The double-entry system for the Asset of Stock (Inventory)

The purchase of stock

Goods that are bought with the prime intention of selling are known in accounting terms as Purchases or Inventory. Goods are usually sold above cost price with the difference being Profit. In the event that goods are sold below the cost price then the difference would be known as a Loss.

In certain circumstances goods purchased from the supplier are returned because they are faulty or surplus (not needed anymore). In accounting terms these returns are classified as Returns Outwards or Purchases/Inventory Returns.

In order to record the purchase of stock and any returns outwards to the supplier, two accounts are opened:

- 1- Purchases Account in which purchases of goods are recorded.
- 2- Returns Outwards Account in which goods being returned out to a supplier are entered. The alternative name for this is the Purchases Returns Account.

Sales of Stock

In accounting terms the word Sales refers to the sale of those goods which were bought with the prime intention of re-selling. As a result for an accountant there is a clear difference between the sale of stock and the disposal of an asset that might bring money into the firm. For example, a firm that deals in the sale of glass would consider the sale of stock items such as glass pots and trays as sales of stock/inventory. However, if the firm disposed of a delivery van for a sum of money by selling it to someone outside the firm, then this would **NOT** be considered as a sale of stock and would be recorded as a Disposal.

In certain circumstances goods that have been sold to a customer might be returned inwards to the firm. The accountant will record these returns from the customer as Returns Inwards or Sales Returns.

In order to record the sale of stock and the returns inwards by customers two accounts have to be opened:

- 1- Sales Account in which sales of goods are entered.
- 2- Returns Inwards Account in which goods being returned into the firm are entered. The alternative name for this account is the Sales Returns Account.

Purchase of stock on credit

- 1 August 20X4. Goods costing \$1,650 are bought on credit from D Hoover. First, the double entry effect must be considered.
- 1 An increase in an asset. The asset of stock is increased on the debit side of the Purchases/Inventory account.
- 2 An increase in a liability. As the stock/inventory has not yet been paid for then the liability to D. Hoover (Creditor) will be shown on the credit side.

Dr	Pt	Cr			
August 1	D. Hoover	\$ 1,650			\$
Dr		Cr			
		\$	August 1	Purchases or Inventory	\$ 1,650

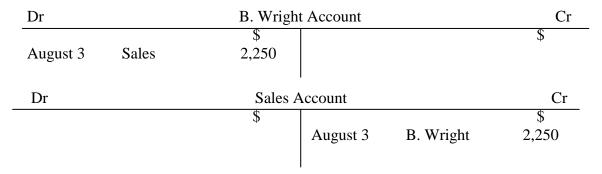
www.igcseaccounts.com Purchase of stock for cash

- 2 August 20X4. Goods/Inventory costing \$220 are bought with the owner paying cash.
- 1 The asset of stock/inventory is increased, so that a debit entry will be needed on the purchases account.
- 2 The asset of cash is decreased and this will be shown as a credit entry in the cash account.

Dr	P	Cr			
August 1	D. Hoover	\$ 1,650			\$
August 2	Cash	220			
Dr		Cr			
		\$	Aug 2	Cash	\$ 220

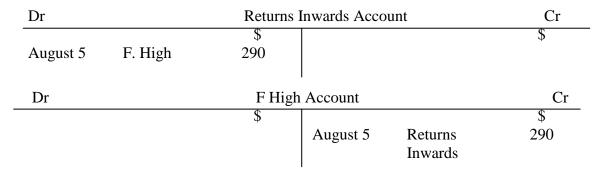
Sales of stock on credit

- 3 August 20X4. Sold goods on credit for \$2,250 to B Wright.
- 1 An asset account is increased. B. Wright is now a debtor (Asset) to the business and this is recorded on the debit side of his named debtor account.
- 2 The asset of stock is decreased. For this a credit entry to reduce the asset of stock is made in the Sales account.



Returns Inwards

- 5 August 20X4. Goods sold to F High for \$290 are now returned by him to the business. This could be for various reasons such as:
- we have sent him goods of the wrong size, the wrong colour or the wrong model;
- the goods may have been damaged when transported;
- the goods are of bad quality;
- 1 The asset of stock is increased by the goods returned and a debit entry is made in the Returns Inwards or Sales Returns account.
- 2 A decrease in an asset. The debt of F High is now reduced and this is recorded on the credit side of his debtor 'T' account.



Returns Outwards

- 6 August 20X4. Goods previously bought for \$960 are returned by the firm to K Watt.
- 1 The liability of the firm to K Watt is decreased and this is shown by a debit entry to K Watts creditor account.
- 2 The asset of stock is decreased by the goods sent out which is entered as a credit in the Returns Outwards or Purchases Returns.

Dr		Cr			
August 6	Returns Outwards	\$ 960			\$
Dr		Returns	Cr		
		\$	August 5	K Watt	\$ 960







