

Accounting Standard 2 – “Valuation of Inventories”

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Introduction

- ❑ This Standard should be applied in accounting for inventories other than:
 - work in progress arising under construction contracts, including directly related service contracts
 - work in progress arising in the ordinary course of business of service providers
 - shares, debentures and other financial instruments held as stock-in-trade
 - producers' inventories of livestock, agricultural and forest products, and mineral oils, ores and gases to the extent that they are measured at net realisable value in accordance with well established practices in those industries.

What are Inventories?

- assets held for sale in the ordinary course of business
- in the process of production for such sale
- in the form of materials or supplies to be consumed in the production process
- Inventories encompass goods purchased and held for resale

Cost of Inventories includes

- Cost of purchase including duties and taxes which are not recoverable, freight inwards and other expenditures directly attributable
- Cost of conversion of raw materials into finished goods
- Other costs are included only to the extent that they are incurred in bringing the inventories to their present location and condition.
- Borrowing cost in accordance with AS-16

What are not included in the cost of Inventories?

- abnormal amounts of wasted materials, labour, or other production costs
- storage costs, unless those costs are necessary in the production process prior to a further production stage
- administrative overheads that do not contribute to Inventories
- selling and distribution costs.

Valuation of Inventories

- ❑ Cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects should be assigned by specific identification of their individual costs.
- ❑ Cost of Inventories other than those referred above can be measured using either First-in-First-out (FIFO) method or weighted average method.
- ❑ Inventories should be valued at lower of cost or net realizable value at each periodic interval.

Disclosures

- ❑ accounting policies adopted in measuring inventories, including the cost formula used
- ❑ total carrying amount of inventories and its classification appropriate to the enterprise

Issues

- Whether stock which is booked by the customer can be valued at the rate booked by them? (EAC Vol 36 Page 197)
- Whether stock which is held as base stock the quantity of which remains unchanged can be valued at cost and whether the same can be recognised as Property, Plant & Equipment? (EAC Vol 36 Page 197)
- Whether regeneration expenses incurred for raising standard crops classified as Inventory of Standard crops can be revalued to their present market value/real worth? (EAC Vol 37 Page 81)
- Whether dead stock which is not held for sale and which is used as part of Property, Plant & Equipment for its intended use can be classified as Property, Plant & Equipment or it should be classified as Inventory? (EAC Vol 40 Page 115)
- Whether the value of inventories consisting of spares parts which has become obsolete can be written off in full? (EAC Vol 14 Page 35)
- Whether the cost of imported goods-in-transit includes freight, custom duty, clearing charges, warehouse charges, interest on custom duty and insurance? (EAC Vol 15 Page 11)

Issues

- Whether interest cost incurred directly relates to seasonal stock held for sale can be included in the cost of such stock? (EAC Vol 21 Page 1, Page 4 & Page 7)
- Whether interest on CC and Overdraft used for inventories can be included in valuation ? Treatment of interest so included in opening inventory? (EAC Vol 21 Page 98)
- Whether cost of handling of raw materials from one production process to another can be included in the cost of inventory? (EAC Vol 21 Page 80)
- Whether stock of crude in pipelines can be valued at a fixed price or it can be valued as per standard cost? (EAC Vol 21 Page 93)
- Whether inventory of crude in pipeline can be valued at cost where net realizable value ascertainment can lead to subjectivity ? (EAC Vol 21 Page 137)
- Where the number of items in inventory is more and its is not practicable to assess the NRV of each item, therefore adequate provisions for slow moving or non moving items are provided on a periodical basis. Whether this accounting treatment is in accordance with AS – 2? (EAC Vol 21 Page 143)
- Whether transportation cost of goods from factory to field godowns or stockyard should form part of cost of Inventory? (EAC Vol 23 Page 49 & Page 157)

Issues

- ❑ Whether net realizable value of old Inventories can be ascertained based on the average realization of present period? (EAC Vol 24 Page 22)
- ❑ Whether specific identification method can be used for determining the cost of imported raw materials (some are duty-free and some liable to import duty) which is interchangeable instead of weighted average or FIFO method? (EAC Vol 24 Page 13)
- ❑ Whether consumable and spares parts used for consumption in production process or rendering of services can be valued at cost if the finished goods is expected to be sold at or above cost? (EAC Vol 25 Page 182)
- ❑ Whether the accounting policy for Inventory should specifically provide that the Inventory are valued at lower of cost or NRV even when the finished goods is always expected to sold at or above cost? (EAC Vol 25 Page 148)
- ❑ Whether royalty charges on crude oil at a rate applicable as on valuation date and other cost of tank farm and pipeline viz, depreciation, operation and maintenance cost and insurance charges are to be include in the valuation of finished crude oil stock? (EAC Vol 34 Page 94)

Issues

- Whether goods manufactured internally and capitalised as a part of CWIP or PPE, can be considered as revenue in the P&L a/c? (EAC Vol 34 Page 353)
- What will be accounting treatment in case of goods manufactured internally are sold to related entities as per AS 21, 23 and 27? (EAC Vol 34 Page 354)
- When goods manufactured internally are subsequently capitalised, then the cost of such goods will be determined as per AS – 2 (lower of cost or NRV) or as per AS – 10 (actual cost incurred)? (EAC Vol 34 Page 354)
- Whether the year-end unutilised export license can be recognised as Inventory as per AS – 2? (EAC Vol 27 Page 27)

Thank You