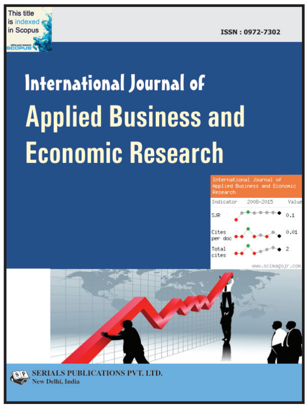

International Journal of Applied Business and Economic Research

ISSN : 0972-7302

available at http: www.serialsjournal.com

Volume 15 • Number 4 • 2017

A Note on Inventory Reporting by Selected Indian Automobile Firms

Abhishek Ranga[1]

[1] *Associate Professor, Goa Institute of Management. Email: abhishek@gim.ac.in*

ABSTRACT

The study is an attempt to examine the disclosure made by selected Indian Automobile firms regarding inventory valuation. Various accounting standards like AS-2, AS-5 and AS-1 requires certain disclosures to be made by Indian firms in its annual report as a note to accounts. Disclosures like accounting policies adopted in measuring inventories, including the cost formula used, total carrying amount of inventories and its classification appropriate to the enterprise needs to be classified. Any change in accounting policy needs to be disclosed; preferably an explanation for the need to change the policy should be disclosed.

JEL Classification: M41, G14, G1

Keywords: Inventory Disclosure, Accounting Standard.

1. INTRODUCTION

This study attempts to examine the level of compliance by selected Indian Automobile firms with the inventory disclosure requirement of Indian GAAP. Various accounting standards mention about the inventory related disclosure, as follows:

(i) As per para 26 of accounting standard-2, on valuation of inventories (here after AS-2) the financial statements should disclose:

   (a) The accounting policies adopted in measuring inventories, including the cost formula used.

   (b) The total carrying amount of inventories and its classification appropriate to the enterprise.

(ii) As per para 27 of AS-2, disclosure should be made on information about the carrying amounts held in different classifications of inventories and the extent of the changes in these assets. Common classifications of inventories are raw materials and components, work in progress, finished goods, stores and spares, and loose tools.

(iii) As per para 14 (a) of accounting standard – 5, on Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies (here after AS-5) the write-down of inventories to net realisable value as well as the reversal of such write-downs needs to be disclosed in the annual report.

(iv) As per para 20 of AS-5, estimates for inventory obsolescence needs to be disclosed

(v) As per accounting standard-1 (here after AS-1) on Disclosure of Accounting Policies and para 32 of AS-5, any change in accounting policy needs to be disclosed. Preferably an explanation for the need to change the policy should be disclosed.

2. SAMPLE FIRMS

For the study following firms were identified

(i) Amtek Auto Ltd.

(ii) Ashok Leyland Ltd.

(iii) Bajaj Auto Ltd.

(iv) Castex Technologies Ltd.

(v) Ceat Ltd.

(vi) Dynamatic Technologies Ltd.

3. REPORTING AND ANALYSIS

(i) Amtek Auto Ltd.

Inventory Policy as reported in the annual report for the accounting year 2014-15: Raw Materials, Stores, Spares & dies, Goods under process and Finished Goods are valued at cost or Net Realizable Value, whichever is lower. Waste and Scrap is valued at Net Realizable Value. Cost of inventories of Raw Materials and Stores and Spares is ascertained on FIFO Basis. Cost of goods under process and finished goods comprise of cost of materials, production overhead and depreciation on plant and machinery. Cost of material for this purpose is ascertained on First in First out basis. Provision for obsolescence in inventories is made, whenever required.

Only Material cost is as per FIFO not total cost which includes production overhead and depreciation on plant and machinery. The allocation of production overheads may vary as per the production level. AS 2 requires cost formula to be applied on total inventory cost, material cost in only one component of the inventory cost. Thus this is not in compliance with the requirements of AS-2.

(ii) Ashok Leyland Ltd.

Inventory Policy as reported in the annual report for the accounting year 2014-15:

(a) Inventories are valued at lower of cost and net realisable value; cost being ascertained on the following basis:

- Stores, raw materials and components and work-in-progress: On monthly moving weighted average basis.
- spares, consumable tools: weighted average basis

In respect of works-made components, cost includes applicable production overheads.

- Finished/trading goods: under absorption costing method.

(b) Cost includes taxes and duties and is net of eligible credits under CENVAT/VAT Schemes.

(c) Cost of patterns and dies is amortised over a period of five years.

(d) Surplus/obsolete/slow moving inventories are adequately provided for.

Finished goods and trading goods are valued based on absorption costing as the disclosure states, the cost formula (FIFO or Weighted average) used for valuing inventory is not disclosed for finished and trading goods. This is not in compliance with the requirements of AS-2.

(iii) Bajaj Auto Ltd.

Study Period: AY 2007-08 to AY 2015-16 (9 years), During this period Dalal and Shah LLP were the auditor for Bajaj Auto Ltd (BAL). Dalal and Shah LLP is a member firm of PwC Network. During the period BAL for calculating its cost of inventories included all costs of purchases, cost of conversion and other costs incurred in bringing the inventories to their present location and condition in the inventory cost, which is in compliance with the requirements of AS-2.

