IAS - 2

Inventories

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International Accounting Standard No 2 (IAS 2)

Inventories

This revised Standard replaces IAS 2 (revised 1993) existence, and will apply for annual periods beginning on or after January 1, 2005. Earlier application is encouraged.

Objective

1. The objective of this Standard is to prescribe the accounting treatment of stock. A key theme in the accounts of stocks is the amount of cost that should be recognized as an asset, be deferred until the relevant ordinary income to be recognized. This Standard provides a practical guide for determining this cost, as well as for the subsequent recognition as a cost of the exercise, including any deterioration which lowered the carrying amount to net realizable value. It also provides guidelines on the cost formulas that are used to assign costs to stocks.

Scope

2. **This Standard applies to all stocks, except:**

   (a) work in progress, from construction contracts, including service contracts directly related (see IAS 11, Construction Contracts);

   (b) financial instruments;

   (c) assets related biological farming and agricultural products at the point of harvest or collection (see IAS 41, Agriculture).

3. **This rule does not apply to the valuation of stock held by:**

   (a) Producers of agricultural and forest products, agricultural products after harvesting or collection, as well as minerals and mineral products, provided they are measured by their net realizable value, according to well-established practices in those sectors. In the event that these stocks are measured at net realizable value, changes in this value will be recognized in profit or loss in the occurrence of such changes.

   (b) Intermediaries that trade with raw materials listed, provided that its stock valued at fair value less selling costs. In the event that these stocks are counted by an amount that is fair value less selling costs, changes in this amount will be recognized in profit or loss occurring in them.

4. Stocks that have been referred to in paragraph (a) of paragraph 3 are valued by their net realizable value at certain stages of production. This occurs, for example, when they have collected agricultural crops or minerals have been removed, provided that their sale is secured by a term contract of whatever type or guaranteed by the government, or when there is an active market and the risk of failure in the sale is minimal. These stocks are excluded solely on valuation requirements set out in this Standard.

5. Brokers who trade are those who buy or sell commodities listed self or on behalf of third parties. Stocks that have been referred to in paragraph (b) of paragraph 3 are purchased mainly for the purpose of selling in the near future and generate earnings from fluctuations in price or a higher profit. When these stocks are accounted for at fair value less selling costs, will be excluded solely on valuation requirements set out in this Standard.

Definitions

6. **The following terms are used in this standard, with the meanings specified below: Existing assets are:**

   (a) owned to be sold in the normal course of business;

   (b) production process in the face of such sale, or

   (c) in the form of materials or supplies to be consumed in the production process or in providing services.

   Net realizable value is the estimated selling price of an asset in the normal course of business, less the estimated costs to complete its production and necessary to conduct the sale.

   Fair value is the amount by which it can be exchanged an asset or a liability canceled, among stakeholders and duly informed, engaged in a transaction at arm's length.

7. The net realizable value refers to the net amount that the entity expects to derive from the sale of stocks, in the normal course of business. The fair value reflects the amount by which this very existence could be exchanged on the market between buyers and sellers properly informed and interested. The first is a specific value for the entity, while the latter not. The net realizable value of stocks cannot be equal to fair value less selling costs.

8. Among stocks also include goods purchased and stored to resell, which include, for example, goods purchased by a retailer to resell to its customers, and also land or other real estate investments that are to be sold third. They are also stocks finished products or manufacturing underway by the entity, as well as materials and supplies to be used in the production process. In the case of a service provider, as described in paragraph 19, stocks include the cost of services for which the entity has not yet recognized the corresponding ordinary income (see IAS 18 Revenue).

Valuation of stocks

9. Inventories are valued at less than the cost or net realizable value.

Cost of stocks

10. The cost of stocks comprises all costs of acquisition and processing, as well as other costs they incurred to give them their current status and location.

Acquisition costs

11. The acquisition cost of stocks comprising the purchase price, import tariffs and other taxes (which are not recoverable, then the tax authorities), transport, storage and other costs directly attributable to the acquisition of goods, materials or services. The trade discounts, rebates and other similar items are deducted to determine the cost.

Costs of transformation

12. Processing costs of stocks include those costs directly related units produced, such as the workforce directly. They also include the one hand, calculated in a systematic way, indirect costs, fixed or variable, which incurred for transforming raw materials into finished products. Indirect costs are fixed all those who remain relatively constant, regardless of the volume of production, such as depreciation and maintenance of buildings and equipment of the factory, as well as the cost of management and administration of the plant. Indirect costs are all those variables that vary directly, or almost directly, with the volume of production, such as materials and labor indirectly.

13. The process of distribution of indirect costs to fixed processing costs is based on normal working capacity of the means of production. Normal production capacity is expected to achieve under normal circumstances, considering the average number of years or seasons, and taking into account the loss of capacity resulting from planned maintenance operations. You can use the actual level of production provided that closely approximates the normal capacity. The amount of indirect fixed costs distributed to each unit of production will not increase as a result of low production, or the existence of idle capacity. Indirect costs should not be recognized as expenses in the year in which they were incurred. In periods of abnormally high production, the amount of indirect cost distributed to each unit of production decline, so that no stocks are valued above cost. Indirect costs variables will be distributed to each unit of production, based on the actual level of use of means of production.

