

How Do You Balance Order Costing?

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When you look at your Profit and Loss (P & L) each month, is the bottom line accurately reflecting the profit margin on that month's sales?

Or, for example, do you have to make mental adjustments for a large order of imprinted T-shirts you are doing. You received the shirt vendor's invoice a few days before closing the month but will not bill your customer until you receive the bill from the decorator. Or maybe it is the other way around. You had a large order that shipped on the 29th and you want to bill your customer even though you do not yet have the bill from the vendor. If you are making these mental adjustments, you will want to consider implementing steps to correct the situation. You want to achieve an accrual accounting principle known as matching. Matching on your P & L means that the sales reported for a month go with the expense reported for the month. When you have matching of costs, you are better informed about your business performance and can make better financial decisions. This document will help you to decide how best to solve the above situation, then give you the detailed instructions you will need to implement the method you choose.

P & L Matching

The matching discussed in the previous section can be achieved in two ways. Your choice of methods should be influenced by these two considerations:

1. Do you have a large volume of multiple vendor orders and other orders for which you post your invoice from a vendor in a different month than you invoice your customer?
2. Do you have someone internally who feels sufficiently comfortable with accounting principles to oversee the matching process and make

adjustments?

If your answer to either question is NO, you should be using the manual method of matching described in Method One. Method One uses G/L #400 Cost of Sales-Drop Ship Account for posting and balancing. If your answer to both questions is YES, you should be using the computer method of matching described in Method Two. Method Two use G/L # 135 Drop Ship Merchandise Account for posting and balancing.

If you have one Yes and one NO, then you will have to weigh the benefits and requirements of each to arrive at your decision. Use the detailed explanation of both methods detailed below to help with your decision.

Manual Matching

GL # 400

1. Matching can be achieved manually by simply making sure all work that goes together is completed by the end of the month. That is, make sure you have invoiced everything to customers for which you have been invoiced by your vendors and vice-versa.

2. If there is something left over that you cannot match, you may choose to do a journal entry for that amount to offset the cost. Doing this journal entry is optional. It is not required. If you do this journal entry, you will need to reverse the journal entry in the next month. Your journal entry is a DR/CR to 135 & 400. The Order Costing Report can be used to help you make this journal entry. Refer to the section on balancing the order costing report for help with using this report.

When using the manual method, you will have to setup your software as follows.

Company Information:

The Drop Ship Merchandise G/L Account and the Cost of Sales-Drop Ship G/L Account numbers should both be set with #400 if using the PPAI chart of accounts.

Vendor Masters:

The G/L account for merchandise should be your Cost of Sales-Drop Ship

Account, G/L #400 if using the PAAI chart of accounts.

Computer Matching

1. Matching can be achieved by allowing the computer to post the cost at the same time the sale is being posted (at invoicing time). When using this method, the system will post a debit to your Cost of Sales - Drop Ship (400) account and a credit to your Drop Ship Merchandise account (135).

2. The amounts posted (debited) for orders through vouching will go to a "holding account" called Drop Ship Merchandise (135). This vouched cost should be matched to the billed cost on the order being billed. The cost actually posted to the general ledger account for Cost of Sales - Drop Ship (400) is taken from the billed cost on the order.

3. To make all this work correctly in your office, cooperation is required among several areas:

- The person doing vouching or preparing invoices for vouching needs to know something about how the orders will be billed out to the customers.
- The person doing billing needs to follow well-defined rules established to meet the needs of your company.
- The controller or your company's equivalent person needs to balance the Drop Ship Merchandise (135) account monthly.
- To do this balancing, you will use the Order Costing Report among other reports.

4. A correcting journal entry may be necessary between the Drop Ship Merchandise (135) and Cost of Sales - Drop Ship (400) when the account balance is proved.

If the vouching is being done properly, if the billing people are correctly following their rules, and if the rules are well established, these journal entries should be for relatively insignificant amounts. Refer to the section on using the Order Costing Report for information on balancing and suggestions that will help make balancing a smooth process.

When using the computer method, you will have to setup your software as follows.

Company Information:

The Drop Ship Merchandise G/L Account and Cost of Sales-Drop Ship G/L Account numbers should both be set up with their respective numbers, #135 and #400 in the PPAI chart of accounts.

Vendor Masters:

The G/L account for merchandise should be your Cost of Sales - Drop Ship account, #135 in the PPAI chart of accounts.

Vouching and Billing

There are 3 different scenarios/options for vouching and billing. There are pros and cons to each. Keep in mind a "pro" to one company may be a "con" to another. The happenings/consequences of each program are explained below. Please review each option and pick the best option for your scenario.

1. Vouching with Order Entry

Vouching:

- Once an order is added for order distribution the Order Costing Icon is available in the toolbar but the vendor costing will not be there.
- Vendor costing will not be there until you distribute GL and click OK.
- To view:

Go to Distribution Tab

Click on Order Costing Distribution

Click the order.

Click on the Order Costing icon

Select to display "order costing not yet posted."

Customers Order Costing

Order Entry:

- If distribution has been made to this order in vouching, a message will appear stating your station has this order locked but will let you continue.
- Cannot enter quantity shipped if there are over/under runs, but can change quantity ordered.
- Cannot enter Shipping & Handling (S&H) for freight but can enter an SH line item for quantity ordered only.
- Can add additional charges not on the order.
- Booked information for salesperson will be updated. If the salesperson is paid on booked with no overruns this would not be the correct method.
- Order costing icon will not show vouched cost by vendor. Will have to view

it in vouching.

2. Vouching with Billing

Vouching:

- Once an order is added for order distribution, the Order Costing Icon is available but the vendor costing will not be there.
- Vendor costing will not be there until you distribute GL and click OK.
- To view:

Go to Distribution Tab

Click on Order Costing Distribution

Click the order.

Click on the Order Costing icon

Select to display "order costing not yet posted."

Billing:

- SH line item or Shipping & Handling (S&H) can be added. If uncertain of the freight amount vouched, view the order costing in vouching.
- Quantity shipped can be modified for over/under runs. Quantity Back Ordered (B/O) can be entered.
- If not ready to bill the order must place on billing hold. Only Credit Supervisor can take off hold.
- If multiple vendor costs and not all ready to be vouched, can either start with order entry method and then last vendor bill the order, or place order on billing hold until last vendor vouched.

3. Vouching then Billing

Vouching:

- Finish all vouching and post.

Billing:

- Bring the orders into billing and you will be able to compare vouched cost and billed costs on the line item screen with Order Costing Icon.
- Order Costing Icon will now show the breakdown for vendor(s).

- SH line item or Shipping and Handling (S&H) can be added. If uncertain of the freight amount vouched, view the Order Costing Icon.
- Quantity shipped can be modified for over/under runs. Quantity Back Ordered (B/O) can be entered.
- If not ready to bill the order must place on billing hold. Only Credit Supervisor can take off hold.
- If multiple vendor costs are not all vouched place order on billing hold until last vendor vouched.

Note: This method is following the Daily Paper Flow-Data Input for Supplier Invoices found in the Reference Manual-System Tab-Part 1 Optimize your Office System. Matching your vendor Invoices to the office copy and writing any changes on the office copy. This information could also be entered in Order Notes instead of writing on the office copy and can be done during vouching in any of the above methods. Billing personnel would need to view the order notes.