Finished stocks, auto spare parts and work-in-progress are valued at cost or net realisable value whichever is lower. Finished stocks lying in the factory premises, Branches, Depots are valued inclusive of excise duty. Though the valuation policy is in compliance with AS-2, but the cost formula (FIFO or weighted average) used for the calculation of cost was not disclosed in any of the annual report under study, which is departure from the requirements of AS-2.

During AY 2007-08 to AY 2013-14 stores and tools were valued at cost arrived at on weighted average basis. However, obsolete and slow moving items were valued at cost or estimated realisable value whichever was lower. Irrespective of the inventory type AS-2 requires that each inventory to be valued at lower of cost and net realisable value, BAL from the AY 2014-15 started valuing stores, packing material and tools are at cost arrived at on weighted average basis or net realisable value, whichever is lower, which is in alignment with AS-2.

Raw materials and components are valued at cost arrived at on weighted average basis or lower of cost and net realisable value, as circumstances demand. However, obsolete and slow moving items are valued at cost or estimated realisable value whichever is lower. This is in alignment with AS-2.

Machinery spares and Maintenance materials are charged out as expense in the year of purchase. However, Machinery spares forming key components specific to a machinery and held as insurance spares are capitalised along with the cost of the Asset. This is in alignment with AS-2.

Goods in transit are stated at actual cost incurred upto the date of Balance Sheet, AS-2 requires that each inventory to be valued at lower of cost and net realisable value, thus this is departure from the requirements of AS-2, also cost formula (FIFO or weighted average) not specified.

(iv) Castex Technologies Ltd.

Inventory Policy as reported in the annual report for the accounting year 2014-15: Raw Materials, Stores, Spares & Dies, Goods under process and Finished Goods are valued at cost or Net Realizable Value, whichever is lower. Waste and Scrap is valued at Net Realizable Value. Cost of inventories of Raw Materials and Stores and Spares is ascertained on FIFO Basis. Cost of goods under process and finished goods comprise of cost of materials, production overhead and depreciation on plant and machinery. Cost of material for this purpose is ascertained on First in First out basis. Provision for obsolescence in inventories is made, whenever required.

Only Material cost is as per FIFO not total cost which includes production overhead and depreciation on plant and machinery. The allocation of production overheads may vary as per the production level.

(v) Ceat Ltd.

Inventory Policy as reported in the annual report for the accounting year 2014-15:

(a) Raw materials, components, stores and spares are valued at lower of cost and net realizable value. However, materials and other items held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at or above cost. Cost is determined on a weighted average basis. Cost of raw material is net of duty benefits under Duty Entitlement Exemption Certificate (DEEC) scheme.

(b) Work-in-progress and finished goods are valued at lower of cost and net realizable value. Cost includes direct materials and labour and a proportion of manufacturing overheads based on normal operating capacity. Cost of finished goods includes excise duty. Cost is determined on a weighted average basis.

(c) Traded goods are valued at lower of cost and net realizable value. Cost includes cost of purchase and other costs incurred in bringing the inventories to their present location and condition. Cost is determined on a weighted average basis.

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

In point (a), It appears that firm is referring to Raw material or components, ideally the inventory value should not be decided based on the value of finished goods.

(vi) Dynamatic Technologies Ltd.

Inventory Policy as reported in the annual report for the accounting year 2014-15:

(a) Inventories are carried at the lower of cost and net realisable value.

(b) Cost of inventories comprises purchase price and all incidental expenses incurred in bringing the inventory to its present location and condition. The method of determination of cost is as follows:

- Raw materials and components – on a weighted average basis
- Stores and spares – on a weighted average basis

- Work-in-progress – includes costs of conversion
- Finished goods – includes costs of conversion
- Goods in transit – at purchase cost

The Company in the current year has revised its method of valuation of inventories to weighted average as compared to first in first out (FIFO) in the previous year. In the view of the Management, the revised policy would result in a more appropriate presentation of its financial statements. Had the Company followed FIFO method for valuation of inventories, the value of inventories as at 31 March 2015 would have increased from ₹8,256 lacs to ₹8,315 lacs and resultant increase in profit before tax from ₹2,978 lacs to ₹3,037 lacs.

(c) Fixed production overheads are allocated on the basis of normal capacity of production facilities.

(d) The comparison of cost and net realisable value is made on an item-by-item basis.

(e) The net realisable value of work-in-progress is determined with reference to the net realisable value of related finished goods. Raw materials and other supplies held for use in production of inventories are not written down below cost except in cases where material prices have declined, and it is estimated that the cost of the finished products will exceed their net realisable value.

(f) The provision for inventory obsolescence is assessed on a quarterly basis and is provided as considered necessary.

Good disclosure made (pls. refer to point-*b*) with regard to change in accounting policy. Explanation with proper effect on inventory value and Profits have been provided by the firm.

Refrences

AS 1, Disclosure of Accounting Policy.

AS 2, Valuation of Inventory.

AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies.

Amtek Auto Ltd Annual Report 2014-15.

Ashok Leyland Ltd Annual Report 2014-15.

Bajaj Auto Ltd Annual Report (AY 2007-08 to AY 2015-16).

Castex Technologies Ltd Annual Report 2014-15.

Ceat Ltd Annual Report 2014-15.

Dynamatic Technologies Ltd Annual Report 2014-15.