

All Of The Units Sold Were Priced At \$2,360 Per Unit. Splish Brothers Ltd. Uses The Periodic Inventory

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In the world of inventory management and retail accounting, understanding how to accurately calculate cost of goods sold (COGS) and ending inventory is crucial for financial accuracy and strategic decision-making. Splish Brothers Ltd., a company that recently sold a specific quantity of units at a fixed price, employs the periodic inventory system—an approach that differs significantly from the perpetual inventory method. This article explores the concepts behind the periodic inventory system, its application in the context of Splish Brothers Ltd., and how to perform essential calculations using this method.

Understanding the Periodic Inventory System

What Is the Periodic Inventory System?

The periodic inventory system is a method of inventory accounting where updates to inventory records are made at specific intervals—such as monthly, quarterly, or annually—rather than continuously. Under this system, companies do not keep a running tally of inventory levels after each sale or purchase. Instead, they perform a physical count of inventory at the end of the accounting period to determine ending inventory and COGS.

Key Features of the Periodic Inventory System

- **Physical Counts:** Inventory is counted physically at the end of each period.
- **No Continuous Tracking:** Inventory records are not updated after each transaction.
- **Simpler Record-Keeping:** Less complex than perpetual systems, making it suitable for small businesses or those with less frequent transactions.
- **Cost of Goods Sold Calculation:** Calculated based on beginning inventory, purchases during the period, and ending inventory.

Applying the Periodic Inventory System to Splish Brothers Ltd.

Scenario Overview

Suppose Splish Brothers Ltd. sold 100 units of a product at a price of \$2,360 per unit during a specific period. For simplicity, let's assume:

- Beginning inventory at the start of the period: 50 units
- Purchases during the period: 150 units at varying costs
- Ending inventory (after physical count): to be determined

The key accounting challenge is to determine the cost of goods sold and ending inventory for this period, given the units sold and the inventory data.

Data Assumptions for Illustration

Description	Units	Cost per Unit	Total Cost
Beginning Inventory	50	\$2,200	\$110,000
Purchases	150	Varying (assume two batches)	\$330,000 (see details below)
Total Units Available	200		\$440,000

Let's assume the purchases during the period occurred in two batches:

- 100 units purchased at \$2,250 each
- 50 units purchased at \$2,350 each

Total purchase cost:

- 100 units x \$2,250 = \$225,000
- 50 units x \$2,350 = \$117,500
- Total = \$342,500

Total units available:

- Beginning inventory: 50 units
- Purchases: 150 units
- Total: 200 units

Units sold:

- 100 units at \$2,360 each (sales revenue)
- The cost of these 100 units needs to be calculated for COGS.

Calculating Cost of Goods Sold (COGS) Using the Periodic Method

To determine the COGS under the periodic system, businesses typically use inventory valuation methods such as FIFO (First-In, First-Out), LIFO (Last-In, First-Out), or weighted average cost. Here, we'll demonstrate calculations using FIFO and weighted average, as they are common.

1. FIFO (First-In, First-Out)

FIFO assumes that the oldest inventory is sold first.

Step 1: Determine the cost of the earliest inventory units.

- Beginning inventory: 50 units at \$2,200
- First 50 units sold: at \$2,200 each
- Next 50 units sold: from the 100 units purchased at \$2,250

Step 2: Calculate COGS for 100 units sold:

- 50 units x \$2,200 = \$110,000
- 50 units x \$2,250 = \$112,500

Total COGS:

- \$110,000 + \$112,500 = \$222,500

Step 3: Determine ending inventory:

- Remaining units after sale:
 - From the purchase batch at \$2,250: 50 units remaining (since 100 units purchased, 50 sold)
 - From the purchase batch at \$2,350: 50 units
 - From beginning inventory: 0 units (all sold)
- Ending inventory:
 - 50 units at \$2,250 = \$112,500
 - 50 units at \$2,350 = \$117,500

Total ending inventory:

- \$112,500 + \$117,500 = \$230,000

2. Weighted Average Cost Method

This method averages the cost of all units available for sale.

