Chapter 3
Inventory

Objectives

After completing this chapter, you should be able to:

- Activate the Inventory function (page 47).
- Set up Inventory Items in the Item list (page 48).
- Use QuickBooks to calculate the average cost of inventory (page 53).
- Record sales of Inventory using sales forms (page 54).
- View the accounting entries behind the scenes of inventory sales using the Transaction Journal report (page 54).
- Use purchase orders to order inventory (page 55).
- Receive against purchase orders (page 57).
- Adjust your inventory (page 68).
- Create Inventory Assembly Items and Build Assemblies (page 71).
- Create reports about inventory (page 74).

Restore this File

This chapter uses Chapter 6.QBW. To open this file, restore the Chapter 6.QBB file to your hard disk. See page 98 for instructions on restoring files.

In this chapter, you’ll learn how to set up and manage your inventory in QuickBooks.

QuickBooks Tools for Tracking Inventory

The Vendor Navigator shows a graphical representation of the steps involved in managing inventory. The Vendor Navigator (see Figure 3-1) is already showing on the screen in your sample file.
Table 3-1 shows an overview of the accounting behind the scenes for different business transactions that involve inventory. Familiarize yourself with this table, and refer to it when you encounter business transactions involving inventory.

<table>
<thead>
<tr>
<th>Business Transaction</th>
<th>QuickBooks Transaction</th>
<th>Accounting Entry</th>
<th>Comments</th>
</tr>
</thead>
<tbody>
<tr>
<td>Purchasing Inventory with Purchase Orders</td>
<td>Purchase Orders</td>
<td>Non-posting entry used to record Purchase Orders.</td>
<td>You don’t have to use purchase orders. If you do, QuickBooks tracks the status of your orders and matches them with the bill from your vendor.</td>
</tr>
<tr>
<td>Receiving Inventory (no Bill from Vendor)</td>
<td>Receive Items</td>
<td>Increase (debit) Inventory, increase (credit) Accounts Payable. Increase inventory counts for each item received.</td>
<td>Use this transaction when you receive inventory items that are not accompanied by a bill. This transaction enters an item receipt in the Accounts Payable account. Although it increases A/P, no bill shows in the Pay Bills window.</td>
</tr>
<tr>
<td>Receiving Inventory (with Bill from Vendor)</td>
<td>Receive Items with Bill</td>
<td>Increase (debit) Inventory, increase (credit) Accounts Payable. Increase inventory counts for each item received.</td>
<td>Use this transaction when you receive inventory accompanied by a Bill from the vendor.</td>
</tr>
<tr>
<td>Entering a Bill for Previously Received Inventory Items</td>
<td>Receive Bill</td>
<td>No change in debits and credits. This transaction only changes an Item Receipt transaction into a bill.</td>
<td>When an item receipt is turned into a bill, QuickBooks shows the bill in the Pay Bills window.</td>
</tr>
<tr>
<td>Purchase Inventory with Check or Cash</td>
<td>Checks</td>
<td>Increase (debit) Inventory, decrease (credit) Checking.</td>
<td>Use this transaction when you buy inventory with a check. If you use cash to buy inventory, use the Write Checks window of a Petty Cash account.</td>
</tr>
<tr>
<td>Purchase Inventory with Credit Card</td>
<td>Credit Card Changes</td>
<td>Increase (debit) Inventory, increase (credit) Credit Card Liability.</td>
<td>Use this transaction if you use a credit card to purchase inventory and you track that credit card with a Credit Card account.</td>
</tr>
<tr>
<td>Build Inventory assemblies from individual parts</td>
<td>Build Assemblies</td>
<td>Reduce inventory on hand for each component item, and increase inventory on hand for the assembly item. No net effect on total inventory dollar balance.</td>
<td>Use this transaction to record the assembly of component parts into a finished assembly.</td>
</tr>
</tbody>
</table>

Table 3-1 Summary of inventory transactions
Tracking Inventory with QuickBooks

When you use Inventory Part Items to track your inventory, QuickBooks handles all the accounting for you automatically, according to how you set up your Inventory Part Items in the Item list. QuickBooks keeps a perpetual inventory, meaning that every purchase and every sale of inventory immediately updates all your account balances and reports.

When QuickBooks calculates the cost of inventory, it uses the average cost method, explained on page 53. QuickBooks does not support the first-in, first-out (FIFO) or last-in, first-out (LIFO) methods.

Key Term: Perpetual Inventory
QuickBooks keeps a continuous record of increases, decreases, and balance on hand of inventory items.

Key Term: Average Cost
Inventory cost method that divides the cost of inventory by the number of units in stock. It is most appropriate when prices paid for inventory do not vary significantly over time, and when inventory turnover is high. QuickBooks calculates the cost of inventory using this method.

The average cost method is most appropriate when the price paid for inventory does not vary significantly over time, and when inventory turnover is high (i.e., products sell through quickly).

In order to keep your inventory system working smoothly, it is critical that you use Inventory Parts Items on all transactions involving inventory. This means you must use the Items tab on every purchase transaction that involves inventory part Items. Figure 3-2 illustrates the QuickBooks Inventory process.

