INVENTORY

Definition of Inventories by AASB 102
→ 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 ≠ Fixed Assets

Cost of Inventories
Upon acquisition, inventory should be recorded at cost

Freight Costs
Costs for transporting the inventory. May be incurred by the seller or allocated into new account

Operating Cycles
Service Business, Perform Services → rise in A/R → send invoices → receive cash

Merchandising Business, Inventory → sells inventory → rise in A/R → send invoices → receive cash

Classifying Inventory
Raw Materials
Materials will be used in production process

Working in Progress
Materials already started in production process but not yet completed

Finished Goods
Completed manufactured items that are ready for sale

Periodic System
Cost of Sales are determined only at end of accounting period by a physical inventory count and the revenues is recorded when the sale is made

THE MAIN DIFFERENCES IS WHEN THE COS IS COMPUTED

To determine CoS (Cost of Goods/Supplies) by Periodic System
- Record purchases of inventory
- Determine CoS purchased
- Determine CoS on hand at beginning and end of accounting period - undertake a physical inventory count

To determine CoS by Perpetual System
Detailed Inventory system in which the cost of inventory and the cost of sales is maintained on a continual basis

Purchase Discounts
Settlement Discounts
Discounts given to customers as a reward for prompt payment (payment within the discount period)

Trade Discounts
Percentage reduction in the list price of inventory sold (fixed)

Perpetual vs Periodic Recording

Perpetual	Periodic
Better control and cost saving	Assumes inventory sold, relies on stocktake for CoS calculation

Cost Methods
Specific Identification
If the item is in limited variety with high unit cost items that can be clearly identified, such as motor vehicle

Cash Flow Assumptions
First-in, first out (FIFO)
Assumes first goods purchased = first goods sold

Last-in, last out (LIFO)
Assumes last goods purchased = first goods sold

Weighted average cost
Assumes all goods are similar in nature, therefore calculate the average costs

Income statement effect
<u>*In period of increasing prices*</u>
FIFO reports highest net income
LIFO reports the lowest

<u>Period of increasing prices and allocated to ending inventory using</u>
FIFO will approximate current costs
LIFO will understated

<u>In periods of decreasing prices</u>
FIFO reports the lowest net income
LIFO reports the highest

Where WAC falls in the middle