

AS-2 / Ind-AS-2 (Valuation of inventories)

- 1) Inventories should be valued at cost or market price (Net realisable value) whichever is lower.
- 2) Cost of inventories
It includes
 - a) Cost of purchases
 - b) Cost of conversions
 - c) other costs incurred to bring inventories to their present location and conditions.
- 3) Cost of purchases includes the following
 - a) Purchase Price
 - b) (+) All duties & taxes
 - c) (+) Transport, handling and other costs directly attributable to acquisition of materials
 - d) (-) Trade discounts / rebates etc.
 - e) (-) Cenvat credit / duty drawback etc.

example

S Ltd purchased raw material for ₹ 1,25,000 less a rebate of 2%. It paid ₹ 25,000⁽⁺⁾ as import duty including ₹ 10,000⁽⁻⁾ as special duty. It spent ₹ 3,000⁽⁺⁾ on ocean freight, clearing agent charges ₹ 2,000⁽⁺⁾, ₹ 4,000^(X) as warehouse rent and ₹ 1,500^(X) on security guard salary. It will get a credit of amount paid as special duty.
Compute value of inventory.

Ans Statement for valuation of inventory

Particulars	Amount	Amount
Purchase cost		1,25,000
<u>Less: Rebate (2% of 1,25,000)</u>		<u>(2,500)</u>
		1,22,500
<u>Add: Import duty</u>	25,000	
<u>Less: Special duty (Tobacco refunded)</u>	(10,000)	<u>15,000</u>
		1,37,500
<u>Add: ocean freight</u>		3,000
<u>Add: clearing agent charges</u>		<u>2,000</u>
Total Cost of inventory		1,42,500

4) Cost of Conversion : Means Cost incurred to change raw material into finished goods or Saleable product

Cost of conversion include

- Costs directly related to unit of production
(e.g. Labour charges, direct expenses etc)
- Allocation of production overheads (Fixed or variable)

Fixed overheads:

Remain constant irrespective of change in level of output or production.

e.g. Factory rent, Supervisor salary etc.

Variable overheads

Allocation of these overheads is based on actual use of production facilities

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Ex At Big Restaurant the fuel consumed for cooking is a variable overhead (Indirect material). For every 100 meals Big Rest needs fuel of ₹ 50. Therefore per meal overhead cost is 50 paise. It uses raw material of ₹ 100 and wages of ₹ 5 per meal.

Ans Cost per meal.

Material	₹ 100
Wages	5
Fuel ($50 \div 100$)	<u>0.50</u>
Cost per meal	<u>105.50</u>

Ex X Ltd incurs the fixed production overheads of ₹ 10,00,000 each year normal capacity of production is 1,00,000 units. In the year 2015 80,000 units were produced and in 2016, 120,000 units were produced.

Ans Fixed overhead to be allocated per unit ₹ 10 per unit
($10,00,000 \div 1,00,000$)

	2015	2016
No of units produced	80,000	1,20,000
Fixed OH allocated per unit ₹	10	10
Fixed overhead recovered ₹	8,00,000	12,00,000
Actual fixed overheads	10,00,000	10,00,000
(Under) / over recovery	(2,00,000)	2,00,000

5) other costs

Other costs are included in the cost of inventories to the extent they are incurred for bringing the inventories to present location and condition.

Ex: A product is manufactured according to the specifications given by customer. Material cost is ₹ 3,00,000 and wages are ₹ 1,30,000. Professional fees ₹ 25,000 paid for having product designed.

Ans The fees paid to professional is other cost. The total cost will be as under.

Material	₹ 3,00,000
wages	1,30,000
other cost	<u>25,000</u>
Total cost	₹ <u>4,55,000</u>

6) Costs excluded from cost of inventory.

Costs that do not satisfy the above conditions are not included in cost of inventory rather recognized as expenses.