DO NOT ENTER THIS BILL NOW. IT IS FOR REFERENCE ONLY.

Activating the Inventory Function

The first step in using QuickBooks for inventory is to activate Inventory in your company Preferences.

Computer Practice

Step 1. Select the Edit menu and then select Preferences.

Step 2. Scroll down in the Preferences window and click on Purchases & Vendors.
Step 3. Click the Company Preferences tab.

Step 4. Make sure that the box next to *Inventory and purchase orders are active* is checked (see Figure 3-3). Click OK.

**Note:**
When inventory is activated, Purchase Orders are also activated. However, you are not required to use Purchase Orders when tracking inventory.

After you activate the Inventory function, the Item list shows a new Item type called *Inventory Part*. The first time you create an Inventory Part Item in the Item list, QuickBooks automatically creates two accounts in your Chart of Accounts: An *Other Current Asset* account called *Inventory Asset* and a *Cost of Goods Sold* account called *Cost of Goods Sold*.

QuickBooks uses these two important accounts to track inventory (see Table 3-2). The Inventory Asset account holds the value of your inventory until you sell it. The Cost of Goods Sold account records the cost of the inventory when you sell it.

<table>
<thead>
<tr>
<th>Accounts for Tracking Inventory</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Inventory Asset</strong></td>
</tr>
<tr>
<td><strong>Cost of Goods Sold</strong></td>
</tr>
</tbody>
</table>

Table 3-2 Two accounts track inventory

**Setting up Inventory Items**

To set up an inventory part in the Item list, follow these steps:

**COMPUTER PRACTICE**
Step 1. Select the Lists menu and then select Item List. Alternatively, click Items & Services on the Vendor navigator.

Step 2. Select the Item menu at the bottom of the list and then select New. Alternatively, press CTRL+N.

Step 3. Select Inventory Part from the Type drop-down list (see Figure 3-4). Then press TAB.

Step 4. Enter 106-Slider in the Item Name/Number field and then press TAB.

You might want to give each item in your inventory a part number, and then use the part numbers in the Item Name/Number field.

Step 5. Skip the Subitem of field by pressing TAB.

This field allows you to create subitems of items. If you use subitems, the Sales by Item reports and graphs will show totals for all sales and costs of the subitems.

**Key Term:** Subitems These help you to organize the Item list. Use subitems to group and subtotal information about similar products or services in sales reports and graphs.

Step 6. Enter 12 ft. Sliding Door – Wood Frame in the Description on Purchase Transactions field and then press TAB.

The description you enter here appears as the default description when you use this Item on purchase orders and bills.

![Figure 3-4 The completed New Item window](image)

Step 7. Enter 350.00 in the Cost field, and then press TAB.

Use this field to track the price you pay to your vendor for the item. QuickBooks takes this amount as the default price when you enter this Item on purchase orders and bills. If the price
changes, you can override the amount on the purchase orders and bills or you can edit the amount here.

Step 8. In the COGS Account field Cost of Goods Sold is already selected. Press TAB.

QuickBooks uses the Cost of Goods Account to record the average cost of this item when you sell it. For more information on average cost, see page 53.

Step 9. Select Ace Glass from the Preferred Vendor drop-down list and then press TAB.

The Preferred Vendor field is used to associate the item with the vendor from whom you normally purchase this part. It’s an optional field and you can leave it blank without compromising the integrity of the system.

Step 10. Press TAB to leave the Description on Sales Transactions field unchanged. The text in this field defaults to whatever you entered in the Description on Purchase Transactions field.

QuickBooks allows you to have two descriptions for this Item: one for purchase forms and one for sales forms. You can use your vendor’s description when purchasing the item and a more customer-oriented description on your sales forms.

Step 11. Press TAB to accept the already selected sales price of 420.00 in the Sales Price field.

The Sales Price field automatically calculates a price based on the cost of the item plus the markup percentage entered in the company preferences. To modify this markup percentage, go to the company preferences for sales and customers.

The Sales Price field is where you enter how much you normally charge your customers for the Item. If the price changes, you can override it on sales forms.

Step 12. The Tax Tax Code is already selected. Press TAB.

Tax Codes determine the default taxable status of the Item. Since the Tax Code called Tax is taxable, QuickBooks calculates sales tax on this Item when it appears on sales forms. You can override the default Tax Code on each sales form. For more information on Sales Tax Codes see page 30.

Step 13. Select Product Sales from the Income Account drop-down list. Press TAB.

Choose the income account to which you want to post sales of this Item.

Step 14. In the Asset Account field, Inventory Asset is already selected. Press TAB.

The Inventory Asset account is the account that tracks the cost of your inventoried products between the time you purchase them and the time you sell them.
The accounting behind the scenes:
When you purchase inventory, QuickBooks increases (debits) the Inventory Asset account by the amount of the purchase price. When you sell inventory, QuickBooks decreases (credits) the Inventory Asset account and increases (debits) the Cost of Goods Sold account for the average cost of that item at the time it is sold. For details on how QuickBooks calculates average cost, see page 53.

Step 15. Enter 5 in the Reorder Point field and then press TAB (see Figure 3-5).

