Perpetual vs. Periodic Inventory System Journal Entries

THE BEST WAY TO UNDERSTAND AN ACCOUNTING TRANSACTION IS THROUGH EXAMPLES, PLEASE WORK THROUGH THIS SENARIO EXAMPLES AND BE MINDFUL OF THE DIFFERENT JOURNAL ENTRIES FOR THE 2 DIFFERENT SYSTEMS USED.

A. The Sale and Purchase of Products

Perpetual inventory systems show all changes in inventory in the "Inventory" account. Purchase accounts are not used in a perpetual inventory system.

When Good are Sold

Dr BANK / Acc REC

Cr Sales

Dr Cost of Sales

CR Inventory

Note from this transaction a sale of goods is recorded to increase Sales increase bank

And

Then the contra account affects because of the Sale is increase cost of Sales, and inventory is decreasing

Periodic inventory systems keep the inventory balance at the same value that it was at the beginning of the year. At year end, the inventory balance is adjusted to a physical count. To account for inventory purchases in a periodic inventory system, an account called "Purchases" is used rather than debiting "Inventory".

When Goods are Sold

Dr BANK / Acc REC

Cr Sales

Under Periodic system Goods are sold only affects Sales, and not COST OF SALES account. And inventory account is updated at year end; refer to Nr 4 of sample exercise below.

REFER TO EXAMPLE BELOW

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Example: (Unit cost is held constant to avoid the necessity of a using
            a cost flow assumption)

                Beginning inventory        100 units @ R6   = R 600
                Purchases                  900 units @ R6   = R5,400
                Sales                      600 units @ R12  = R7,200
                Ending inventory           400 units @ R6   = R2,400

      Perpetual Inventory System          |       Periodic Inventory System
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1. Beginning inventory 100 units at R600

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Inventory account shows R600 in inventory.	Inventory account shows R600 in inventory.

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2. Purchase of 900 units at R6 per unit

(Here we see under Perpetual purchases are DR to Inventory were under Periodic purchase are DR to Purchases)

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Inventory	5,400		Purchases	5,400	
Acc. Payable		5,400	Acc. Payable		5,400

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3. Sale of 600 units at a selling price of R12 per unit

Note the entry to Record sales the additional Jrnl to record "COST OF SALES AGAINST INVENTORY"

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Acc. Receivable	7,200		Acc. Receivable	7,200	
Sales		7,200	Sales		7,200
Cost of Sales	3,600		No entry		
Inventory		3,600			

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4. End-of-period entry for inventory adjustment

Note the additional jnl under Periodic Inventory System and no entry under Perpetual system

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No entry needed. The ending balance of inventory shows 2,400.	Inventory		1,800
	Cost of Goods Sold	3,600	
	Purchases		5,400

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Note: The periodic inventory adjustment in transaction 4 adjusts inventory to the physical count, closes out any purchase accounts,and runs any difference through cost of sales.

B. Cost of Goods Sold in a Periodic Inventory System

Perpetual inventory systems record cost of goods sold and keep inventory at its current balance throughout the year. Therefore, there is no need to do a year-end inventory adjustment unless the perpetual records disagree with the inventory count. In addition, a separate cost of goods sold calculation is unnecessary since cost of goods sold is recorded whenever inventory is sold.

The inventory account in a periodic inventory system keeps its beginning balance until the end of period adjustment to the physical inventory count. Therefore, a separate cost

of goods sold calculation is necessary. The following calculation shows the calculation for the preceding example.

```
Beginning Inventory              600
Net Purchases                  5,400
                              -------
Goods Available for Sale       6,000
Ending Inventory               2,400
                              -------
Cost of Goods Sold             3,600
                              =======
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Please note the 4TH steps indicated above, if you understand the two journal methods that is used then you will master the concept on this two inventory systems. Be careful in the an examination question to always look out for the type of inventory system used and base answers on the Journal rules mentioned above. I trust this helps you understand the concepts. Should you need further clarity please let me know.

Good Luck, Happy Studying

Regards
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