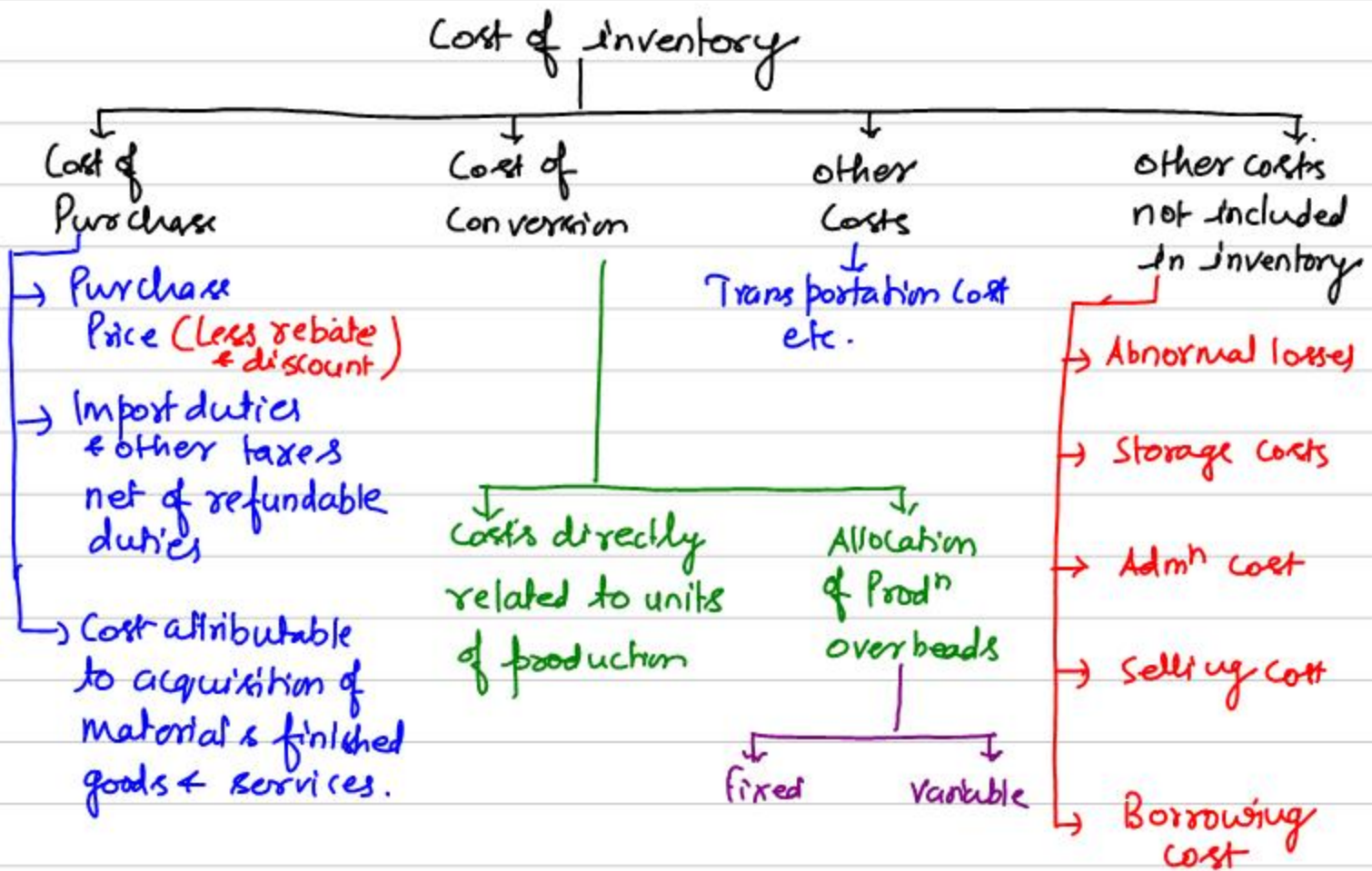
a) Abnormal costs Such as abnormal wastages of material, labours & other costs.

e.g Loss of material by fire

Idle time of workers due to break down of machine

b) Storage costs except that are necessary in production process before further production stage.

- c) Administrative overheads e.g. staff salary, Rent of admⁿ building etc.
- d) Selling expenses : Any kind of selling expenses will not be included in cost of inventory
- e) Borrowing cost : Except permitted by AS-16/Ind-AS-23.



Cost formulae

Cost formula is needed to determine the value of material issued and material remaining in inventory.

a) Specific Identification method

This method is used for those items which are not ordinarily interchangeable. $\therefore$ specific cost is attributed to the cost of inventory.

e.g. Made to order furniture.

b) Other methods

i) FIFO: First in first out

Under this method we assume that inventory which brought first is sold first.

ii) Weighted Avg

$$= \frac{\text{Total cost of material}}{\text{Total quantity of material}}$$

$$\left(\frac{N_1 R_1 + N_2 R_2}{N_1 + N_2} \right)$$

Example: Following details are available from B Ltd

Date	Particulars	Quantity	Rate (₹)
01/04/2015	Opening inventory	500	20
04/04/2015	Purchases	150	22
08/04/2015	Issue	200	

Required

Determine value of inventory as at 8th April 2015 under FIFO & wtd avg method.

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Ans Method 1: FIFO

Date	Particulars	opening qty	Qty Purchased.
1.4.15	opening inventory	500	-
4.4.15	Purchase	-	150
8.4.15	Issue	<u>(200)</u>	<u>-</u>
8.4.15	closing inventory	300	150
	Rate (₹)	20	22.
	Value of inventory	6000	3300
	Total value	₹ 9300	

Method 2: Weighted avg

Date	Particulars	Qty	Rate	Amount
1.4.15	opening	500	20	10,000
4.4.15	Purchase	<u>150</u>	<u>22</u>	<u>3,300</u>
		650	20.46 *	13,300
8.4.15	Issue	<u>200</u>	<u>20.46</u>	<u>4092</u>
8.4.15	closing inventory	<u>450</u>	<u>20.46</u>	<u>9208</u>

$$* \frac{10,000 + 3300}{500 + 150} = ₹ 20.46$$

Notes: LIFO method is not permitted by AS-2

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