# IAS 2 INVENTORIES

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# *IAS 2 INVENTORIES*

Effective date periods beginning on or after 1st January 2005

## DEFINITIONS

**IAS 2 DEFINES INVENTORIES AS ASSETS THAT ARE:**

- Held for sale in ordinary course of business.
- Inventories are assets in the process of production for such a sale.
- In the form of materials or supplies to be consumed in the production process or in the rendering of services.

Such as: Merchandise, Production Supplies, Materials, Work in progress, Finished Goods.

## MEASUREMENT RULE

Inventories should be measured at lower of:

COST | NRV

Measurement exceptions-

- Producers of agricultural, forest products, minerals, and mineral product
- Commodity dealers and brokers.

## MEASUREMENT OF INVENTORIES

**COST**

COST OF PURCHASE | COST OF CONVERSION | OTHER COSTS

**COST OR PURCHASE-**Include purchase price, import duties non-refundable taxes, cost directly attributable to the acquisition of finished goods like transport and deduct trade discount and similar items.

**COST OF CONVERSION-**Cost directly related to the units of production like direct materials direct labour and also production overhead allocated on a systematic basis.

**Other Cost**-Include any other cost into the cost of inventories only if they are incurred in bringing the inventory to present condition.

**DO NOT INCLUDE**

- **ABNORMAL WASTE**
- **STORAGE COST(But include those necessary in the production process.)**
- **Administrative Overheads.**
- **Selling Costs.**

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## COST MEASUREMENT TECHNIQUES

**Standard cost-** Producers of large amount or small items.

**Retail method**-Retailers with large turnover of inventories with similar profit margin.

## NET RELIASABLE VALUE

It is **ESTIMATED SELLING PRICE** (LESS) **ESTIMATED COSTS OF COMPLETION** (LESS) **ESTIMATED SELLING COSTS.**

We need to make sure that the inventories in the financial statements are not stated above this NRV.

If NRV<costs then u need to write down the inventories to the net-realisable value.

## COST FORMULAS

**Are the inventories not interchangeable?**

**Are the goods or services produces and segregated for specific project?**

**YES** — SPECIFIC COST

**NO** — FIFO OR WEIGHTED AVERAGE

**For example- Dealing in vintage cars are not interchangeable and very specific so if you buy a specific car for $1000000 and sell it for $1200000 you need to recognize for $1000000 specifically.**

## DISCLOSURES

IAS 2 also prescribes when and how to recognize inventories as an expense in Profit/ Loss.

- ❑ When inventories are sold- Carrying amount of item sold  is transferred to Statement of profit & loss as an expense. –

**DEBIT**- P/L COST OF SALES

    **CREDIT**- INVENTORIES

- ❑ When NRV is lower than cost or loss in inventories then you need to recognize it as expense in the period when the write/loss occurs.

**DEBIT**- P/L Write down /COS

    **CREDIT**- INVENTORIES

- ❑ When there is reversal of any write down due to increase in NRV then you should recognize it as an expense in the period in which the reversal occurs.

**DEBIT**- INVENTORIES

    **CREDIT**- P/L Reversal of write- down/COS.

**Disclosure Example-**

Cost of raw materials : Rs. 10/-

Direct Labour: Rs.5/-

The entity incurred Rs.80000 towards production overheads. 7000 units were produced during 2017 and 9000 were produced during 2018 .The normal level of production is 8000 units. Inventory at the year end were- 2017- 1000 and 2018-1500. Cost of closing inventory?

2017

Cost of raw material – 10

Cost of labour- 5

Fixed production overhead- 80000/8000= 10

Total cost per unit- 25

Cost of inventory- (1000*25)= 25000/-

2018-

Cost of materials – 10

Cost of labour- 5

Fixed production overhead- 80000/9000=8.89

Total cost per unit-23.89

Cost of inventory- (1500* 23.89)= 35,835.

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