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Session 3- Inventory

Learning Objectives



Define inventories



Explain measurement and valuation of inventory



Understand the double entry principles for recording inventories

Definition Of Inventory

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Inventories are the assets produced or consumer goods in the production process.

Inventories include Assets:

Held for sale in the ordinary course of business (**finished goods**)

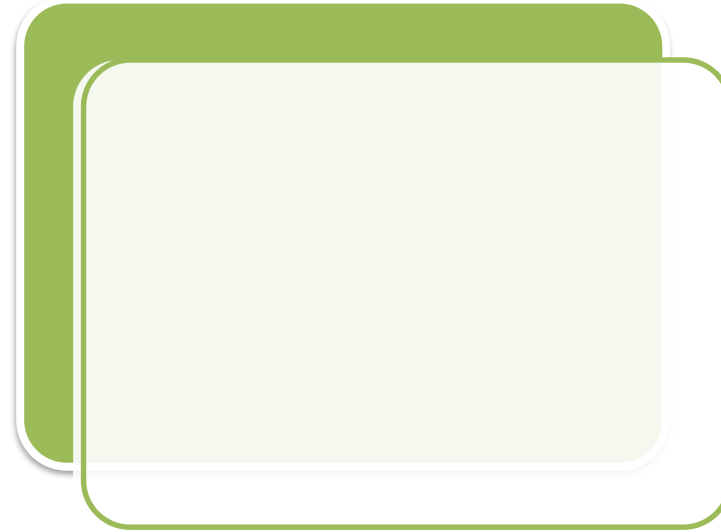
In the process of production for such sale (**work in process**)

In the form of materials or supplies to be consumed in the production process or in rendering a service (**raw materials**).

Fundamental Principle of Measuring

Inventory

Inventory is measured at the **lower of cost and net realizable value**.



Net realizable value: the estimated selling price less the estimated cost of completion and the estimated costs necessary to make the sale.

Cost: the price paid to acquire the asset

Measuring Inventory Cost

Initial inventory cost should include:

- costs of purchase (including taxes, transport, and handling) net of trade discounts received
- costs of conversion (including fixed and variable manufacturing overheads) and
- other costs incurred in bringing the inventories to their present location and condition

But excludes:

- Abnormal waste/loss
- Administrative overheads unrelated to production
- Selling cost

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- Storage cost
- foreign exchange differences arising from purchases invoiced in foreign currency
- interest cost when inventories are purchased with deferred settlement terms

Measuring Inventory Cost

- The standard cost and retail methods may be used for the measurement of cost, provided that the results approximate actual cost.

For inventory items that are not interchangeable, specific costs

For items that are interchangeable, IAS 2 allows the FIFO or weighted average cost formulas.

APPROACHES UNDER IFRS:

- Specific Identification

- First In First Out (FIFO)
- Weighted Average Cost

Example on Inventory Valuation

	Number	Cost per unit Ghc	Resalable Value Ghc
Toshiba	60	2,000	1,600

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- A company stocks and sells computers. They receive a stock of 200 computers of various brands. Due to changes in technology, the values of the computers have changed as presented in the table.

HP	75	1,650	1,800
Acer	30	1,700	1,600
Huawei	35	1,350	2,000

- To resell, an additional Ghc50 software installation is necessary. What is the value of inventory in its stores?

DOUBLE ENTRY FOR INVENTORY

Periodic Inventory System

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- When inventory is acquired, it is recorded as purchases

**Dr Purchases Cr Cash/Accounts
payable**

- When inventory is sold, they are recorded as sales

**Dr Cash/Accounts receivables
Cr Sales**

DOUBLE ENTRY FOR INVENTORY

- At the end of the year, an inventory count is done to ascertain the amount of inventory in store. This becomes the **closing inventory for the year**. This is recorded as:

Dr Inventory account

Cr P/L account

- At the beginning of the year the **closing stock is entered again as opening stock**.

Dr P/L account

Cr Inventory account

EXAMPLE

- As at 31st December 2018, KK Ltd had in stock Ghc2,500 worth of inventory. During 2019, purchases amounted to Ghc10,000 while sales were worth Ghc12,000 (cost price was Ghc8,000). In 2020, a further Ghc15,000 was purchased while goods costing Ghc11,000 were sold for Ghc16,500.
- Assume that no goods were damaged during the years under review.

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- Show the necessary double entries and financial statement extracts for the above.



Session 4 – Depreciation of Tangible Noncurrent Assets

Learning Objectives



Determine the value of tangible non-current assets

Identify methods of depreciating tangible non-current assets

Learn to make entries for depreciation in books of accounts

Accounting for Non-current Assets



Non-current asset –

This is that asset acquired to be used in the organisation for a period more than (normally) one year.

Such expenditure is referred to as **capital expenditure**; that type of expenditure to acquire an asset of a permanent nature; in contrast to revenue expenditure; the expenditure to acquire asset that is consumed within one year, or that exists for only one year.

Value of non-current assets

- Initial value of any non-current asset is the cost of the asset, which comprise of;
 - the purchase price of the asset
 - Carriage inwards on the asset
 - any additional/related expenditure incurred to put the asset in its usable state.

The Concept of Depreciation

RECALL:

Definition of Depreciation?

- It is the systematic allocation of the depreciable amount of an asset over its useful life (IAS 16).
- May be explained as the measure of wearing out, consumption or other reduction in the useful economic life of a non-current asset whether arising from use, efflux of time or obsolescence through technological or market changes.

Causes of Depreciation

The level of usage

The passage of time

Technological obsolescence

Market Obsolescence

- Any portion of non-current assets that is determined as having been used or consumed becomes an expense (Depreciation).

Methods for Charging Depreciation

- Different methods are applied based on the type of asset and usage, or based on the different assumptions that are made:

2 Common Methods:

- Straight line method
- Reducing balance or diminishing balance method

(Discussed in ACF 255)

Other methods: Sum of years' digits, revaluation method, machine hour method, depletion unit method, unites of output method

Accounting Entries

Purchase of Non-current Asset by cash

- DR Asset A/c
- CR Cash/Bank A/c

With the cost of the asset

When Depreciation is Charged for the year

- DR Depreciation Expense A/c
- CR Provision for Depreciation A/c(Accumulated Depreciation A/c)

With the depreciation charge for the period

Accounting Entries

At the end of the year

- Close off Depreciation Expense a/c to P/L account

At the end of the year

- Balance on provision for depreciation a/c remains as closing balance (Bal. c/d)

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Balance on provision for depreciation a/c used to determine the net book value (NBV) at year end.

NBV= cost – provision for depreciation bal. (accumulated depreciation)

Disposal of Non-current Assets

Disposal or sale of Non-current Asset

- DR Asset Disposal a/c
- CR Non-current asset a/c

With the cost price of the asset sold/disposed

Disposal or sale of Non-current Asset

- DR Provision for Depreciation a/c
- CR Disposal a/c

With the total depreciation already charged on the asset (bal. c/d at time of disposal)

Disposal of Non-current Assets

Disposal or sale of Non-current Asset

- DR Cash/ account receivables a/c
- CR Disposal a/c

With proceeds received/receivable on the disposal

Determine profit or loss on disposal

- DR Disposal a/c
- CR P/L a/c

With the profit on disposal

- Dr P/L a/c
- Cr Disposal a/c

With the loss on disposal

Example

Worksheet 2

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THE FINANCIAL DOCTOR