The QuickBooks Reminders list reminds you when it’s time to reorder inventory items based on the Reorder Point.

Step 16. Leave the Qty on Hand, Total Value, and As of fields unchanged.

Note:
Don’t enter the On Hand, Total Value and As of fields. The Qty on Hand, Total Value, and As of fields are intended for use during the initial setup of the data file.

The accounting behind the scenes: If you enter a quantity and value in this window, QuickBooks increases (debits) Inventory for the total value, and increases (credits) Opening Bal Equity.

However, even if you are setting up the data file it is better to leave the Qty on Hand and Total Value fields set to zero when you set up the item. Then, as you’ll see later in the chapter, use a single inventory adjustment transaction to set up the quantity and value on hand for all the inventory items.

Step 17. Click OK to save the new Item.
Tip:
Before setting up inventory, think about what products you’ll track as Inventory Parts. It may not be necessary for you to separately track every product you sell as an Inventory Part. If you don’t need detailed reports and inventory status information about certain products you sell, consider using Non-inventory Part items to track those products. In general, use Inventory Part items only when you really need to track the stock status of a product.

Setting up Group Items

Sometimes, you sell items in bundles. For example, every time Academy Glass sells a 106-Slider Item, they also install that window. Therefore, they sell the labor along with the window. Academy Glass uses Group Items to bundle products and/or services on sales forms.

**Computer Practice**

Step 1. The Item list should still be open on your screen. If not, Select the Lists menu and then select Item List or click Items & Services on the Vendor navigator.

Step 2. Select the Item menu at the bottom of the Item list and then select New. Alternatively, press CTRL+N.

Step 3. Select Group from the Type drop-down list and then press TAB.

Step 4. Enter 106 Replace in the Group Name/Number field and then press TAB.

Step 5. Enter Remove and Replace 106-Slider in the Description field, and press TAB.

Step 6. Click the Print items in group box (see Figure 3-6). Press TAB.

The Print items in group box controls whether the items in the group will print on sales forms. You’ll always see the items in this group on the screen version of the sales form, but the printed form shows the detail only if this box is checked.

Step 7. On the first line at the bottom of the window, select 106-Slider from the Item drop-down list. Press TAB.

Step 8. Enter 1 in the Qty column and then press TAB.

The Qty column indicates how many of each item is included in the group.

Step 9. On the second line at the bottom of the window, select Labor from the Item drop-down list. Press TAB.

Step 10. Enter 8 in the Qty column. Press TAB.
Figure 3-6 Specify items in the group and whether to print items on the sales form.

Note:
The New Item window in Figure 3-6 does not include a Sales Price field. When you enter a Group item on sales forms, QuickBooks uses the sales prices of the Items within the group to calculate a total price for the group. You can override the price of each item within the group directly on the sales form.

Step 11. Click OK to save the Group Item and then close all open windows.

Average Cost of Inventory

When you use an inventory Item on a purchase form (e.g., a Bill), QuickBooks increases (Debits) the Inventory Asset account for the actual cost of the inventory purchase. At the same time, it recalculates the average cost of all Items in inventory.

When you use an inventory Item on a sales form (e.g., an Invoice), QuickBooks increases (debits) Cost of Goods Sold and decreases (credits) Inventory Asset for the average cost of the items.

Table 3-3 shows how QuickBooks calculates the average cost of inventory Items.

<table>
<thead>
<tr>
<th>Situation/Transaction</th>
<th>Calculation</th>
</tr>
</thead>
<tbody>
<tr>
<td>You have ten 104-Sliders in stock. Each originally costs $300.</td>
<td>10 units × $300 per unit = $3,000 total cost</td>
</tr>
<tr>
<td>You buy three new 104-Sliders at $325 each.</td>
<td>3 units × $325 per unit = $975 cost</td>
</tr>
<tr>
<td>The combined cost in inventory.</td>
<td>$3,000 + $975 = $3,975</td>
</tr>
<tr>
<td>The average cost per unit is equal to the total cost of inventory divided by the total units in inventory.</td>
<td>total cost/total units = average cost/unit</td>
</tr>
<tr>
<td></td>
<td>$3,975 / 13 = $305.77 avg. cost/unit</td>
</tr>
</tbody>
</table>

Table 3-3 QuickBooks calculates the average cost of inventory items.

Each time you sell inventory Items, the average cost per unit is multiplied by the number of units sold. Then this amount is deducted from the Inventory Asset account and added to the Cost of Goods Sold account.
Invoicing for Inventory Items

Selling Inventory Items Using an Invoice Form

When you sell inventory, always use an Invoice or a Sales Receipt to record the sale. This ensures that QuickBooks updates your inventory records and your financial reports at the same time.

**Computer Practice**

Step 1. Enter the Invoice as shown in Figure 3-7, recording a sale of two 104-Sliders.

![Invoice Image]

Step 2. Click Save & New to save the Invoice.

Creating a Transaction Journal Report

To see how this Invoice affects the General Ledger, use a Transaction Journal report.

**Computer Practice**

Step 1. Display the invoice shown in Figure 3-7.

