

8 - Consignment Accounts

Nature of a Consignment

When a trader sells goods directly to customers, whether they are in his home country or overseas, these are ordinary sales. However, a trader may send goods to an agent to sell them for him. These goods are said to be sent on **consignment**. The main features are:

- (a) The trader sends the goods to the agent. The goods do not belong to the agent; his job is to sell them for the trader. The goods are owned by the trader until they are sold. The trader sending the goods is called the **consignor**. The agent is called the **consignee**.
- (b) The agent will store the goods until they are sold by him. He will have to pay some expenses, but these will later be refunded by the trader.
- (c) The agent will receive a commission from the trader for his work.
- (d) The agent will collect the money from the customers to whom he sells the goods. He will pay this over to the trader after deducting his expenses and commission. The statement from the agent to the trader showing this is known as the *account sales*.

Consignment accounts are to be found mainly in overseas trade.

Consignor's (the trader's) records

For each consignment to an agent a separate consignment account is opened. Think of it as a trading and profit and loss account for each consignment. The purpose is to calculate the net profit or loss on each consignment.

Goods consigned and expenses paid by the consignor

Double entry needed:

Goods consigned (a)	Debit consignment account
	Credit goods sent on consignment account
Expenses paid (b)	Debit consignment account
	Credit cash book

Expenses of the agent (consignee) and sales receipts

When the sales have been completed the consignee will send an account sales to the consignor. This will show:

	£	£
Sales		xxx
Less Expenses	xxx	
Commission	<u>xxx</u>	
Balance now paid		<u>xxx</u> <u>xxx</u>

The consignor enters these details in his books. The double entry needed is:

Sales (c):	Debit consignee's account
	Credit consignment account
Expenses of consignee (d):	Debit consignment account
	Credit consignee's account
Commission of consignee (e):	Debit consignment account
	Credit consignee's account
Cash received from consignee (f):	Debit cash
	Credit consignee's account

Consignee's (the agent's) records

The only items needed in the consignee's records will be found from the account sales he sent to the consignor after the goods have been sold.

He does not enter, in his double entry, the goods received on consignment. They never belong to him. His job is to sell the goods. Of course he will keep a note of the goods, but not in his double entry account records.

The double entry needed is:

Cash from sales of consignment (c)	Debit cash book Credit consignor's account
Payment of consignment expenses (d):	Debit consignor's account Credit cash book
Commission earned (e):	Debit consignor's account Credit profit and loss account
Cash to settle balance shown on account sales (f):	Debit consignor's account Credit cash book

Bad debts and consignments

Normally, when an agent sells the goods of the consignor he will collect the sale money from the customer. If the customer does not pay his account, the money in respect of this does not have to be paid by the agent to the consignor.

To make certain he does not have such bad debts, the consignor may pay an extra commission to the agent. When this happens the money for the debt will have to be paid by the agent even though he has not collected it. This extra commission is called *del credere commission*.

Consignor's accounting period and incomplete consignments

we have looked at consignments which were all sold by the agent before the financial year end of the consignor. For instance, if a consignor's account year ends annually on 31 December, all goods consigned in 19X7 will have been sold by 31 December 19X7.

Sometimes this will not be true. We could have sent goods to the agent in September 19X7, and the final sales may be in March 19X8. When the consignor prepares his final accounts up to 31 December 19X7, there will be an incomplete consignment at the date of the balance sheet.

Accounting for incomplete consignments

The main difference between a completed consignment at the balance sheet date and an uncompleted one is that the unsold stock has to be valued and carried down to the following period. This stock will appear in the balance sheet of the consignor as a current asset.

Advantages

- Consignee can save on inventory costs
- It allows a seller (manufacturer) to place merchandise in wholesale and retail outlets for additional exposure to the buying market
- It can provide an incentive for the wholesaler and retailer to stock goods in inventory because their capital is not tied up in inventory
- Reduces risk for new products or sales channels
- Helps nurture a better supplier / retailer relationship
- It provides the manufacturer with the opportunity to have the merchandise exposed to the buying market, instead of having it stored and isolated in a warehouse while waiting for an order from a buyer
- Cost effective method to expand business
- Manufacturers can sell the product even when there is no demand in their areas
- It can encourage wholesalers and retailers to stock seasonal or otherwise newly introduced merchandise which they might not usually buy because of a lack of demand

Disadvantages

- While your merchandise is being exposed on the shelves of a wholesaler or retailer, you get no money until they sell
- As the manufacturer you must have enough cash on hand to wait extended periods for payments of merchandise sold
- Since the goods are out of your physical control, you cannot control the damage and shopper abuse which inventory merchandise is generally subject to
- You cannot always affect shelving decisions which wholesalers and retailers make concerning maximum exposure of the merchandise
- Where personal selling is important, outright owned merchandise might be promoted over consigned goods because, again, return on investment matters where investment exists
- If the gross margin to the seller is greater than the percentage commission with the sale of consigned goods, then the seller might tend to favour selling the outright owned goods

Main points to remember

- 1 Goods sent to an agent on consignment continue to belong to the consignor until they are sold.
- 2 The consignee, or agent, sells the goods and collects the money due from customers.
- 3 The money collected is passed to the consignor after deduction of expenses and commission.

