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1. Effective Date

- 1.1 This policy is effective on **1 April 2024**.
- 1.2 This policy replaces the previous version of Financial Administration Manual (FAM) Chapter 1020-5 – Inventory issued on 18 June 2019.
- 1.3 The policy was approved by the Assistant Deputy Minister, Finance (ADM(Fin)) on **1 April 2024**.

2. Application

- 2.1 The purpose of this FAM chapter is to define the Department of National Defence (DND) and Canadian Armed Forces (CAF) financial management (FM) policy on Inventory. It details the policy requirements for the appropriate accounting and reporting of Inventory in the DND/CAF.

3. Context

- 3.1 DND manages billions of dollars' worth of inventory, stored in facilities all over the world. Inventory is used to support every aspect of DND's operations, from completing missions to administering its internal services. DND's financial management of inventory is frequently subject to review to ensure compliance with accounting principles.
- 3.2 Due to the nature and complexity of its programs, the department and the CAF are faced with unique situations that may not be addressed or fully articulated under GC 4200 Inventories, part of the Treasury Board (TB) Directive on Accounting Standards. This FAM chapter serves to outline and explain the DND/CAF inventory financial policies in these circumstances.
- 3.3 This financial policy must be read in conjunction with and after reading the Directive on Accounting Standards: GC 4200 Inventories.
- 3.4 Certain paragraphs of this FAM Chapter reference International Public Service Accounting Standard (IPSAS) 12. Only the paragraphs of IPSAS 12 that are specifically referenced in this FAM Chapter are applied as part of the department's FM policy for inventory.
- 3.5 All financial documentation supporting the transactions must be retained for six years from the end of the fiscal year in which the transaction takes place. When an Accounts Receivable is created, all documentation is retained until the account is cleared. When a criminal, disciplinary or recovery action is taken, all documentation must be retained and protected for six fiscal years after the process is completed.
- 3.6 See [Appendix A](#) for the definitions applicable to this policy and a list of acronyms used.

4. Objectives and Expected Results

4.1 The objectives of this policy are to:

- Ensure that DND/CAF's inventory items are recognized and valued appropriately;
- Ensure that all subsequent transactions, changes in condition and consumption of DND/CAF's inventory items over their lifecycle are appropriately recorded on a timely basis in the department's [financial management system](#) (FMS);
- Identify the DND/CAF key stakeholders involved with the financial management of inventory and outline their roles and responsibilities; and
- State and explain the DND/CAF FM policies and standards for inventory that are not addressed in the TB Directive on Accounting Standards: GC 4200 Inventories.

4.2 The expected results of implementing this policy are:

- Inventory values are fairly presented in the departmental financial statements and the Public Accounts of Canada; and
- Key DND/CAF stakeholders are aware of and understand their roles and responsibilities with respect to inventory.

5. Requirements

Definition of Inventory

5.1 Inventory are purchased or produced goods that are not immediately consumed, as defined in GC 4200.01.

5.2 Further to GC 4200.01 b), inventory would exclude the following:

- [Tangible capital assets](#) (TCAs) as defined in FAM chapter 1020-4, paragraph 4.2.1;
- Items that meet the capitalization criteria of a TCA as defined in paragraph 5.1 of [FAM chapter 1020-4 Tangible Capital Assets](#), but their cost falls below the applicable capitalization threshold; and
- Items accounted for as Asset Pooled Items (API) as defined in Appendix B of [FAM chapter 1020-4 Tangible Capital Assets](#).

5.3 Examples of inventory include, but are not limited to, the following:

- Ammunition;
- Medication;
- Fuel and lubricants;
- Rations;
- Nails, nuts, bolts and screws; and
- Construction materials.

5.4 All items that meet the definition of inventory in [paragraphs 5.1](#) and [5.2](#) for which title has passed to the Crown that are under the control of DND shall be included in DND's inventory (GC 4200.03), even if the inventory is held by contractors.

- 5.5 When a kit contains one or more items that meets the policy criteria for inventory, those items must be accounted for separately as inventory in accordance with this FAM chapter.

Measurement of Inventories

- 5.6 Inventories are measured at the lower of cost and [net realizable value](#) (NRV) (IPSAS 12.15), except for inventories held for distribution at no or nominal charge which shall be measured at the lower of cost and current replacement cost (GC 4200.10).