Step 2. Select the Reports menu and then select Transaction Journal (or press CTRL+Y).
Figure 3-8 Transaction Journal report

The accounting behind the scenes:
When you sell an inventory part, QuickBooks increases (credits) the income account defined for the item sold on the Invoice or Sales Receipt form. The Transaction Journal report (Figure 3-8) shows the accounting behind the scenes of the invoice. You can use the Transaction Journal report to see the accounting behind any QuickBooks transaction.

Step 3. If you want to see the Transaction Journal in debit and credit format, click Modify Report. Then uncheck the Amount column and check the Debit and Credit columns in the columns section.

Step 4. Close the report by clicking the close box (X) in the upper right corner.

Purchase Orders

Use Purchase Orders to track inventory purchases, and to easily determine which items you have on order.

If you use purchase orders, you’ll be able to create reports that show what is on order and when it is due to arrive from your supplier. In addition, you can create a list of open purchase orders.

Purchase orders do not post to the Chart of Accounts. However, QuickBooks tracks Purchase Orders in a non-posting account called Purchase Orders. You can see this account at the bottom of your Chart of Accounts.

Using Reminders for Inventory

Because you sold two 104-Sliders and inventory fell below five units, QuickBooks reminds you that it’s time to reorder.

Computer Practice

Step 1. Select the Company menu and then select Reminders (see Figure 3-9).

Step 2. Double-click on the Inventory to Reorder line.
Creating a Purchase Order

Create a Purchase Order to reorder inventory, filling out each item and quantity.

Note:
Since Purchase Orders are non-posting, QuickBooks does not include them on the Reminders or Pay Bills windows.

**COMPUTER PRACTICE**

Step 1. Select the Vendors menu and then select Create Purchase Orders (see Figure 3-10).
Step 2. Select Ace Glass from the Vendor drop-down list or type the name into the Vendor field. Press TAB.
Step 3. Enter Walnut Creek in the Class field. Press TAB.
Step 4. Press TAB three times to leave the Ship To field blank and to accept Custom Purchase Order as the default form template.

If you want the order shipped directly to one of your customers, enter the customer’s information in the Ship To field. By default, QuickBooks enters your company’s address from the Company Information window. To change your Ship To address, you could override it here or select the Company menu and then select Company Information. Then click the Ship to Address button.

Step 5. Enter 04/05/2004 in the Date field and then press TAB.
Step 6. Press TAB to accept the default Purchase Order number of 2004–1002.

QuickBooks automatically numbers your Purchase Orders in the same way it numbers Invoices. It increases the number by one for each new purchase order. However, you can override this number if necessary.

Step 7. Press TAB twice to accept the default vendor address and ship-to address.

Step 8. Enter the 104-Slider and 106-Slider items in the body of the purchase order, as shown in Figure 3-10.

The Customer column allows you to associate your purchases with the customer or job to which you want to assign the expense for this purchase. Since you’re purchasing inventory, you don’t know the customer information, so don’t use this column.

Step 9. Enter Reorder sliders in the Memo field and then press TAB.

Step 10. Click the Print icon to print the purchase order on blank paper.

Step 11. When you have finished printing the purchase order, click Save & Close to save.

Receiving Inventory

There are several ways to record the receipt of inventory in QuickBooks. How you record the receipts depends on when you receive the inventory and how you intend to pay for it.

You have two options for receiving inventory:

1. You could pay for items at the time you receive them. For example, you may be at your vendor’s store and write a check or charge your credit card for the items. In this case, you’ll use Write Checks or Enter Credit Card Charges to record your receipt of inventory.
2. Alternatively, you could use the inventory ordering and receiving process displayed in Figure 3-11. If you choose this method for processing inventory, you will issue a purchase order and later receive part or all of the order. If the bill doesn’t accompany the shipment, use the **Receive Items** function. When the bill comes, use the **Enter Bill for Received Items** function. If you receive the bill when you receive the order, use the **Receive Items with Bill** function.

![Vendor Navigator](image)

*Figure 3-11 The Vendor Navigator Includes a Flowchart for Ordering and Receiving Inventory*

The **Receive Items** and the **Receive Items with Bill** functions both record transactions that are connected to **Purchase Orders**. This connection is used by QuickBooks to track whether a purchase order is open or not.

**Purchasing Inventory at a Retail Store with Check or Credit Card**

If you buy inventory at a retail store, use the **Write Checks** or **Enter Credit Card Charges** functions to record the purchase. Record the purchased items using the **Items** tab at the bottom of the check or credit card charge window (see Figure 3-12).
Receiving Shipments against Purchase Orders

If you use Purchase Orders and you receive a shipment that is not accompanied by a Bill, follow these steps:

**COMPUTER PRACTICE**

1. Select the Vendors menu and then select **Receive Items**. Alternatively, click **Receive Items** on the Vendor navigator.
2. The Create Item Receipts window opens. Enter **Ace Glass** in the Vendor field (see Figure 3-13) and then press TAB.
Figure 3-13 The Create Item Receipts window

Step 3. Since there is an open **Purchase Order** for this vendor, QuickBooks displays the message in Figure 3-14. Click **Yes**.

