect the activities recorded in the various Lists and Activities windows.
* Inventory activities entered in the various windows flow into the reports, many of which should be displayed and printed at the end of the month.

### Inventory Reports from the Reports Menu

* Inventory reports, such as the *Inventory Valuation Detail* report, *Inventory Stock Status by Item* report, and the *Purchases by Item Detail* report help the company track and manage its inventory.

**Inventory Valuation Detail report**

* + The *Inventory Valuation Detail* report displays the transactions affecting each inventory item along with the quantity and value on hand for each.
  + See text for steps to view and print the *Inventory Valuation Detail* report.

**Inventory Stock Status by Item report**

* + The *Inventory Stock Status by Item* report displays the on-hand status of each inventory item.
  + The report indicates whether an item should be ordered based upon on-hand quantity and the reorder amount.
  + See text for steps to view and print the Inventory Stock Status by Item report.

**Purchases by Item Detail report**

* + The *Purchases by Item Detail* report displays all purchase information for each inventory item.
  + The report shows vendor name, cost per unit, quantity purchased, and the total cost.
  + See text for steps to view and print the *Purchases by Item Detail* report.
  + This report, like several of those reviewed in prior chapters, allows you to drill down to view the source transaction.
  + See text for an example of drilling down from a report.

### Inventory Reports from the Lists Menu

* QuickBooks allows you to view and print several inventory reports from the Lists windows.
* Once a list is accessed, a report list is available that is accessed by clicking the Reports menu button in the List window.
* The *Sales by Item Detail* report shows sales of all inventory items both on account and for cash.
* See text for steps to view and print the *Sales by Item Detail* report.
* In addition to the Sales reports, Purchase, Inventory, Item, and Price reports can be viewed from the Reports menu of the Item List.
* See text for practice exercise.

### Accounting Reports and Financial Statements: Journal, Income Statement, Balance Sheet

* At the end of each month, the *Journal*, *Profit & Loss (Income Statement)*, and *Balance Sheet* reports should be viewed and printed.

# Chapter 5 Accounting Terms

**inventory** Merchandise that is sold to customers for a profit.

**inventory adjustment** An amount recorded in an expense or loss account to reflect the reduction of inventory value and/or quantity due to loss, theft, or damage.

**periodic inventory system** Values the inventory periodically based on a physical count of the merchandise; usually done once a year.

**perpetual inventory system** Values the inventory after every purchase and sale of inventory items.

**sales discount** A reduction in the selling price if the invoice payment is made shortly after the invoice date.

**sales tax** An amount charged on the sale of merchandise, usually a percentage of the sales price. It is collected by the company as part of the sale and later remitted to the appropriate government agency.