Cost

- 5.7 For inventories of raw materials, goods purchased for resale and for internal consumption, the cost includes all costs incurred in acquiring the item, including duties, shipping and handling charges but excluding Goods and Services Tax (GST), Harmonized Sales Tax (HST) and Quebec Sales Tax (QST) (GC 4200.06). In accordance with IPSAS 12.19, applicable trade discounts, rebates and other similar items are also excluded from the cost of inventory.
- 5.8 For work in process and finished goods, the cost includes all direct costs of materials and services, plus the cost of direct labour applied to the product. [Overhead costs](#) directly attributable to production should also be included in the cost (GC 4200.07).
- 5.9 Costs that should be excluded from the cost of inventories and expensed in the period they are incurred include: (GC 4200.11)
- Abnormal amounts of wasted materials, labour, or other production costs;
 - Storage costs, unless those costs are necessary in the production process before a further production stage;
 - Administrative overheads that do not contribute to bringing inventories to their present location and condition; and
 - Selling costs.

Inventory Costing Methods

- 5.10 In accordance with GC 4200.05, several methods are used in determining inventory cost, such as specific identification, average cost, first in, first out (FIFO), and standard costing. The method selected for determining cost should be one that results in the fairest matching of costs against program delivery activity, regardless of whether or not the method corresponds to the physical flow of goods.
- 5.11 Moving weighted average cost is the only method to measure the cost of inventory that is currently approved for use at DND.
- 5.12 The chosen costing method (i.e. valuation methodology) for the departmental FMS must be applied consistently and documented for audit purposes. The same costing method must be used for all inventories that have a similar nature and use.
- 5.13 The costing method may be changed if the new method is a better match of costs against program delivery activity.

- 5.14 The selection of a costing method or a change in the costing method must be approved by Asset and Inventory Strategy and Analysis (AISA), in consultation with Director Financial Systems Integration (DFSI).

Impairment of Inventories

- 5.15 Further to GC 4200.12, inventories that no longer have service potential or have reduced service potential should be valued at the lower of cost or NRV. Impairments are accounted for as follows:
- Obsolete items, which are no longer considered to be usable, should be disposed of and expensed;
 - Surplus items, which are no longer deemed to have service potential, should be valued at the lower of cost or NRV;
 - Damaged items should be valued at the lower of cost or NRV; and
 - Missing and lost items, which are no longer in inventory due to shortages, loss by fire, theft, or unauthorized distribution (e.g. fraud and negligence) should be expensed.
- 5.16 In accordance with IPSAS 12.38, the cost of impaired inventories may not be recoverable. The practice of writing inventories down below cost to NRV is consistent with the view that assets are not to be carried in excess of the future economic benefits or service potential expected to be realized from their use, sale, exchange or distribution.
- 5.17 Expenses for impairments of inventory are to be recognized in the period in which the impairment occurs.
- 5.18 In accordance with IPSAS 12.42, when the circumstances that caused inventory to be impaired no longer exist, or when there is clear evidence of an increase in the NRV of impaired inventory because of changed economic circumstances, then an amount of the write-down must be reversed. The amount of the reversal cannot exceed the amount of the original write-down, and the new value of inventory must remain the lower between the cost and the NRV. Reversals of impairments of inventory are recognized as a reduction in the expense of inventory in the period in which the reversal occurs.

Recognition

- 5.19 Inventory is recognized as an expense in the same period in which it is used, sold, exchanged or distributed to other parties for no charge or for a nominal charge. Inventory is also recognized as an expense when the related service is rendered.
- 5.20 When inventory is consumed as part of the creation of a TCA, the cost of the inventory is added to the cost of the TCA so that it can be amortized over the new TCA's useful life (i.e. included in the TCA's amortization expense). For more information, refer to the subsection "Internally Constructed TCAs" in [FAM chapter 1020-4 Tangible Capital Assets](#).
- 5.21 When inventory is consumed as part of a betterment to an existing TCA, the cost of the inventory is added to the cost of the TCA so that it can be amortized over the

existing TCA's useful life. When inventory is consumed as part of repairs and maintenance to an existing TCA, the cost of the inventory is expensed. For more information on betterments and repairs and maintenance, refer to the section "Added Costs for Existing Assets" in [FAM chapter 1020-4 Tangible Capital Assets](#).

- 5.22 Inventory is funded from the operating expenditures vote (Vote 1), except for inventory that will be capitalized after it is consumed as part of the creation or betterment of a TCA, which is funded from the capital expenditures vote (Vote 5). For further guidance, please refer to the [Vote Usage Guide for Projects at DND](#).

6. Roles and Responsibilities

Deputy Minister

- 6.1 The Deputy Minister (DM) is responsible for:

- Implementing an effective framework for the management of assets including inventory.