Figure 3-14 QuickBooks displays an Open POs Exist message, if applicable

Step 4. Select the **Purchase Order** you’re receiving against from the list in Figure 3-15 by clicking in the √ column. Then click **OK**.

Figure 3-15 Open Purchase Orders window

All of the open POs for this vendor show here. If you are receiving against more than one PO, you must enter a separate receipt for each PO.
Step 5. QuickBooks fills in the Item Receipt with the information from the Purchase Order as shown in Figure 3-16.

Step 6. Enter 04/05/2004 in the Date field. Press TAB twice.

Step 7. Enter 4431 in the Ref. No. field (see Figure 3-17).

In the Ref. No. field you enter the shipper number on the packing slip that accompanies the shipment. This helps you match the receipt with the vendor’s bill when you receive it.

Step 8. Tab to the Qty column. Change the quantity to 4 for the 104-Slider, and to 3 for the 106-Slider (see Figure 3-17).

Do not worry about the Cost column. You haven’t received the bill yet, so QuickBooks uses the amounts you entered on the Purchase Order. When you get the actual bill for this shipment, you’ll correct or adjust the Cost column if necessary.
Step 9. To save the Item Receipt, click Save & Close.

The accounting behind the scenes:
When you record an Item Receipt, QuickBooks increases (credits) Accounts Payable for the total amount of the Item Receipt. It also increases (debits) Inventory for the same amount.

However, since you haven’t received the bill, your Pay Bills window will not yet show the bill, even though the balance in Accounts Payable was increased by the Item Receipt. This may seem strange at first because you normally expect the total in Pay Bills to match the balance in Accounts Payable. However, Item Receipts never show in the Pay Bills window.

It turns out that Item Receipts and Bills are exactly the same transaction. The only difference is that the Bill Received box is not checked on Item Receipts, and it is checked on Bills.

Creating Open Purchase Orders Reports

Computer Practice
Step 1. Select the Reports menu, select Purchases, and then select Open Purchase Orders.

This report (see Figure 3-18) shows the total dollar amount for all open purchase orders, not just the open balance of each Purchase Order. To see the open balance on a Purchase Order, double-click on it from this report.

Checking Purchase Order Status

To check the status of a purchase order or to change or cancel it, edit the purchase order directly.

Computer Practice
Step 1. Display the Purchase Order by double-clicking on it from the Open Purchase Orders report shown in Figure 3-18. Alternatively, you can also display a Purchase Order by clicking PO List on the Vendor navigator.
Step 2. Review the quantity of each Item in the Rcv’d column.

On the Purchase Order in Figure 3-19, you can see that Academy Glass has received four 104-Sliders and three 106-Sliders.

If you know you won’t be receiving items on a Purchase Order, you can close specific line items or close the whole order. To close any line of the order, click in the Clsd column. To close the whole order and cancel the rest of the order, click the Closed box at the bottom of the form. If you cancel an order, don’t forget to notify your vendor.

Step 3. Close the window without making any changes to the purchase order.

**Entering the Final Shipment**

When the final shipment arrives, enter another Item Receipt.

**Computer Practice**

Step 1. Select the Vendors menu and then select Receive Items. Alternatively, click Receive Items on the Vendor navigator.

Step 2. The Create Item Receipts window opens.

Step 3. Enter Ace Glass in the Vendor field and then press TAB (see Figure 3-20).
Step 4. Because there is an open **Purchase Order** for this vendor, QuickBooks displays the message shown in Figure 3-21. Click **Yes**.

![Figure 3-21 The Open PO's Exist window appears](image)

Step 5. Select the **Purchase Order** you’re receiving against from the list (see Figure 3-22) and then click **OK**.

![Figure 3-22 Open Purchase Orders window](image)

Step 6. QuickBooks automatically fills in the item receipt with the information from the purchase order.

Step 7. Enter **04/05/2004** in the **Date** field.
Step 8. Enter 4441 in the Ref. No. field (see Figure 3-23).

Step 9. Click Save & Close to record the receipt.

**Entering Bills for Received Inventory**

Now that you’ve recorded Item Receipts for your inventory shipments, the next step in the process is to record the Bills when they arrive from the vendor.

**Converting an Item Receipt into a Bill**

**COMPUTER PRACTICE**

Step 1. Select the Vendors menu and then select Enter Bill for Received Items. Alternatively, click Receive Bill on the Vendor navigator.

Step 2. Enter Ace Glass in the Vendor field and then press TAB.

Step 3. Select the first line on the window shown in Figure 3-24. Click OK.
Step 4. QuickBooks displays the Item Receipt and automatically checks the Bill Received box (see Figure 3-25). Checking the Bill Received box converts the Item Receipt into a Bill. Verify that the Bill matches your records and make changes to price, terms, due date, or any other field that doesn’t match the vendor’s bill.

**Note:** QuickBooks doesn’t add a new transaction when you use the Enter Bill for Received Items function. That’s because you’ve already recorded an Item Receipt, which increases Inventory and Accounts Payable. This function simply converts your Item Receipt into a Bill.

Step 5. Click Save & Close to record the Bill.

Step 6. Click Yes when you see the Recording Transaction message.