Exercises

Ex 1 On 8 February 19X8 PJ, a London trader, consigned 120 cases of goods to MB, an agent in New Zealand.

The cost of the goods was £25 a case. PJ paid carriage to the port £147 and insurance £93.

On 31 March 19X8 PJ received an *account sales* from MB, showing that 100 cases had been sold for £3,500 and MB had paid freight, at the rate of £2 a case, and port charges amounting to £186. MB was entitled to a commission of 5 per cent on sales. A *sight draft* for the net amount due was enclosed with the *account sales*.

You are required to show the accounts for the above transactions in the ledger of PJ and to show the transfer to profit and loss account at 31 March 19X8.

Ex 2 100 cases of goods costing £3,500 were sent on consignment by X Limited to Y Limited on 1 February 19X7. At the same time, X Limited paid delivery expenses of £100 and insurance of £20. On 1 March 19X7 an interim account sales was received from Y Limited showing that 80 cases had been sold for £63 each and that storage charges of £180 and selling expenses of £100 had been deducted from the account. After also deducting the commission on sales which was agreed at 5 per cent of the gross sales, Y Limited settled the balance due to X Limited for goods sold by a bank draft.

Required:

- (i) Prepare the interim account sales, and
- (ii) Prepare the consignment account in the books of X Limited.

Ex 3 On 15 November 19X8, Hughes consigned 300 cases of wooden items to Galvez of Madrid. On 31 December 19X8, Galvez forwarded an account sales, with a draft for the balance, showing the following transactions:

- 1 250 cases sold at £20 each and 50 at £18 each.
- 2 Port and duty charges £720.
- 3 Storage and carriage charges £410.
- 4 Commission on sales 5% + 1% del credere.

Required:

- (a) Prepare the account sales, and
- (b) Show the consignment inward account in the books of Galvez. Ignore interest.

Ex 4 Stone consigned goods to Rock on 1 January 19X8, their value being £12,000, and it was agreed that Rock should receive a commission of 5 per cent on gross sales. Expenses incurred by Stone for freight and insurance amount to £720. Stone's financial year ended on 31 March 19X8, and an account sales made up to that date was received from Rock. This showed that 70 per cent of the goods had been sold for £10,600 but that up to 31 March 19X8, only £8,600 had been received by Rock in respect of these sales. Expenses in connection with the goods consigned were shown as being £350, and it was also shown that £245 had been incurred in connection with the goods sold. With the account sales, Rock sent a sight draft for the balance shown to be due, and Stone incurred bank charges of £12 on 10 April 19X8, in cashing same.

Stone received a further account sales from Rock made up to 30 June 19X8, and this showed that the remainder of the goods had been sold for £4,800 and that £200 had been incurred by way of selling expenses. It also showed that all cash due had been received with the exception of a debt for £120 which had proved to be bad. A sight draft for the balance due was sent with the account sales and the bank charged Stone £9 on 1 July 19X8, for cashing same. You are required to write up the necessary accounts in Stone's books to record these transactions.

Ex 5 Fleet is a London merchant. During the financial year to 31 March 19X8, he sent a consignment of goods to Sing, his agent in Bali. The details of the transaction were as follows:

- (a) On 1 April 19X7, 1,000 boxes were sent to Sing. These boxes had originally cost Fleet £20 each.
- (b) Fleet's carriage, freight and insurance costs of the consignment paid on 30 April 19X7 amounted to £2,000.
- (c) During the voyage to Bali, ten boxes were lost. On 30 September 19X7, Fleet received a cheque for £220 as compensation from his insurance company for the loss of the boxes.
- (d) On 1 March 19X8, Fleet received £20,000 from Sing.
- (e) Both Fleet and Sing's accounting year end is 31 March.
- (f) On 15 April 19X8, Fleet received the following interim account sales from Sing:

