LKAS 02
INVENTORIES

Objective

The objective of this Standard is to prescribe the accounting treatment for inventories. A primary issue in accounting for inventories is the amount of cost to be recognized as an asset and carried forward until the related revenues are recognized.

This Standard provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realizable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

Scope

This Standard applies to all inventories, except:

a) work in progress arising under construction contracts, including directly related service contracts (see LKAS 11 Construction Contracts);
b) financial instruments (see LKAS 32 financial Instruments: presentation and LKAS 39 Financial Instruments: Recognition and Measurement); and
c) biological assets related to agricultural activity and agricultural produce at the point of harvest (see LKAS 41 Agriculture).

This Standard does not apply to the measurement of inventories held by:

a) producers of agricultural and forest products, agricultural produce after harvest, and minerals and mineral products, to the extent that they are measured at net realizable value in accordance with well-established practices in those industries. When such inventories are measured at net realizable value, changes in that value are recognized in profit or loss in the period of the change.
b) commodity broker-traders who measure their inventories at fair value less costs to sell. When such inventories are measured at fair value less costs to sell, changes in fair value less costs to sell are recognized in profit or loss in the period of the change.

Definitions

The following terms are used in this Standard with the meanings specified:

Inventories are assets:

a) held for sale in the ordinary course of business;
b) in the process of production for such sale; or
c) in the form of materials or supplies to be consumed in the production process or in the rendering of services.

Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm’s length transaction.

Measurement of inventories

Inventories shall be measured at the lower of cost and net realizable value.

Cost of Inventories

The cost of inventories shall comprise all **costs of purchase** *(direct purchase costs including direct taxes less any rebates)*, **costs of conversion** *(incurred both direct & indirect overheads in the event of conversion of raw materials/WIP to finished goods)* and **other costs** *(costs such as packaging, labeling and etc.)* incurred in bringing the inventories to their present location and condition.

Examples of cost **excluded** from the cost of inventories and recognized as expenses in the period in which they are incurred are:

a) abnormal amounts of wasted materials, labor or other production costs;

b) storage costs, unless those costs are necessary in the production process before a further production stage;

c) administrative overheads that do not contribute to bringing inventories to their present location and condition; and

d) selling costs.

Cost formulas

The cost of inventories of items that are not ordinarily interchangeable and goods or services produced and segregated for specific projects shall be assigned by using specific identification of their individual costs.

The cost of inventories, other than those described in above, shall be assigned by using the first-in first -out (FIFO) or weighted average cost formula. An entity shall use the same cost formula for all inventories having a similar nature and to the entity. For inventories with a different nature or use, different cost formulas may be justified.

Recognition as an expense

When inventories are sold, the carrying amount of those inventories shall be recognized as an expense in the period in which the related revenue is recognized. The amount of any write-down of inventories shall be recognized as an expense in the period the write-down or loss occurs.

Amount of any reversal of any write-down of inventories, arising from an increase in net realizable value, shall be recognized as a reduction in the amount of inventories recognized as an expense in the period in which the reversal occurs.

Disclosure

The financial statements shall disclose:

a) the accounting policies adopted in measuring inventories, including the cost formula used;
b) the total carrying amount of inventories and the carrying amount in classifications appropriate to the entity;
c) the carrying amount of inventories carried at fair value less costs to sell;
d) the amount of inventories recognized as an expense during the period;
e) the amount of any write-down of inventories recognized as an expense in the period;
f) the amount of any reversal of any write-down that is recognized as a reduction in the amount of inventories recognized as expense in the period;
g) the circumstances or events that led to the reversal of a write-down of inventories; and
h) the carrying amount of inventories pledged as security for liabilities.