Step 7. Repeat Step 1 through Step 6 for Item Receipt #4441 and accept the defaults for all quantities and amounts.

**Handling Overshipments**

If your vendor ships more than you ordered on a Purchase Order, you have three choices.

1. You could refuse the extra shipment and send it back to the vendor without recording anything in QuickBooks.
2. You could receive the extra shipment into inventory and keep it (and pay for it).
3. Or, you could receive the extra shipment into inventory, and then send it back and record a Bill Credit in QuickBooks.

**If you keep the overshipment (and pay for it):**

**DO NOT PERFORM THESE STEPS NOW. THEY ARE FOR REFERENCE ONLY.**

1. Override the number in the Qty column on the Item Receipt so that it exceeds the quantity on your Purchase Order. This increases the Inventory Asset and Accounts Payable accounts for the total amount of the shipment, including the overshipment.
2. When the bill arrives from the vendor, match it with the Item Receipt and pay the amount actually due. Unless you edit the Purchase Order, it will not match the Item Receipt or Bill. This may be important later when you look at Purchase Orders and actual purchase costs, so consider updating your Purchase Order to match the actual costs.

If you send the overshipment back after receiving it into inventory:

**DO NOT PERFORM THESE STEPS NOW. THEY ARE FOR REFERENCE ONLY.**

3. Override the number in the Qty column on the Item Receipt so that it exceeds the quantity on your Purchase Order. This increases the Inventory Asset and Accounts Payable accounts for the total amount of the shipment, including the overshipment.

4. When you return the excess items, create a Bill Credit for the vendor. On the Bill Credit, enter the quantity returned and the cost for each item.

5. If you receive a refund from the vendor, record the refund as explained in the expenses chapter.

6. To apply the Bill Credit to an unpaid bill for that vendor, use the Pay Bills window.

**Handling Vendor Overcharges**

If you have a discrepancy between your purchase order and the vendor's bill, there are several ways to handle it.

If the vendor overcharged you, the vendor might agree to revise the bill and send you a new one. In this case, wait for the new bill before recording anything in QuickBooks.

On the other hand, you might decide to pay the incorrect bill and have the vendor adjust the next bill. In that case, use the Expenses tab on the Bill to track the error.

In this example, assume you were overcharged by $48.00.

**Computer Practice**

Step 1. Select the Vendors menu and then select Enter Bills. Alternatively, click Enter Bills on the Vendor navigator.

Step 2. Click Previous on the Enter Bills window to display Bill #4441.

Step 3. Select the Expenses tab to record a $48.00 overcharge from the vendor. Use the Cost of Goods Sold account and the Overhead class to track the overcharge.

Step 4. Click Recalculate to update the Amount Due field (see Figure 3-26).
Step 5. Click Save & Close. Click Yes on the Recording Transaction message window.

Since the Bill in Figure 3-26 is $48.00 too much, contact the vendor to discuss the overage on the bill. The vendor will either issue you a Credit or, if you have already paid the bill, a refund check. The vendor may also apply the overpayment to your account – to be applied to a future bill.

Depending on the vendor’s action, do one of the following:

- If the vendor refunds your money, add the refund directly onto your next deposit. Code the deposit to the Cost of Goods Sold account and the Overhead class (the account and class you used when you recorded the overage on the bill).
- If the vendor sends you a credit memo, enter a Bill Credit. Code the Bill Credit to the Cost of Goods Sold account and Overhead class (the account and class you used when you recorded the overage on the bill).

**Note:** Always use the same account when you record the overcharge and the refund or credit. In the example above, the Expenses tab of the Bill for Ace Glass increases Cost of Goods Sold by $48.00 and the deposit or credit from the vendor reduces Cost of Goods Sold by the same amount. Alternatively, you could use an Other Current Asset account called something like Due from Vendors.

### Adjusting Inventory

QuickBooks automatically adjusts inventory each time you purchase or sell inventory Items. However, it may be necessary to manually adjust inventory after a physical count of your inventory, or in case of an increase or decrease in the value of your inventory on hand. For example, you might decrease the value of your inventory if it has lost value due to new technology trends.
Adjusting the Quantity of Inventory on Hand

**COMPUTER PRACTICE**

Step 1. Select the Vendors menu, select Inventory Activities, and then select Adjust Quantity/Value on Hand (see Figure 3-27). Alternatively, click Adjust Qty on Hand in the Vendor navigator.

Step 2. Enter 04/30/2004 in the Adjustment Date field and then press TAB.

Step 3. Enter 2004–1 in the Ref. No. field and then press TAB.

Step 4. Enter Inventory Variance in the Adjustment Account field and then press TAB.

QuickBooks adjusts the account you enter into the Adjustment Account field to offset the change in the Inventory Asset account balance. In this example, we’re using Inventory Variance, an expense account, but you can use whatever account is best for your records.

**Figure 3-27 Adjust Quantity/Value on Hand window**

Step 5. Skip to the New Qty column. Enter 7 on the 104-Slider line and then press TAB.

