Accounting for Special Transactions - 3.Sale on Approval or Return Basis

CHAPTER OVERVIEW

- 1. Concept of Sale on Approval or Return basis
- 2. A/cing Methods
 - (a) Casual Sale or Return
 - (b) Infrequent Sale or Return (use of S/R Journal)
 - (c) Routine and numerous S/R transactions (use of Memoranda Books)

3. Sale of Goods on Approval or Return Basis

3.1 Concept of "Sale of Goods on Approval or Return basis"

- Need: In order to increase the sales of a product or to introduce a new product, a Firm may sell goods on approval or return basis. Generally, these transactions take place between the Manufacturer (or Wholesaler) and a Retailer.
- 2. **Effect**: In a Sale of Goods on Approval or Return basis, the goods will be delivered to the customers, with the option of either retaining them or returning them within a specified period.
- Possession vs Ownership: When goods are sold on Approval or Return basis, there is a change in possession of goods only, and not a transfer of ownership of goods.
- 4. **Transfer of Ownership:** As per the Sale of Goods Act, in respect of goods sent on approval or return basis, the transfer of ownership will take place only
 - (a) When the Buyer / Customer gives his approval, (direct consent)
 - (b) When the Buyer / Customer does some act which denotes that he accepts the transaction, i.e. consumption or use of the goods involved, (implied consent)
 - (c) If the Buyer / Customer has not given his approval or acceptance to the Seller but retains the goods without giving the notice of rejection, on the expiry of the specified time (if a time has been fixed) or on the expiry of a reasonable time (if no time has been fixed) (by lapse of time)

3.2 Methods of accounting of Goods sold on Approval or Return basis

Accounting Treatment for Sale of Goods on Approval or Return basis When transactions are very When transactions are very less, i.e When transactions are very frequent frequent, but not numerous i.e. casual Sale or Return and numerous frequent Sale or Return Transaction is treated as Ordinary Sale or Return Day Book and Ledger Sale or Return Journal is prepared Sales. are prepared. These are regarded as with 4 main columns. See Para 3.4 Memoranda Books. See Para 3.3 below below

3.3 Entries if the Firm sends goods casually on Sale or Return basis

Scheme of Journal Entries in case of INFREQUENT Sale or Return transactions

Transaction

Journal Entry

Remarks

1. Goods despatched on Approval or Return Basis

Sundry Debtors A/c
To Sales A/c

To Sales A/c

At Selling Price.

	Transaction	Journal Entry	Remarks
2.	Goods returned by Customer within the specified period	Sales Returns or (Sales) A/c Dr. To Sundry Debtors A/c	At Selling Price.
3.	Goods accepted by Customer within specified period	No separate Journal Entry is required since it is already recorded as Normal Sales only.	Not Applicable
4.	Goods accepted at a price higher than the Invoice Price	Sundry Debtors A/c Dr. To Sales A/c	Difference in Price only.
5.	Goods accepted at a price lower than the Invoice Price	Sales A/c Dr. To Sundry Debtors A/c	Difference in Price only.
6.	Goods pending approval at the end of the accounting period	Sales A/c Dr. To Sundry Debtors A/c	At Selling Price.
7.	Recognition of Stock with customers at year—end	Stock with Customers A/c Dr. To Trading Account	Cost or NRV, whichever is less.

Illustration 1: Sale or Return - Casual and Infrequent transactions

Ram sends his goods to some of his customers on Approval or Return basis. The cost of the product is ₹8,000 per unit and a markup of 25% on cost is used. The following information is given –

- Goods sent to customers during the period = 25 units.
- Goods returned by customers before approval period = 6 units.
- Goods approved by customers before end of the financial period = 16 units.
- Goods with customers pending approval (period not expired) = 3 units.

Ram accounts for these transactions as Ordinary Sales. Give the Journal Entries for the above.

Solution:

Journal Entries

	Particulars	10 S E	Dr.	Cr.
1.	Sundry Debtors A/c To Sales A/c	Dr.	2,50,000	2,50,000
E lo	(Being Goods despatched to Customers on Approval or Return Basis, at ₹8,000 + 25% Markup = ₹10,000 per unit for 25 units)		to esidon	m
2.	Sales A/c (or) Sales Returns A/c	Dr.	60,000	
	To Sundry Debtors A/c			60,000
	(Being Goods returned by S/R Customers = 6 units at ₹10,000 reversed)			
3.	Sales A/c	Dr.	30,000	
	To Sundry Debtors A/c			30,000
	(Being goods pending approval at the end of the accounting period, earlier sales entry now cancelled = 3 units at ₹10,000, now reversed)	al ye	urara ancilal	When board
4.	Stock with Customers on Sale or Return basis A/c	Dr.	24,000	
	To Trading A/c			24,000
	(Being 3 units Stock with customers at year-end, valued at Cost 8,000 p.u.)	4n0 t	12/19/21/2	

Note: 1. No entry is required for goods approved by Customers ₹1,60,000.