14. The production process can lead to the simultaneous production of more than one product. This is the case, for example, joint production or the production of major products alongside. When the costs of processing each type of product are not separately identifiable, the total cost will be distributed among the products, using uniforms and sound foundations. The distribution may be based, for example, the market value of each product, either as production under way at the time that products are beginning to be identified separately, or when they complete the production process. Most of the products, by their very nature, do not have significant value. When this is the case, is frequently measured by its net realizable value, that amount by deducting the cost of main product. As a result of this distribution, the carrying amount of the main product will not be significantly different from its cost.

Other costs

15. In calculating the cost of stock, will include other costs, in where it has been engaged in them to give them their current status and location. For example, it might be appropriate to include as cost of stocks, not some indirect costs stemming from the production or the cost of designing products for specific customers.

16. Examples of costs excluding the cost of stocks, and thus recognized as an expense in the year they are incurred, as follows:

    (a) abnormal amounts of waste materials, labor and other production costs;

    (b) storage costs, unless those costs might be needed in the production process, prior to a process of further development;

(c) indirect costs of administration that have not contributed to giving stocks their current condition and location and

(d) selling costs.

17. In IAS 23 Interest Costs, identifies the limited circumstances under which the financial costs would be included in the cost of stocks.

18. An institution may buy stocks with deferred payment. When the agreement contains an element of de facto financing, as can be, for example, the difference between the purchase price in normal appropriation and the amount paid, this element will be recognized as interest expense over the period of funding.

Cost of stocks for a service provider

19. In the event that a service provider to take stock, assess the costs involved in their production. These costs consist primarily of labor and other costs of personnel directly involved in providing the service, including supervisory personnel and other indirect costs distributable. The labor and other costs related to sales and general administration staff, will not be included in the cost of stocks, but be counted as expenses in the year in which it is incurred. The costs of stockpiled a service provider not include profit margins or non-distributable indirect costs that often are reflected in the prices charged by the service provider.

Cost of agricultural products collected from active biological

20. According to IAS 41 Agriculture, stocks that comprise agricultural products, that the entity has harvested or collected from its biological assets, is valued for its initial recognition, by fair value less the estimated costs at point of sale, considered at the time of harvest or collection. This will be the cost of stock on that date, for the implementation of this standard.

Systems for assessing costs

21. The systems for determining the cost of stocks, such as cost method or standard method of retailers, may be used for convenience provided the result of applying them comes close to cost. Costs standards will be established from normal levels of consumption of raw materials, supplies, manpower, efficiency and capacity utilization. In this case, the conditions of calculation will be reviewed on a regular basis and, if necessary, be changed standards as long as these conditions have changed.

22. The method of retailers is often used in the commercial sector retail, for the valuation of stocks, where there are a large number of items that rotate rapidly, which have similar margins and for which it is impractical to use other methods of calculation cost. In this method, the cost of stock is determined by deducting the purchase price of the article in question, an appropriate percentage of gross margins. The percentage applied will take into account the portion of stocks that have been marked below their original purchase price. It is often uses an average percentage for each section or commercial department.

Formulas cost

23. The cost of stockpiled goods that are not usually interchangeable with each other, as well as goods and services produced and segregated for specific projects shall be determined through the specific identification method of their individual costs.

24. The specific identification of cost means that each type of concrete cost will be distributed among certain items identified in stocks. This procedure will be adequate treatment for those products that segregation for a specific project, regardless of which have been produced by the entity or purchased abroad. However, the specific identification of costs will be inadequate when, in stocks, have a large number of products that are usually interchangeable. Under these circumstances, the method for selecting what individual products will remain in existence end could be used to obtain predetermined purpose in profit or loss.

25. The cost of stocks, other than those dealt with in paragraph 23, will be allocated using methods first inning, first out (FIFO) or weighted average cost. The entity uses the same formula of cost for all stocks that have a similar nature and use within it. For stocks with a different nature or use, can be justified using formulas cost too different.

26. For example, within the same entity, stocks used in a segment of exploitation can have a use other than that given to the same type of stocks, in another segment operating income. Notwithstanding the foregoing, the difference in the geographical location of stocks (or tax rules) is not, by itself, sufficient grounds to justify the use of different formulas cost.

27. The formula Fife, assumes that the products in stock purchased or produced before, will be sold first and, consequently, that products are in the end there will be those produced or purchased more recently. Using the method or formula weighted average cost, the cost of each unit of output will be determined on the basis of the weighted average cost of similar items, held at the beginning of the year, and the cost of the same items purchased or produced during the exercise. You can calculate the average periodically or after receiving each additional shipping, depending on the circumstances of the entity.

Net realizable value

28. The cost of stocks may not be recoverable if they are damaged, whether they have become partially or totally obsolete, or if their market prices have fallen. Also, the cost of stocks may not be recoverable if the estimated costs for its termination or sale have increased. The practice of lowering the balance until the cost is equal to net realizable value is consistent with the view according to which the assets are not valued in books over the amounts that are expected to get through sale or use.