Notice that QuickBooks calculates the quantity difference (-1) in the Qty Difference column. Also, notice that QuickBooks automatically calculates the Total Value of Adjustment in the bottom right corner. QuickBooks uses the average cost method to calculate this value. Look at the Inventory Valuation Detail report later in this chapter to see how the average cost changes each time you purchase or adjust inventory in this way.

Step 6. Enter Adjust Inventory for physical counts in the Memo field.

Step 7. To save the adjustment, click Save & New.
Adjusting the Value of Inventory

**Computer Practice**

With the Adjust Quantity/Value on Hand window displayed, follow these steps to record a value adjustment to your inventory.

**Step 1.** At the bottom left of the Adjust Quantity/Value on Hand window, click the Value Adjustment box (see Figure 3-28).

**Step 2.** Confirm that **04/30/2004** is already selected in the Adjustment Date field. Press TAB.

**Step 3.** Enter **2004-2** in the Ref. No. field. Press TAB.

**Step 4.** Confirm that Inventory Variance is already selected in the Adjustment Account field.

**Step 5.** Enter **1,800.00** in the New Value column on the 106-Slider line and then press TAB.

Notice that QuickBooks calculates the Total Value of Adjustment.

**Step 6.** Click Save & Close to save the adjustment.

QuickBooks will post the amount of this adjustment ($1,800) to the General Ledger. Since this adjustment lowers the value of the 106-Sliders, it reduces the average cost of each unit on hand. Therefore, the next time you sell a 106-Slider, QuickBooks will transfer the new (lower) average cost out of Inventory and into Cost of Goods Sold.
The accounting behind the scenes:
Inventory adjustments always affect your **Inventory Asset** account. If the **Total Value of Adjustment** is a positive number, the **Inventory** account increases (debit) by that amount and the **Adjustment Account** decreases (credit). If the **Total Value of Adjustment** is a negative number, the debits and the credits are reversed.

**Inventory Assemblies**

**Note:**
This feature is only available in QuickBooks Premier. If you are not using the Premier edition, skip this section.

If you build or assemble items from raw materials, you can create an **Inventory Assembly Item** in QuickBooks to track your assembled inventory. An **Inventory Assembly** is defined by specifying which components (must be inventory items) are needed to produce it. Essentially, you define the **Bill of Materials** for each **Inventory Assembly** item when you set up the item.

When you “build assemblies” from **Inventory Items** into **Assembly Items**, QuickBooks automatically adjusts the quantities and values on hand of the inventory items (components) and the assemblies (finished goods).

**COMPUTER PRACTICE**

Step 1. Select the **Lists** menu and then select **Item List**. Alternatively, click **Items & Services** on the **Vendor** navigator.

Step 2. Select the **Item** menu at the bottom left of the **Item List** and then select **New** (or type **CTRL+N**).

Step 3. Select **Inventory Assembly** from the **Type** drop-down list and then press **TAB**.

![Figure 3-29 Creating an Inventory Assembly item](image)
An Inventory Assembly Item is similar to a Group Item. However, unlike a Group item it can only include other Inventory Part items in the Components Needed list. By creating an Assembly item, you are describing what individual inventory items (components) are used to make up the finished goods item (assembly).

**Step 4.** Enter **104-Slider 4-pane** in the Item Name/Number field. Press TAB three times to advance to the COGS Account field.

When you sell the assembled inventory product (i.e., finished goods), select this Item name from the Item column on sales forms.

**Step 5.** Cost of Goods Sold is already selected from the COGS Account drop-down list. Press TAB.

QuickBooks increases (debts) the account you enter in this field when you use this item on Invoices and Sales Receipts.

**Step 6.** Enter **10 ft. Slider - Wood Frame - with 4-pane grids and screen** in the Description field and then press TAB.

On sales forms, QuickBooks will enter this description by default. Unlike Group items, QuickBooks will not display the descriptions of the component items.

**Step 7.** Enter **559.00** in the Sales Price field and then press TAB.

**Step 8.** Tax in the Tax Code field is already selected. Press TAB.

**Step 9.** Select Product Sales from the Income Account drop-down list and then press TAB.

**Step 10.** Enter the items and quantities on the Components Needed section as shown in Figure 3-29. Press TAB.

List all of the items you will need to create the 104-Slider 4-Pane Assembly Item (i.e., finished goods).

**Step 11.** Inventory Asset in the Asset Account field is pre-selected. Press TAB.

QuickBooks increases (debts) the account you enter in this field when you record a Build Assembly transaction.

**Step 12.** Enter **5** in the Build Point field and then press TAB.

QuickBooks will remind you to build more of the Assembly Item if your quantity on hand drops below 5.

**Step 13.** Click OK to save the Assembly Item.

On an ongoing basis, you will create 104-Slider 4-pane products using one 104-Slider, two 4-Pane Grids and one Screen-104. When you finish assembling the items, you must record a Build Assembly transaction to tell QuickBooks that you’ve built the items.

**Computer Practice**

**Step 1.** Select the Vendors menu, select Inventory Activities, and then select Build Assemblies. Alternatively, click Build Assemblies on the Vendor navigator.
Step 2. Select 104-Slider 4-pane from the Assembly Item drop-down list and then press TAB.