2. Alternatively, Cost of Goods lying with Customers = ₹30,000 × 100/125 = ₹24,000.

Illustration: "OR" Option: Accounting for Sale on Approval basis

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Mr. Ganesh sends out goods on approval to few Customers and includes the same in the Sales Account. On 31.03.2018, the Trade Receivables balance stood at ₹ 75,000 which included ₹ 6,500 Goods sent on approval against which no intimation was received during the year. These Goods were sent out at 30% over and above Cost Price and were sent to –

Mr. Adhitya ₹ 3,900 and Mr. Bakkiram ₹ 2,600.

Mr. Adhitya sent intimation of accepting on 25th April 2018 and Mr. Bakkiram returned the goods on 15th April 2018. Make the Adjustment Entries and show how these items will appear in the Balance Sheet as on 31st March 2018. Show also the Entries to be made during April 2018. Value of Closing Inventories as on 31st March 2018 was ₹ 50,000.

Solution:

1. Adjustment Entries

	Particulars		Dr.	Cr.
31.3.18	Adhitya (Sundry Debtors) A/c	Dr.	3,900	
	Bakkiram (Sundry Debtors) A/c	Dr.	2,600	
	To Sales A/c		Accessor	6,500
	(Being Goods despatched to Customers on Approval or Return Basis, at ₹ 75,000) Note: This Entry has already been passed and given only for information.			
31.3.18	Sales A/c	Dr.	6,500	nadili s
	To Adhitya (Sundry Debtors) A/c		D 2002 F	3,900
	To Bakkiram (Sundry Debtors) A/c		must name	2,600
	(Being goods pending approval at the end of the accounting period, earlier sales entry, now reversed)		matell male	
31.3.18	Stock with Customers on Sale or Return basis A/c	Dr.	5,000	
	To Trading A/c			5,000
	(Being Stock with customers at year–end, valued at Cost $\frac{75,000}{130} \times 100$)		molfren	
25.4.18	Adhitya (Sundry Debtors) A/c	Dr.	3,900	
	To Sales A/c		- m timber	3,900
	(Being goods sent to Adhitya on Sale or Return basis, and accepted by him)			

Note: No Entry is required to be passed on 15.04.2018 for goods returned by Mr. Bakkiram. Goods should be included physically in the Stock in Trade. (and reduced from Stock with Customers).

2. Balance Sheet (Extract)

Liabilities	₹	Assets	₹	₹
374.34		Trade Receivables (75,000 – 6,500)	\$1 \$2 \$2 \$10 \$1 \$2 \$4 \$2 \$1	68,500
nam at Selmo Price		Stock in Trade	50,000	Constant
ed amountain		Add: Stock with Customers on Sale or Return basis	5,000	55,000

3.4 Accounting Treatment when Sale of Goods on Approval or Return basis are frequently done

When Sale or Return transactions are **very frequent, but not numerous,** a separate Register called "Sale or Return Journal" is maintained. The format of this Register is as under –

Goods sent on approval			Goods Returned			Goods Approved				Balance		
1	2	3	4	5	6	7	8	9	10	11	12	13
Date	Particulars	LF	Amt	Date	Particulars	LF	Amt	Date	Particulars	LF	Amt	Amt.
No e	entry in Finan	cial Bo	ooks	No e	entry in Finan	cial B	ooks	-	Recorded as	Sales	0.00	Treated as Stock

Transaction	Treatment				
1. Goods despatched to Customers	 No entry in Financial Books. Record the despatch in Columns 1 to 4 of the above Journal. 				
2. Goods returned by Customers	 No entry in Financial Books. Record the return in Columns 5 to 8 of the above Journal. 				

Transaction	Treatment						
3. Goods approved by Customers	 Record the approval in Colur Record as Sales, by the follo Sundry Debtors A/c To Sales A/c 	owing Journal Entry – Dr. (At Selling Price) (At Selling Price)	Sawjaa Sawjad sihulo2				
4. Stock at end of the period	Recorded as Closing Stock, by the Stock with Customers A/c Dr. (A To Trading Account	ne following Journal Entry –	81.0.16				

3.5 Accounting Treatment when transactions relating to Sale of Goods on Approval or Return basis are frequent and numerous

- When Sale on Approval or Return transactions are frequent and numerous, there is a need to ensure proper control
 over the Sale or Return transactions. For this purpose, the Firm maintains
 - (a) Sale or Return Day Book Same format as specified in Q.No.4 above.
 - (b) Sale or Return Ledger containing the Ledger Accounts of Customers to whom goods are sent.
- 2. This Day Book & Ledger are Memorandum Books. They do not form part of the regular financial books.