Assistant Deputy Minister (Finance)/Chief Financial Officer

- 6.2 The Assistant Deputy Minister, Finance/Chief Financial Officer (ADM(FIN)/CFO) is responsible for:

- Overseeing the implementation and monitoring of this policy.

Director General, Strategic Financial Governance

- 6.3 The Director General, Strategic Financial Governance (DGSFG) is responsible for:

- Supporting the implementation and monitoring of compliance with this policy.

Director General, Financial Operations and Services

- 6.4 The Director General, Financial Operations and Services (DGFOS) is responsible for:

- Ensuring the accuracy and reasonableness of departmental financial accounting and reporting of inventory, in compliance with relevant legislation, regulations and all applicable FM policy instruments;
- Ensuring that appropriate departmental FM inventory processes are in place to promote compliance with this policy; and
- Ensuring departmental compliance with this policy is monitored.

Director, Financial Accounting

- 6.5 The Director, Financial Accounting (DFA) is responsible for:

- Preparing the departmental financial statements and submissions for the Public Accounts of Canada in compliance with relevant legislation, regulations and all applicable FM policy instruments;

- Monitoring, validating, processing financial transactions and when required, accounting adjustments related to inventory transactions and account balances to ensure compliance with this policy; and
- Exercising a challenge function and, where appropriate, revising the accounting treatment for inventory to ensure that the department's financial statements are accurate and reasonable.

Asset and Inventory Strategy and Analysis

6.6 Asset and Inventory Strategy and Analysis (AISA) is responsible for:

- Overseeing the day-to-day application and monitoring of this policy;
- Developing and maintaining the department's FM processes and procedures for inventory to ensure that they are effective, efficient, incorporate appropriate internal controls, comply with legislative, regulatory and financial policy requirements, except for those that are developed by DFSI;
- Performing the ongoing corporate consolidation and any added central processing required to appropriately capture period activity and reflect the appropriate adjusted balances for inventory;
- Determining which items owned by DND meet the definition of inventory as defined in this FAM chapter;
- Ensuring that inventory that has been impaired (obsolete, surplus, damaged items, etc.) is accurately valued in the departmental FMS at the lesser of cost and NRV based on the information reported by RC Managers; and
- Ensuring that all TCAs recorded in the departmental FMS, including API, are properly identified to exclude them from inventory valuation.

Capital Assets Reporting Monitoring and Analysis

6.7 Capital Assets Reporting Monitoring and Analysis (CARMA) is responsible for:

- Defining and developing departmental FM policy for inventory; and
- Providing policy interpretation assistance on complex inventory FM policy matters.

Director, Financial Systems Integration

6.8 The Director, Financial Systems Integration (DFSI) is responsible for:

- Ensuring the effective management of the departmental FMS for the recording and reporting of all financial transactions, including inventory; and
- When ADM(Fin) is not the lead for inventory process or procedures with financial implications, developing and maintaining the FM component of these processes and procedures to ensure that they are effective, efficient, incorporate appropriate internal controls, comply with legislative, regulatory and financial policy requirements;
- Supporting the implementation and monitoring of this policy; and
- Providing ongoing oversight and monitoring of the department's inventory financial processes.

Director, Financial Controls

6.9 The Director, Financial Controls (DFC) is responsible for:

- Assessing the effectiveness of internal controls related to inventory and making recommendations on how to improve existing controls and create additional required internal controls, based on the results of the assessments;
- Supporting the implementation and monitoring of this policy; and
- Providing ongoing oversight and monitoring of the department's internal controls over the FM of inventory.

Level One Comptrollers

6.10 Level One (L1) Comptrollers are responsible for:

- Advising RC Managers on identifying procured items as inventory based on guidance provided by AISA;
- Ensuring that all inventory information entered into the departmental FMS by users within their L1 organization meets the requirements of FM policies and FM procedures and is complete, accurate and timely;
- Advising RC Managers on determining the NRV of inventory for impairments;
- Collecting data on contractor held/managed inventory such as quantities held, as well as data on items consumed, disposed or written off, so that it can be entered into the departmental FMS; and
- Informing independent contractors of their obligations to report quantities and costs of DND inventory that they manage on behalf of the department as per contractual arrangements made.