Step 3. Enter 2 in the Quantity to Build field and then press TAB.

Step 4. Confirm that 04/30/2004 is in the Date field and then press TAB.

Step 5. Enter 2004-1 in the Build Ref. No. field and then press TAB.

Step 6. Enter Build 104-Slider 4-pane windows in the Memo field.

Step 7. Click Build and Close to record the transaction.

After you build assemblies, QuickBooks adjusts the quantity on hand of each component as well as the assembly.

Step 8. To see the adjustment created by the Build Assembly transaction, select the Reports menu, select Inventory, and then select Inventory Valuation Detail.

Step 9. Enter 04/30/2004 in the From and To fields as shown in Figure 3-31. The Inventory Valuation Detail report shows the component items being used to build the assembly items.
Inventory–Inventory Reports

Figure 3-31 Inventory Valuation Detail report showing the building of component items into an assembly

Inventory Reports

QuickBooks provides several reports for inventory analysis, all of which are customizable in ways similar to other reports.

For daily management of inventory, use the Stock Status by Item report, the Stock Status by Vendor report, or the Inventory Valuation Summary report. These reports give a quick overview of inventory counts, inventory values, and pending orders.

For detailed research about transactions involving Inventory, use the Inventory Item QuickReport or the Inventory Valuation Detail report.

Inventory Item QuickReport

The Inventory Item QuickReport is useful for seeing all transactions involving an Inventory Item.

**Computer Practice**

Step 1. Select the Lists menu and then select Item List.

Step 2. Click on the 104-Slider item to select it.

Step 3. Select the Reports menu at the bottom of the Item list and then select QuickReport: 104-Slider. Alternatively, press CTRL+Q.

Step 4. Set the From date to 01/01/2004 and the To date to 04/30/2004. Press TAB (see Figure 3-32).

Step 5. Close the report by clicking the close box (x) in the upper right corner of the window.
Chapter 3

Inventory–Inventory Reports

Figure 3-32 Inventory Item QuickReport

Another Way:
You can also close reports (and most other windows) in QuickBooks by pressing ESC.

Inventory Stock Status by Item Report

The Stock Status by Item report is useful for getting a quick snapshot of each inventory part, and the number of units on hand and on order. In addition, this report gives you information about your inventory turnover, showing a column for sales per week.

**COMPUTER PRACTICE**

Step 1. Select the Reports menu, select Inventory, and then select Inventory Stock Status by Item.

Step 2. Set the From date to 01/01/2004 and the To date to 04/30/2004. Press TAB (see Figure 3-33).

Figure 3-33 Inventory Stock Status by Item report

Step 3. To close the report, click the close box (🗐) at the top right corner of the window.

Inventory Stock Status by Vendor Report

The Stock Status by Vendor report gives you information about your inventory parts, including how many are on hand, and how many are on order. This report is sorted by the Preferred Vendor field in the item.

**COMPUTER PRACTICE**

Step 1. Select the Reports menu, select Inventory, and then select Inventory Stock Status by Vendor.
Step 2. Set the From date to 01/01/2004 and the To date to 04/30/2004. Press TAB (see Figure 3-34).

Step 3. To close the report, click the close box (X) at the top right corner of the window. Click No if you are prompted to memorize the report.

Inventory Valuation Summary Report

The Valuation Summary report gives you information about the value of your inventory Items on a certain date. This report shows each item in inventory, the quantity on-hand, the average cost, and the retail value of each item.

Computer Practice

Step 1. Select the Reports menu, select Inventory, and then select Inventory Valuation Summary.

Step 2. Set the Date field to 04/30/2004 and then press TAB (see Figure 3-35).

Step 3. To close the report, click the close box (X) at the top right corner of the window.

Inventory Valuation Detail Report

The Inventory Valuation Detail report gives you information about the value of your inventory Items over a date range.

Computer Practice

Step 1. Select the Reports menu, select Inventory, and then select Inventory Valuation Detail.

Step 2. Set the Date fields to 01/01/2004 through 04/30/2004 and then press TAB (see Figure 3-36).
Figure 3-36 Inventory Valuation Detail report

Step 3. To close the report, click the close box (X) at the top right corner of the window.
Chapter Review

In this chapter, you learned about the QuickBooks Inventory function. You learned how to:

- Activate the Inventory function (page 47).
- Set up Inventory Items in the Item list (page 48).
- Use QuickBooks to calculate the average cost of inventory (page 53).
- Record sales of Inventory using sales forms (page 54).
- View the accounting entries behind the scenes of inventory sales using the Transaction Journal report (page 54).
- Use purchase orders to order inventory (page 55).
- Receive against purchase orders (page 57).
- Adjust your inventory (page 68).
- Create Inventory Assembly Items and Build Assemblies (page 71).
- Create reports about inventory (page 74).

It is crucial to think through your company’s information needs before tackling inventory. New users sometimes try to use inventory parts to track products they don’t really need to track in detail. Notice from the chapter examples that you must separately enter every purchase and sale for each inventory part. That might not seem like too much work at first, but if you have hundreds of small products with even a moderate turnover, you might overwhelm your bookkeeping system with detailed transactions.