Step 1: Calculate total cost of inventory:

- Beginning inventory: \$110,000
- Purchases: \$342,500

Total cost = \$110,000 + \$342,500 = \$452,500

Step 2: Calculate total units:

- 50 (beginning) + 150 (purchases) = 200 units

Step 3: Calculate average cost per unit:

- \$452,500 / 200 units = \$2,262.50 per unit

Step 4: Compute COGS:

- 100 units sold x \$2,262.50 = \$226,250

Step 5: Determine ending inventory:

- Remaining units: 100 units
- Ending inventory: 100 units x \$2,262.50 = \$226,250

Note: Under FIFO, the costs are more reflective of recent prices, whereas the weighted average smooths out price fluctuations.

Financial Implications and Reporting

Impact on Profit and Taxes

The choice of inventory valuation method directly affects gross profit, net income, and taxable income:

- FIFO: Usually results in higher net income during periods of rising prices, as older, cheaper costs are matched against current sales.
- Weighted Average: Tends to produce results between FIFO and LIFO, depending on price fluctuations.

Splish Brothers Ltd. must select a consistent inventory valuation method and disclose it in financial statements to ensure transparency and comparability.

Inventory Turnover and Business Strategy

Understanding how inventory is valued can also influence business decisions:

- High inventory turnover might suggest efficient sales.
- Lower costs of goods sold under FIFO can boost profitability reports.
- Strategic inventory management can optimize cash flow and profitability.

Benefits of Using the Periodic Inventory System for Splish Brothers Ltd.

- **Simplicity:** The system's reliance on physical counts at set intervals reduces the need for complex tracking systems.
- **Cost-Effective:** Suitable for small businesses with less frequent transactions.
- **Compliance:** Meets accounting standards for certain types of businesses, especially when integrated with robust internal controls.

Limitations of the Periodic Inventory System

- **Less Real-Time Data:** Inventory levels are not updated after each sale, which might lead to stockouts or overstocking.
- **Potential for Errors:** Physical counts are susceptible to errors or theft if not properly managed.
- **Delayed Financial Reporting:** COGS and inventory figures are only accurate after physical counts, which could delay decision-making.

Conclusion

Splish Brothers Ltd.'s use of the periodic inventory system offers a straightforward approach to managing inventory and calculating COGS. By understanding fundamental concepts like inventory valuation methods—FIFO, LIFO, and weighted average—and their implications on financial statements, the company can make informed decisions that align with its operational needs and strategic goals. Whether the company is choosing to focus on simplicity or seeking detailed real-time insights, the periodic inventory system remains a valuable tool in the broader financial management toolkit.

Effective inventory management, combined with accurate financial reporting, enables Splish Brothers Ltd. to maintain profitability, optimize stock levels, and comply with accounting standards, ultimately supporting sustained business growth.

Frequently Asked Questions

What is the unit price used by Splish Brothers Ltd. for all units sold?

The unit price used by Splish Brothers Ltd. for all units sold is \$2,360 per unit.

How does using the periodic inventory system affect inventory tracking at Splish Brothers Ltd.?

Using the periodic inventory system means that inventory levels are updated at specific intervals, typically through a physical count, rather than continuously tracking inventory after each sale.

What are the advantages of using a periodic inventory system for Splish Brothers Ltd.?

Advantages include simplicity of record-keeping, lower ongoing costs, and ease of implementation, especially for small or seasonal businesses.

How is the cost of goods sold (COGS) calculated for Splish Brothers Ltd.?

COGS is calculated by subtracting ending inventory from the beginning inventory plus purchases made during the period, based on periodic inventory counts.

Why might Splish Brothers Ltd. choose a uniform unit price of \$2,360 for all units sold?

They might choose a uniform price for simplicity in accounting, especially if all units are identical or if they use a specific inventory valuation method like specific identification or FIFO.

Does using the periodic inventory system impact the accuracy of inventory valuation for Splish Brothers Ltd.?

It may impact accuracy slightly, as inventory levels are only updated periodically, which can lead to discrepancies between actual and recorded inventory between counts.

What are the typical steps involved in the periodic inventory process at Splish Brothers Ltd.?

Steps include conducting a physical inventory count at the end of the period, calculating COGS, updating inventory records, and adjusting for any purchases or returns.

How does the pricing at \$2,360 per unit influence the financial statements of Splish Brothers Ltd.?

Pricing at \$2,360 per unit determines revenue and COGS calculations, impacting gross profit and overall profitability reported in financial statements.

What considerations should Splish Brothers Ltd. keep in mind

when using the periodic inventory system with a fixed unit price?

