AS-2

Objective:
The main purpose of inventory accounting is to figure out how much the inventory is worth in the financial statements until it is sold and generates revenue. This standard explains how to calculate that value, including the cost of inventory and any reduction in its value if it becomes worth less than expected.

Scope:
This standard applies to most types of inventories, but it **does not cover**:

1. Work in progress for construction projects or related services (covered by another standard).
2. Work in progress for businesses that provide services.
3. Shares, debentures, and other financial items treated as stock-in-trade.
4. Certain items like livestock, crops, or natural resources (like oil and gas) that are measured at their market value using established industry practices.

For the items in point 4, their value is often based on the price they can fetch in the market after they are ready for sale, like harvested crops or extracted minerals, especially when there's a guaranteed sale or a stable market. These are not covered by this standard.

Definitions

1. **Inventories** are assets such as:
   - Items held for sale (e.g., goods in a store).
   - Items being produced to sell later.
   - Raw materials or supplies used to create products or deliver services.
2. **Net Realisable Value** is the selling price of an item minus the costs required to finish it and sell it (e.g., packaging or delivery costs).
3. **What inventories include:**
   - Items bought for resale (e.g., merchandise, software, or property).
   - Finished goods, work in progress, raw materials, tools, and consumables for production.
   - Items like spare parts or equipment related to property or machines are **not** part of inventory; they fall under another standard (AS 10).

How Inventories are Valued

- Inventories are valued at the **lower of cost or net realisable value**.

What Makes Up the Cost of Inventories?

1. **Costs of Purchase:**
   - Purchase price, taxes, freight, and other directly related costs.
   - Subtract discounts, rebates, or duty refunds.

2. **Costs of Conversion:**
    - Costs directly related to production, like wages and materials.
    - Overheads:
        - **Fixed Overheads**: Costs like factory rent or depreciation that remain constant regardless of production.
        - **Variable Overheads**: Costs that vary with production, like utilities or indirect labor.
    - Overheads are allocated based on normal production capacity, not the actual volume (to avoid overpricing during low production).
3. **Other Costs:**
    - Any cost that helps bring inventory to its current state and location. For example, custom designs for customers.
    - **Interest and borrowing costs are usually excluded** unless directly related to the inventory.

Special Cases in Production

- If multiple products are produced together (e.g., joint products or by-products):
    - Costs are divided between them based on a fair method, like relative sales value.
    - Small-value by-products or waste can be measured separately at net realisable value and deducted from the cost of the main product.

What Costs are Excluded?

Some costs are **not included in inventory costs** and are recorded as expenses instead:

- Wasted materials or labor (unusual or excessive amounts).
- Storage costs (unless part of the production process).
- Administrative costs unrelated to inventory.
- Selling and distribution expenses.

Cost Formulas

1. **Specific Identification of Cost:**
    - Used for unique or special items, like goods set aside for specific projects.
    - Each item is assigned its actual cost.
    - Not suitable for large quantities of interchangeable items because it could unfairly manipulate profits.
2. **FIFO (First-In, First-Out):**
    - Assumes the oldest items are sold first, so the remaining inventory is the newest.

3. **Weighted Average Cost:**
   - The cost is calculated as an average of all similar items bought or produced during the period.
   - This average can be updated periodically or with each new purchase.

Techniques for Measuring Costs

1. **Standard Cost Method:**
   - Uses pre-set costs based on normal material usage, labor, and efficiency.
   - Regularly reviewed to ensure accuracy.
2. **Retail Method:**
   - Used in retail for quickly valuing large, fast-moving inventory.
   - Cost is estimated by subtracting a fixed percentage (gross margin) from the selling price.

Net Realisable Value (NRV)

- NRV is the selling price of an item minus the costs required to complete or sell it.
- Inventory is reduced (written down) to NRV if:
  - It is damaged, obsolete, or its selling price has dropped.
  - Costs to complete or sell it have increased.
- This ensures inventory is not valued higher than its expected sale value.

Special Cases

- Inventory write-downs are usually done **item by item**.
- In some cases, similar items in the same product line can be grouped for valuation.

When to Reassess Inventory Value

- Inventory value is reassessed at each balance sheet date.
- For items used in production, raw materials are not written down if finished products are expected to sell above cost.

Disclosure Requirements

Financial statements must disclose:

1. The method used to calculate inventory costs (e.g., FIFO, weighted average).
2. The total value of inventory, categorized as:

- Raw materials.
- Work-in-progress.
- Finished goods.
- Goods held for trading.
- Stores and spares.
- Loose tools.
- Any other specific type of inventory.