Responsibility Centre Managers

6.11 Responsibility Centre (RC) Managers are responsible for:

- Identifying procured items as inventory based on guidance provided by their L1 Comptroller;
- Entering inventory information into the departmental FMS in accordance with the requirements of FM policies and FM procedures on a timely basis, including acquisitions, consumption, unrecorded (missed) assets, and disposals; and
- Ensuring that impaired inventory is recognized and valued appropriately:
 - Identifying when inventory no longer has service potential or has reduced service potential (when inventory is obsolete, surplus, damaged or missing);
 - Determining the NRV of that inventory in consultation with their comptroller staff or the Regional Departmental Accounting Office (RDAO);
 - Reassessing the NRV on a regular basis; and
 - Reporting this information to AISA through the financial chain of command.

Regional Departmental Accounting Office Comptrollers

- 6.12 Regional Departmental Accounting Office (RDAO) Comptrollers are responsible for:
- Ensuring that managers within their area of responsibility are properly applying this policy; and
 - Providing guidance and assistance to managers in applying this policy.

7. Consequences of Non-Compliance

- 7.1 Under the TB Policy on Financial Management, the DM is responsible for investigating and acting when significant issues regarding policy compliance arise, and ensuring that appropriate remedial action is taken to address such issues within DND/CAF. The TB Framework for the Management of Compliance provides guidance on the considerations for determining the possible mix of consequences, which include the impact of the non-compliance, whether there has been a history of non-compliance, was there intent and other circumstances.
- 7.2 To support the DM's responsibility under the TB Policy on Financial Management, the ADM(FIN)/CFO or in the case of a member of the CAF, the military chain of command at the ADM(FIN)/CFO's direction, must ensure corrective actions are taken to address instances of non-compliance with this policy. Corrective actions can include a requirement for additional training, changes to procedures or systems, removal or suspension of delegated financial authorities on a temporary or permanent basis, disciplinary action or other measures as appropriate.

8. References

8.1 Treasury Board and Central Agency FM Policy Instruments

[TB Directive on Accounting Standards](#)
[GC Handbook 4200 Inventories](#)

8.2 DND/CAF FM Policies

[FAM Chapter 1020-4 – Tangible Capital Assets](#)

8.3 Other Accounting Standards

IPSAS 12 Inventories

9. Enquiries

- 9.1 Questions on policy interpretation and clarification are to be addressed to the appropriate Comptroller.
- 9.2 If the local Comptroller requires assistance, the question will be escalated through the financial chain of command.

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- 9.3 If the L1 Comptroller needs guidance on the matter(s) raised, the L1 Comptroller may contact AISA.
- 9.4 If AISA needs guidance on the matter(s) raised, they may contact the FM policy analyst at CARMA.

Appendix A – Definitions and Acronyms

Definitions

Financial Management System (Système de gestion financière) is any combination of business processes (end-to-end, automated and manual), procedures, controls, data and software applications, all of which are categorized as either a departmental financial and materiel management system or program system or central system that produces financial information and related non-financial information. DND's departmental FMS includes DRMIS and would also include any future replacement of DRMIS.

Net realizable value (Valeur de réalisation nette) is the estimated value of an item that can be realized upon its disposal less a reasonable estimate of the costs associated with the disposal of the item.

Overhead costs (Frais généraux) are all indirect costs that are incurred in converting materials into finished goods. Examples of overhead costs include the following:

- Utilities;
- Indirect labour; and
- Repairs and maintenance and amortization of TCAs.

Tangible capital assets (Immobilisations corporelles) are non-financial assets having physical substance that meet the criteria of a capital asset and include such diverse items as roads, buildings, vehicles, equipment, land, water and other utility systems, aircraft, computer hardware and software, dams, canals, and bridges.

Acronyms

ADM(Fin) – Assistant Deputy Minister (Finance)

ADM(Fin)/CFO – Assistant Deputy Minister (Finance)/Chief Financial Officer

AISA – Asset and Inventory Strategy and Analysis

API – Asset Pooled Items

CAF – Canadian Armed Forces

CARMA – Capital Assets Reporting Monitoring and Analysis

DFA – Director Financial Accounting

DFC – Director Financial Controls

DFSI – Director Financial Systems Integration

DGFOS – Director General Financial Operations and Services

DGSFG – Director General Strategic Financial Governance

DM – Deputy Minister

DND – Department of National Defence

FAM – Financial Administration Manual

FIFO – First In, First Out

FM – Financial Management

FMS – Financial Management System

GST – Goods and Services Tax

HST – Harmonized Sales Tax

L1 – Level One

NRV – Net Realizable Value

QST – Quebec Sales Tax

RC – Responsibility Centre

RDAO – Regional Departmental Accounting Office

TB – Treasury Board

TCA – Tangible Capital Asset