29. Generally, the lowering of the value reaching the net realizable value is calculated for each item of stock. In some circumstances, however, might be appropriate to group similar or related items. This may be the case of stock items related to the same line of products, which have similar purposes or end-uses, are produced and sold in the same geographical area and cannot be, for practical reasons, evaluated separately from other items the same line. It will not be appropriate to undertake the sales value from items that reflect complete rankings of stocks, for example on all finished products, or on all stocks in a particular segment of exploitation. Service providers accumulate, generally, their costs for each service for which they wait to load a price separately to the

customer. Therefore, each service is identified and treated as a separate item.

30. Estimates of net realizable value is based on the most reliable information becomes available, when made, about the amount by which expects stocks. These estimates take into account fluctuations in prices or costs directly related to events after the closure, to the extent that these facts confirm existing conditions at year-end.

31. In making estimates of net realizable value, is taken into account the purposes for which they are kept stocks. For example, the net realizable value of the amount of stocks that have to meet sales contracts or services will be based on the price contained in the contract in question. If the sales contracts are for an amount less than that reflected in stock, the net realizable value of the excess will be determined on the basis of general sales prices. They may appear provisions or contingent liabilities by firm sales contracts that exceed the quantities of products in stock, or products to be obtained by purchase contracts firm. These provisions or contingent liabilities shall be treated for accounting according to IAS 37 Provisions, contingent liabilities and contingent assets.

32. Do not lower the value of raw materials and other supplies, kept for use in the production of stock, to place its carrying amount below cost, provided they expect the finished products to which they are sold to incorporate cost or above. However, when a reduction in the price of raw materials, indicating that the cost of finished products exceed its net realizable value is reduced its carrying amount to cover this difference. Under these circumstances, the replacement cost of raw materials may be the best available measure of its net realizable value.

33. An evaluation of the net realizable value in each subsequent year. When circumstances, which previously resulted in the lowering of value, have ceased to exist, or where there is clear evidence of an increase in net realizable value as a result of a change in economic circumstances, it will revert the amount of so that the new book value is among the lowest cost and net realizable value revised. This will occur, for example, when a stock, which accounted for their net realizable value, has dropped because its selling price is still in stock a year later and its selling price has been increased.

Recognition as an expense

34. **When stocks are sold, the carrying amount of them will be recognized as an expense in the year to recognize the corresponding ordinary income. The amount of any reduction in value, reaching the net realizable value, as well as all other losses in stocks, are recognized in the year occurs reduction or loss. The amount of any reversal of the reduction in value resulting from an increase in net realizable value, will be recognized as a reduction in the value of stocks, which have been recognized as an expense in the period in which recovery takes courage place.**

35. The cost of certain stocks can be incorporated into other asset accounts; such stocks are used as components of the work carried out by the entity, for tangible fixed assets. The value of stocks distributed to other assets in this way, will be recognized as an expense over the life of them.

Disclosure

36. Financial statements disclose the following information:

(a) the accounting policies adopted for the valuation of stocks, including the formula for assessing the costs which have been used;

(b) the total amount of stock in books, and sums according to the classification that is appropriate for that entity;

(c) the carrying amount of stocks to be accounted for at fair value minus cost of sales;

(d) the amount of stocks recognized as an expense during the period;

(e) the amount of sales value of stocks has been recognized as an expense in the year, in accordance with paragraph 34;

(f) the amount of reversals in the previous sales value, which has been recognized as a reduction in the amount of spending by stocks in the exercise, in accordance with paragraph 34;

(g) the circumstances or events that have resulted in the reversal of sales value, according to the said paragraph 34;

(h) the carrying amount of stock pledged as security for the discharge of debts.

37. Information about the carrying amount of different classes of stock, as well as the variation of such amounts in the exercise, would be useful to users of financial statements. A common classification of stocks is what distinguishes between goods and supplies for production, raw materials, products in progress and finished goods. Stocks of a service provider can be described simply as current products.

38. The amount of stocks recognized as an expense during the exercise, known as cost of sales cover costs previously included in the valuation of the products have been sold, as well as indirect costs undistributed and production costs of stocks by abnormal amounts. The particular circumstances of each entity could require the inclusion of other costs, such as distribution costs.

39. Some entities adopt a format for the presentation of income for the year in which figures are different from the figure for the cost of stock recognized as an expense during the year. Under this format, the entity will present an analysis of expenditures through a classification based on the nature of these expenses. In this case, the entity shall disclose the costs recognized as costs of raw materials and consumables, labor costs and other costs, along with the amount of net change in stocks for the year.

Effective Date

40. An entity shall apply this standard for annual periods beginning on or after January 1, 2005. Earlier application is encouraged. If an entity applies this standard to a period beginning before January 1, 2005, disclose that fact.

Repeal of other pronouncements

41. This Standard repealing existing IAS 2, revised in 1993.

42. This Standard repeals SIC-1 Consistency - different formulas for calculating the cost of stocks.