This transparency helps users of financial statements understand how inventory is valued and its impact on the company's finances.

AS-9

Introduction

1. **What this Standard Covers:**
   This standard explains how and when a business should recognize revenue (income) in its profit and loss statement. It applies to revenue earned from:
   - Selling goods.
   - Providing services.
   - Earning interest, royalties, or dividends from others using the business's resources.
2. **What this Standard Does NOT Cover:**
   Revenue recognition for specific cases, such as:
   - Construction contracts (covered under another standard).
   - Revenue from hire-purchase or lease agreements.
   - Government grants and subsidies.
   - Revenue from insurance contracts.
3. **What is NOT Considered Revenue:**
   Some items are not treated as revenue under this standard, for example:
   - Gains from selling or holding long-term assets (e.g., fixed assets).
   - Gains from changes in asset values (e.g., stock price increases or agricultural growth).
   - Gains from foreign exchange changes or translating foreign financial statements.
   - Gains from settling debts for less than the amount owed.
   - Unrealised gains (not yet earned or realised).

Definitions

1. **Revenue:**
   Revenue is the total amount a business earns from its regular activities, such as:
   - Selling goods.
   - Providing services.
   - Allowing others to use its resources (interest, royalties, dividends).

Revenue is the money charged to customers for goods and services. In cases where the business acts as an agent, the revenue is the commission it earns, not the total money collected.

2. **Completed Service Contract Method:**
   Revenue is recorded only after a service contract is fully or mostly completed.
3. **Proportionate Completion Method:**
   Revenue is recorded gradually as services are performed and completed in parts.

Explanation

1. **Key Focus:**
   The standard focuses on the **timing** of revenue recognition—when a business should record revenue in its profit and loss statement.

2. **Revenue Agreement:**
   The amount of revenue usually depends on the agreement between the business and its customer.

3. **Uncertainties:**
   If there is uncertainty about how much revenue will be earned or the related costs, the timing of revenue recognition might be delayed until these uncertainties are resolved.

Sale of Goods

1. **When to Recognize Revenue:**
   - Revenue from selling goods is recorded when the ownership (or control) of the goods is transferred from the seller to the buyer, and the seller receives payment.
   - Usually, ownership transfer happens along with the transfer of risks and benefits of owning the goods.
   - However, if risks and rewards transfer at a different time than ownership (e.g., delayed delivery or specific agreements), revenue is recognized when the risks and rewards are transferred.

2. **Special Cases:**
   - In industries like agriculture or mining, when goods are ready (e.g., crops harvested, ore extracted), revenue may be recorded at their expected selling price if a sale is almost guaranteed (e.g., under contracts or government guarantees). This amount is treated separately in the profit and loss statement.

Rendering of Services

1. **How to Recognize Revenue:**
   - **Proportionate Completion Method:**
     Revenue is recorded in parts as the service is performed (e.g., based on milestones, time spent, or other measurable progress). If services are spread evenly over time, revenue can be recorded evenly across the period.
   - **Completed Service Contract Method:**
     Revenue is recorded only after the service is fully or substantially completed. This is used when a service involves a single act or when the remaining tasks are significant enough to wait for full completion.

Use of Enterprise Resources by Others (Interest, Royalties, and Dividends)

1. **Interest:**
    - Revenue from interest is recorded over time, based on the amount of money owed and the applicable interest rate.
2. **Royalties:**
    - Revenue from royalties (e.g., payments for patents or copyrights) is recognized as per the terms of the agreement, unless a more appropriate method fits the situation.
3. **Dividends:**
    - Revenue from dividends (earned from shares) is recorded only when the right to receive payment is established.
4. **Uncertainty in Foreign Earnings:**
    - If earnings like interest, royalties, or dividends involve foreign exchange permissions and there is uncertainty, revenue recognition may be delayed.

Effect of Uncertainties on Revenue Recognition

1. **When to Recognize Revenue:**
    - Revenue is recorded only if it can be measured and collected reasonably.
    - If collection is uncertain (e.g., due to price changes, incentives, or delayed payments), revenue is recorded only when it is reasonably assured.
2. **Handling Uncertainty After Recognition:**
    - If uncertainty arises after revenue is recorded, it's better to create a separate provision (expense) instead of adjusting the original revenue amount.
3. **Delay in Revenue Recognition:**
    - If payment or value cannot be determined, revenue is postponed and recognized in the period when the uncertainty is resolved.