<i>Interim Account Sales</i>		
	£	£
The Water Front Gama Bali		
31 March 19X8		
Consignment of goods sold on behalf of Fleet, London: 950 boxes of merchandise.		
Sales:		£
950 boxes at £30 each		28,500
Charges:		
Distribution expenses (at £2 per box)	1,900	
Landing charges and import duty (at £1 per box)	990	
Commission (5% × £28,500)	<u>1,425</u>	<u>4,315</u>
		24,185
Less amount previously sent		<u>20,000</u>
Net proceeds per draft enclosed		<u>£4,185</u>
		31 March 19X8 Sing (signed) Bali

Required:

Prepare the following ledger accounts for the year to 31 March 19X8:

- (a) in Fleet's books of account:
 - (i) goods sent on consignment account;
 - (ii) consignment to Sing's account;
 - (iii) Sing (consignee) account;
 and,
- (b) in Sing's books of account:
 - (i) Fleet (London) account;
 - (ii) commission account.

Consignment Accounts

- Q1.** Lee started a business in Indonesia on 1 January 2013 selling lawn mowers. During the first year of trading Lee bought 1000 lawn mowers at \$50 each. He shipped 400 of these to Albert, his agent in Jamaica. Lee also sold 550 lawn mowers in Indonesia.

The following additional information is available.

Freight charges paid by Lee	\$3 600
Landing duties paid by Albert	\$400
Rate of commission paid to Albert	10%
Cash remitted by Albert to Lee	\$19 000

Lee's income statement for the year ended 31 December 2013 included the following.

	\$
Gross profit	22 000
Consignment profit	6 720
Selling, distribution and administration costs (arising in Indonesia)	17 600

Lee's statement of financial position at 31 December 2013 included the following inventory.

	\$
Jamaica	4 800
Indonesia	2 500
Total inventory	7 300

REQUIRED

- (a) Prepare the consignment account in the books of Lee for the year ended 31 December 2013. [8]
- (b) Prepare Albert's account in the books of Lee for the year ended 31 December 2013. [6]
- (c) Calculate the number of unsold lawn mowers Albert was holding on 31 December 2013. [5]

Additional information

Lee is considering whether to concentrate his efforts on sales in Indonesia or in Jamaica.

REQUIRED

- (d) Advise Lee where to concentrate his sales effort. Support your answer with calculations. [6]

[Total: 25]

Q2. Hamid and Patel trade regularly with each other. Patel is based in India and Hamid is based in Scotland.

On 15 November 2014 Hamid sent 100 cases of goods to Patel costing \$12 000. The commission on sales was agreed at 5% of the gross sales.

On the same day Hamid paid delivery charges of \$610 and insurance of \$110.

Hamid's financial year ended on 31 March 2015.

At that date Patel provided the following information:

1 70% of the goods had been sold for \$10 600.

2 \$7475 had been sent to Hamid.

3 There was an irrecoverable debt of \$120.

4 Storage charges of \$350 and selling expenses of \$245 had been paid by Patel.

Patel paid the balance due on 31 March 2015.

Hamid incurred bank charges of \$12 for processing this payment.

REQUIRED

(a) Prepare in the books of Hamid the following accounts at 31 March 2015:

- (i) the goods sent on consignment account [1]
- (ii) the consignment to Patel account [11]
- (iii) Patel account [7]

(b) Analyse the effect on profit of the irrecoverable debt incurred during the year. [2]

Additional information

Hamid and Patel are now considering forming a partnership rather than continuing to trade on a consignment basis.

REQUIRED

(c) Advise whether or not Hamid and Patel should enter into a partnership with each other.

Justify your answer. [4]

[Total: 25]

Q3. Aleksander is a trader with a financial year end of 30 June. He buys containers of sunflower seeds for \$100 each. Some of these he ships to his agent Benji in northern Europe. He pays Benji a commission of 10% of sales value.

The following information is available:

- 1 On 2 April 2017 Aleksander sent 200 containers to Benji. Aleksander paid packing costs of \$120 and freight costs of \$6080.
- 2 Benji paid additional freight costs of \$1600 for transport from the port to his warehouse.
- 3 In the period to 30 June 2017 Benji sold 160 containers for \$170 each. He remitted \$21 000 to Aleksander on 14 June.

REQUIRED

(a) Prepare the following ledger accounts in the books of Aleksander for the 3 months ended 30 June 2017.

- | | |
|----------------------------------|------|
| (i) goods on consignment account | [2] |
| (ii) consignment account | [12] |
| (iii) Benji account | [5] |

Additional information

The government in Benji's country decided to introduce import duties from 1 July 2017 which amount to \$20 per container.

REQUIRED

- (b) Explain how Aleksander might have dealt with this increase in cost. Support your answer by considering the effect on the profit per container. [4]
- (c) State why an advertising campaign paid for by an agent would not be included in the valuation of inventory. [2]

[Total: 25]