3. The accounting process is explained below -

	Entry in								
Transaction	Sale or Return Day Book	Sale or Return Ledger	Financial Books, i.e. Regular General Ledger						
Goods despatched to Customers	Record the despatch in Columns 1 to 4 of the S/R Day Book.	Customer A/c Dr. To Sale or Return A/c (Entry made at Selling Price)	No Entry in Financial Books.						
Goods returned by Customers	Record the return in Columns 5 to 8 of the S/R Day Book.	Sale or Return A/c Dr. To Customer A/c (Entry made at Selling Price)	No Entry in Financial Books.						
Goods approved by Customers (See Note below)	Record the approval in Columns 9 to 12 of S/R Day Book.	Sale or Return A/c Dr. To Customer A/c (Entry made at Selling Price)	Customer A/c Dr. To Sales A/c (Entry made at Selling Price)						
Stock at end of the period	Column 13 denotes Stock at Sale Price.	Balance in Sale or Return A/c is the value of Stock with Customers, at Sale Price.	Stock with Customers Dr. To Trading A/c (Entry made at Cost or NRV, whichever is lower)						

Note: When goods are approved by customers, the earlier memorandum Sale entry in Sale or Return Ledger is reversed, and the regular Sales Entry is recorded in the Financial Books.

Illustration 2: Sale or Return - Frequent and Numerous transactions

Krishna regularly sends goods to his customers on Approval or Return basis. The cost of the product is ₹4,000 per unit and a markup of 1/3rd on Price is used. The following information is given for the month of January –

Date	7 th	14 th	18 th	23 rd	25 th
Customer Name	A	В	С	D	E
Quantity sent	4	4	6	3	2

B and C approved the goods within the stipulated time, while A and E have rejected and returned the goods on 27th. In respect of D, the time period for acceptance has not yet elapsed. Show the accounting entries in the S/R Day Book, Sale or Return Account (in S/R Ledger).

Solution: Note: Since Markup is $1/3^{rd}$ on Price = 1/2 on Cost = $\frac{7}{2}$,000. So, Sale Price = $\frac{7}{6}$,000.

1. Sale or Return Day Book for the month of January

Goods sent on approval					Goods Returned			Goods Approved				Balance
1	2	3	4	5	6	7	8	9	10	11	12	13
Date	Particulars		Amt	Dt	Particulars		Amt	Dt	Particulars	lig	Amt	Amt.
7	A- 4 units		24,000	27	A-4 units		24,000					
14	B- 4 units		24,000		Annual Park and Assessment				B- 4 units		24,000	
18	C-6 units		36,000	AVAILED	The second second	1			C-6 units		36,000	
23	D-3 units		18,000		The state	45	Note Tan	mm	April (Root) Win	83	sommeting of	18,000
25	E-2 units		12,000	27	E-2 units		12,000	31 n	i Grant an America	1 2		w later 33
	Total		1,14,000		Total	Jan.	36,000		Total		60,000	material I

2. Journal Entries in Sale or Return Ledger (Memoranda Book)

	Particulars		Dr.	Cr.
1.	Sundry Customers (A, B, C, D, E) A/c	Dr.	1,14,000	1.3
	To Sale or Return A/c	-		1,14,000
	(Being Goods despatched to Customers on Approval or Return Basis)			
2.	Sale or Return A/c	Dr.	36,000	
	To Sundry Customers (A, E) A/c			36,000
	(Being Goods returned by S/R Customers)			
3.	Sale or Return A/c	Dr.	60,000	
	To Sundry Customers (B, C) A/c			60,000
	(Being goods approved by parties, earlier memorandum entry now cancelled)			

3. Sale or Return A/c (in S/R Ledger)

		7 - ()	
Particulars	₹	Particulars	₹
To Sundry Customers (A,E) (returned)	36,000	By Sundry Customers (A,B,C,D,E)	1,14,000
To Sundry Customers (B,C) (approved)	60,000	1	- 1
To balance c/d (pending approval)	18,000		
Total	1,14,000	Total	1,14,000

Note: In the Financial Books, entry will be passed for Sales made to B and C, to the tune of $\stackrel{?}{\sim}$ 60,000, and also for recording Closing Stock with Customers at Cost (3 units with D at $\stackrel{?}{\sim}$ 4,000 = $\stackrel{?}{\sim}$ 12,000).

Illustration 3: Sale or Return

A firm sends goods on "Sale or Return basis". Customers have the choice of returning the goods within a month. During May 2018, the following are the details of goods sent:

Date (May)	2	8	12	18	20	27
Customers	Р	В	Q	D	E	R
Value (₹)	17,000	22,000	25,000	5,500	2,000	28,000

Within the stipulated time, P and Q returned the goods and B, D and E signified that they have accepted the goods.

Show in the books of the firm, the Sale or Return Account and Customer–Q for Sale or Return Account as on 15th June 2018.

Solution:

1. Sale or Return A/c

1. Sale of Return A/C						
Particulars	₹	Particulars	₹			
To Sundry Customers (P,Q) (returned)	42,000	By Sundry Customers (P,Q,B,D,E,R)	99,500			
To Sundry Customers (B,D,E) (approved)	29,500					
To balance c/d (R) (pending approval)	28,000					
Total	99,500	Total	99,500			

2. Q A/c

Particulars	₹	Particulars	₹
To Sale or Return (Sale on Approval Made)	25,000	By Sale or Return (Goods Returned)	25,000
Total	25,000	Total	25,000