This ensures businesses only record revenue that is accurate, reliable, and reflective of actual transactions.

Main Principles

1. **When to Recognize Revenue:**
    - Revenue from sales or services is recognized **only when performance conditions are met**:
        - The seller has transferred ownership or the risks and rewards of the goods to the buyer.
        - There is no significant uncertainty about collecting the payment.
2. **Excise Duty Disclosure:**

- Revenue from sales should be shown as:

Turnover (Gross)

Less: Excise Duty

Turnover (Net)

- Excise duty linked to inventory changes (opening/closing stock differences) should be reported separately with an explanatory note.

Conditions for Revenue Recognition

- **For Sale of Goods:**
  Revenue is recognized when:
  - Ownership or risks and rewards of the goods have been transferred to the buyer.
  - The seller no longer has significant control over the goods.
  - The price is certain, and payment is reasonably assured.
- **For Services:**
  Revenue depends on the method of performance:
  - **Proportionate Completion Method:** Recognize revenue gradually as the work progresses.
  - **Completed Service Contract Method:** Recognize revenue only after the service is fully completed.
- **For Other Revenues:**
  - **Interest:** Recognized over time based on the outstanding amount and applicable rate.
  - **Royalties:** Recognized as per the agreement.
  - **Dividends:** Recognized when the company declares the right to payment.

Uncertainties in Revenue Recognition

- Revenue should not be recognized if there's uncertainty about:
  - Collecting the payment.
  - Finalizing the amount due (e.g., price escalations or export incentives).
- Any uncertainties arising later should be handled by setting aside a separate provision.

Illustrative Examples

1. **Sale of Goods:**
   - **Delayed Delivery at Buyer's Request:** Revenue can still be recognized if the goods are ready for delivery and billed.

- **Goods Delivered with Conditions:** Revenue is recognized only after the buyer accepts the goods, except for simple cases like installing a TV.

2. **Rendering Services:**
   - **Installation Fees:** Revenue is recognized only after installation is complete and accepted.
   - **Commissions (e.g., Advertising or Insurance):** Revenue is recognized when the service is completed, such as after an ad airs or a policy is renewed.
3. **Other Specific Cases:**
   - **Admission Fees for Events:** Recognized when the event occurs.
   - **Tuition Fees:** Spread over the duration of the course.
   - **Membership Fees:** Depending on the services, fees may be capitalized or allocated over time.

This framework ensures revenue is recorded only when it's earned and collectible, providing clarity and fairness in financial reporting.

AS-10

Simplified Summary of Accounting Standard (AS) 10: Property, Plant, and Equipment

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Objective

The standard specifies how to account for tangible fixed assets like property, plant, and equipment. It helps users of financial statements understand:

- The investment made in these assets.
- How their value changes over time through depreciation or impairment.

Scope

AS 10 applies to:

1. Tangible assets used in production, supply, or administration and expected to last more than a year.
2. Bearer plants (plants used to grow produce for over 12 months).

Exclusions:

- Biological assets related to agriculture, except bearer plants.
- Non-renewable resources like minerals, oil, or gas.

Other standards like AS 19 (Leases) or AS 13 (Investment Properties) might apply in specific cases.

Key Definitions

- **Property, Plant, and Equipment (PPE):** Tangible items used in operations for over a year.
- **Carrying Amount:** Asset's value after subtracting depreciation and impairment.
- **Depreciation:** Allocation of an asset's cost over its useful life.
- **Residual Value:** Estimated value at the end of the asset's useful life.
- **Useful Life:** Period or output expected from an asset.

Recognition Criteria

An asset is recognized if:

1. It will likely bring future economic benefits.
2. Its cost can be measured reliably.

Spare parts and tools are included in PPE only if they meet these criteria; otherwise, they are treated as inventory.

Initial and Subsequent Costs

1. **Initial Costs:** Include purchase price, transportation, installation, testing, and any required dismantling costs.
2. **Subsequent Costs:** Day-to-day servicing costs are **not capitalized** but treated as expenses. Major replacements or inspections can be capitalized if they meet recognition criteria.

Measurement at Recognition

Assets are measured at cost, which includes:

- Purchase price (after discounts).
- Direct costs to bring the asset to working condition (e.g., site preparation, delivery, installation).
- Decommissioning costs, if applicable.