They should ensure accurate physical counts, consider inventory valuation methods that align with their pricing strategy, and be aware of potential inventory discrepancies between counts.

Additional Resources

All Of The Units Sold Were Priced At \$2,360 Per Unit. Splish Brothers Ltd. Uses The Periodic Inventory

Understanding inventory management and pricing strategies is crucial for any business seeking profitability and operational efficiency. In this review, we delve into the specifics of a scenario where all units sold are priced uniformly at \$2,360 per unit, and the company, Splish Brothers Ltd., employs the periodic inventory system. We will explore the implications of such a pricing model, analyze the benefits and drawbacks of the periodic inventory method, and offer insights into how these elements influence financial reporting, inventory control, and overall business performance.

Overview of the Business Context

Splish Brothers Ltd. operates in a competitive market segment where uniform pricing per unit simplifies sales processes. Selling all units at \$2,360 indicates a strategic approach—possibly targeting a niche market or leveraging premium positioning. The choice of inventory management system, specifically the periodic inventory method, further influences how the company tracks inventory levels, cost of goods sold (COGS), and profitability.

Key Points:

- Uniform unit price of \$2,360 simplifies sales transactions.
- Periodic inventory system impacts how inventory and COGS are calculated.
- The combined approach affects financial analysis, inventory control, and strategic decision-making.

Uniform Price Point of \$2,360 Per Unit

Pricing strategy is a foundational element of a business's market positioning and profitability. Setting all units at a fixed price of \$2,360 suggests a deliberate approach, possibly aiming to establish a premium brand or to streamline sales and inventory management.

Advantages of Uniform Pricing

- Simplifies Sales Processes: With a fixed price, sales staff and customers face fewer negotiations, reducing transaction time.
- Eases Inventory Valuation: Calculations for revenue, gross profit, and inventory valuation become straightforward since each unit has the same value.
- Facilitates Financial Analysis: Uniform pricing reduces complexity in profit margin analysis and cost tracking.
- Supports Brand Positioning: A fixed high price can help position the product as a premium offering.

Challenges of Uniform Pricing

- Limited Flexibility: Fixed pricing may restrict the ability to respond to market fluctuations or promotional opportunities.
- Potential for Reduced Competitiveness: If competitors offer discounts or varied pricing, uniform pricing could impact sales volume.
- Customer Perception Risks: Customers might perceive the price as too high or inflexible, affecting demand.

Implications for Business Strategy

- The fixed price sets a clear revenue target per unit.
- The business must optimize its cost structure to ensure profitability at this price.
- Market research must justify the premium price point to maintain demand.

The Periodic Inventory System: Features and Functionality

The periodic inventory method is characterized by updating inventory records at specific intervals—such as monthly, quarterly, or annually—rather than continuously tracking inventory changes.

Features of the Periodic Inventory System

- Infrequent Updates: Inventory levels and COGS are calculated at the end of each period.
- Simpler Record-Keeping: Less detailed record maintenance compared to perpetual systems.
- Physical Counts Required: Regular physical stock counts are essential to determine inventory on hand.
- Cost Calculation: $\text{COGS} = \text{Beginning Inventory} + \text{Purchases during the period} - \text{Ending Inventory}$.

Advantages of the Periodic System

- Cost-Effective: Requires less sophisticated technology and record-keeping.
- Simplicity: Easier to implement for small to medium-sized businesses.
- Suitable for Low-Value or High-Volume Items: When individual item tracking is impractical.

Drawbacks of the Periodic System

- Less Accurate Real-Time Data: Inventory levels are only updated periodically, which can lead to stockouts or overstocking.
- Labor-Intensive Physical Counts: Regular physical counts are necessary, which can be disruptive.
- Limited Insight: Lacks detailed transaction data, making it harder to analyze sales trends or perform FIFO/LIFO assessments accurately.

Impact on Financial Reporting

- The periodic system's reliance on physical counts can introduce inaccuracies if counts are not precise.
- Financial statements may not reflect real-time inventory levels.
- Requires careful timing and reconciliation to maintain accurate records.

Operational Impacts of Combining Uniform Pricing with Periodic Inventory

Integrating a fixed unit price with a periodic inventory approach influences multiple facets of business operations.

Inventory Management

- Simplified Valuation: Since all units are priced equally, calculating inventory value is straightforward.
- Physical Counts Essential: The need for periodic counts ensures inventory accuracy but increases operational workload.
- Potential for Stock Discrepancies: Without continuous tracking, discrepancies may arise, especially in high-volume settings.

Financial Analysis and Reporting

- Predictable Revenue: Uniform pricing facilitates revenue forecasting.
- Cost of Goods Sold Calculation: At period-end, COGS is derived from the beginning inventory, purchases, and ending inventory, making profit analysis more straightforward.
- Impact on Gross Profit: Clear visibility into profit margins per unit, assuming purchase costs are stable.

Pricing Strategy Effectiveness

- Uniform pricing simplifies promotional planning and discount implementation.
- However, it limits price discrimination opportunities, which could maximize revenue if different customer segments are targeted.

Pros and Cons Summary

Pros:

- Simplifies inventory valuation and sales processes.
- Facilitates quick financial analysis.
- Supports a premium branding strategy.

Cons:

- Less real-time data accuracy.
- Potential inventory discrepancies.
- Reduced flexibility in pricing adjustments.

Case Study: Financial Implications for Splish Brothers Ltd.

Suppose Splish Brothers Ltd. sells 1,000 units in a quarter at \$2,360 each, with a consistent purchase cost of \$1,500 per unit. Using the periodic inventory system, their financial calculations would proceed as follows:

- Beginning Inventory: 200 units valued at \$1,500 each = \$300,000.
- Purchases during Period: 800 units at \$1,500 each = \$1,200,000.
- Total Goods Available for Sale: 1,000 units totaling \$1,500,000.
- Ending Inventory: 150 units remaining, valued at \$1,500 each = \$225,000.
- Cost of Goods Sold (COGS):

$$\begin{aligned}\text{COGS} &= \text{Beginning Inventory} + \text{Purchases} - \text{Ending Inventory} \\ &= \$300,000 + \$1,200,000 - \$225,000 \\ &= \$1,275,000\end{aligned}$$

- Revenue:

$$1,000 \text{ units} \times \$2,360 = \$2,360,000$$

- Gross Profit:

$$\text{Revenue} - \text{COGS} = \$2,360,000 - \$1,275,000 = \$1,085,000$$

This simplified calculation demonstrates the clarity and straightforwardness of the periodic inventory method, especially given the uniform unit price.

Strategies for Optimization and Best Practices

While the combination of fixed unit pricing and periodic inventory is effective for certain business models, there are strategies to optimize its benefits:

- Regular Physical Counts: Schedule counts to minimize inventory discrepancies.
- Cost Control: Maintain stable purchase costs to ensure consistent profit margins.
- Pricing Flexibility: Consider occasional promotional discounts to stimulate sales without disrupting the overall pricing strategy.
- Technology Integration: Even with a periodic system, implementing inventory management software can improve accuracy and streamline reconciliation.
- Market Monitoring: Keep abreast of competitor pricing and market demand to adjust sales strategies accordingly.

Conclusion

The scenario where all units sold are priced at \$2,360 per unit, combined with the use of the periodic inventory system, offers a unique blend of simplicity and strategic clarity. For Splish Brothers Ltd., this approach streamlines sales, simplifies inventory valuation, and provides a clear financial picture, especially when purchase costs are stable and inventory turnover is manageable. However, it also introduces challenges such as less real-time data accuracy and limited flexibility in pricing strategies.

Businesses considering similar models should weigh the operational simplicity against the potential for inventory discrepancies and market responsiveness. Regular physical counts, disciplined cost management, and strategic marketing can mitigate some drawbacks while maximizing the advantages of this approach. Ultimately, understanding the interplay between pricing strategies and inventory systems is essential for making informed decisions that enhance profitability and operational efficiency.

In summary:

- Uniform pricing simplifies sales and financial calculations but requires careful market positioning.
- The periodic inventory system is cost-effective and straightforward but less suitable for high-volume or fast-moving inventory.
- Combining these strategies can work well for niche markets or premium brands with stable costs.
- Continuous monitoring and process discipline are key to maintaining accuracy and profitability.

This comprehensive review aims to provide clear insights into how a business like Splish Brothers Ltd. can navigate the complexities of uniform unit pricing and periodic inventory management to achieve its financial and operational goals.

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