Excluded Costs: Administrative expenses, initial losses, and advertising are not part of the asset's cost.

Self-Constructed Assets

- The cost includes materials, labor, and overheads.
- Wastage or abnormal costs are excluded.
- Interest on borrowed funds during construction may be added to the asset cost.

Bearer Plants

Bearer plants are accounted for like other PPE. Cultivation costs are included until they reach the desired condition to produce agricultural output.

Cost Measurement

Assets acquired in exchange for others are valued at **fair value** unless it's unreliable, in which case the carrying value of the given asset is used.

Key Takeaways

1. AS 10 ensures consistency in how companies recognize and measure fixed assets.
2. It separates costs into what can be capitalized as part of the asset versus what must be expensed.
3. Regular updates or replacements of significant components can increase the carrying amount of assets if justified.

This framework helps businesses maintain transparent and accurate financial records for their tangible assets.

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1. **Choosing an Accounting Model**:
    - Businesses must pick either:
        - **Cost Model**: Assets are carried at cost minus depreciation and impairment losses.
        - **Revaluation Model**: Assets are carried at their fair value, updated regularly, minus depreciation and impairment losses.
2. **Fair Value and Revaluation**:
    - Fair value is usually determined by market data or professional valuation.
    - If no market data exists, methods like discounted cash flows or replacement cost estimates are used.
    - Revaluations are done regularly to ensure the asset's book value reflects its market value.
3. **Handling Revaluation**:
    - On revaluation:
        - **Increase in value**: Added to a revaluation surplus in the equity, but may go to the profit and loss statement if reversing a previous decrease.
        - **Decrease in value**: Charged to the profit and loss statement, unless offset by a revaluation surplus.
    - All assets in the same category must be revalued to maintain consistency.
4. **Depreciation**:
    - **Definition**: Spreading the asset's cost over its useful life systematically.
    - Each significant part of an asset with different useful lives is depreciated separately.
    - Depreciation continues even if an asset is idle, but stops once fully depreciated or disposed of.
    - Common methods:
        - Straight-line: Equal depreciation each year.
        - Diminishing balance: Reducing depreciation over time.
        - Units of production: Based on usage/output.
    - The method must match how the asset's benefits are used and should be reviewed annually.
5. **Depreciable Amount and Residual Value**:
    - **Depreciable Amount**: Asset cost minus its residual value.
    - Residual value and useful life are reviewed yearly; adjustments are made as estimates change.
6. **Impairment**:
    - If an asset's value drops below its book value due to damage, market changes, or obsolescence, an impairment loss is recognized.
    - Impairments are evaluated using AS 28, "Impairment of Assets."

7. **Liability Changes (e.g., Decommissioning Costs)**:
   - If liabilities related to an asset change, adjustments are made to the asset's cost or the profit/loss statement.
   - Under the **Cost Model**, liabilities directly affect the asset's value, while under the **Revaluation Model**, they may affect the revaluation surplus or the profit/loss statement.
8. **Class of Assets**:
   - Assets are grouped by type (e.g., land, machinery, vehicles).
   - Revaluation or depreciation policies are applied uniformly within a group to avoid inconsistencies.

This explanation simplifies the technicalities of accounting for property, plant, and equipment while keeping the essential concepts intact. Let me know if you'd like further clarification on any specific section!

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1. **Compensation for Impairment**:
   - When a property or equipment is impaired, lost, or given up, compensation received from third parties should be recognized in the profit and loss statement when it's received.
   - Different events like impairments, compensation, or replacement of assets are treated separately.
2. **Derecognition**:
   - The carrying amount of an asset should be removed from the books when it's sold or no longer provides future economic benefits.
   - The gain or loss from this removal should be recorded in the profit and loss statement.
   - If assets are sold during regular business activities, they should be transferred to inventory at their book value, and proceeds from the sale should be recognized as revenue.
3. **Disclosure Requirements**:
   - Financial statements should disclose details like the depreciation method, asset value, changes in the asset value, and any restrictions or security on the assets.
   - If there are any changes in estimates related to depreciation, useful life, or asset disposal, they should be disclosed.
4. **Revaluation of Assets**:
   - If assets are revalued, the enterprise should disclose the date of revaluation, methods used, and the surplus from revaluation.
5. **Transitional Provisions**:
   - When new standards are applied, businesses can apply them to certain past transactions but need to adjust financial records accordingly.

This summarizes the key points related to the impairment, derecognition, and accounting for property, plant, and equipment in simpler terms.