

INVENTORY EVALUATION AT STOCKTAKING

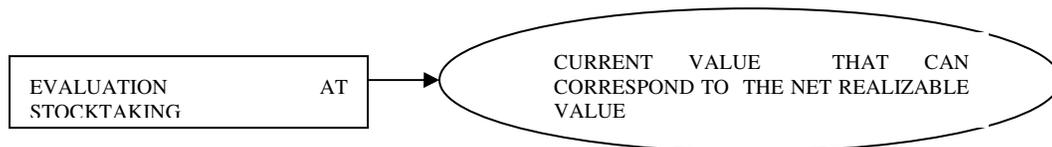
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Abstract: All companies perform the inventorying of their patrimony, (including the stockable items, at the beginning of their activity, on the occasion of mergers or liquidations, whenever it is necessary during the accounting period, (due to internal need for information, replacing the gestionarului, etc.) and compulsorily at the end of the accounting period before drawing up the financial statements. I have treated, in my article, problems related to inventory evaluation at stocktaking, the method used for their inventory, the settlements of shorts and overs at stocktaking, setting the values that will be recorded following the stocktaking as well as the inventory evaluation at stocktaking according to the rules applicable in other countries.

Key words: stocks, stocktaking, settlement, current value, book value, inventory evaluation

Irrespective of the nature of their activities, all companies perform the inventory of their patrimony, (including the stockable items), usually at the end of the year, when these items are evaluated at their **current value** also known as book value that can correspond to the **net realizable value** (representing the assessed price that could be obtained during the normal activity, minus the costs estimated for the product finishing or/and the costs necessary for its sale).



However, we can ask the question: “What are the guidelines of the economists and the other specialists involved in the calculation of the value of the stocks to be inventoried?”

From practical research and by studying the applicable regulations, we can assert that, besides the indications provided by the norms concerning the organization and performance of stocktaking of the asset and liability items, professionalism is needed both for the actual performance of the assessment of the real quantities in stock and also for the evaluation of their book value.

Although my intention is not to mention aspects related to the organization, I would like to specify a few recommendations that are useful to entities in their stocktaking.

For example:

The evaluation of factual stocks is made by counting, weighing, measurements or cubation, on a case-by-case basis. The goods found in their intact original packages are only unpacked at random, this method being mentioned in the related inventory lists.

For **liquids** (thinners, paint, varnishes, etc.) **the effective quantity of which can only be estimated by decantation and measurement**, the content of the recipients – calculated function of their volume, density, composition, etc. is checked by taking samples from these recipients, and taking into account the density, composition and other characteristics of the liquids that are found either organoleptically, or by measurements or by laboratory tests, as the case may be.

If various types of **stocks**, the **weighing and measuring** of which would need **significant expenses or would lead to the degradation of the respective goods**, can be inventoried on the basis of technical calculations (for example: wood that is being pressed, veneers, etc. in an entity in the furniture industry), then the inventory method as well as the technical data on which the calculations were based are mentioned in the inventory lists.

The stocks found with the employees on the date of the inventory (that are generally inventory-item type materials: work and protection equipment, tools, instruments, etc.) are inventoried and put on separate

lists, together with the persons responsible for their custody. Within the description of their formations and work places, the goods will be centralized and compared to the data in the technical and operating records, as well as to the accounting data.

All the stocks that are being inventoried are mentioned in the inventory list that must be drawn up on storage places, accounts and goods categories and the inventory committee has the obligation to inspect all the places where goods that are subject to inventory might be stored.

The goods belonging to other companies (in custody, to be sold on commission, to be processed, etc.) are inventoried and put on separate lists. The inventory lists used for these goods will also contain information related to the number and the date of the delivery and reception document and of the supply document, as well as other useful information. The inventory lists mentioning goods belonging to third parties are also sent to the Romanian or foreign private person of legal entity who owns the respective goods, on a case-by-case basis, within maximum 15 days from the completion of the stocktaking, and the owner of these goods has the obligation to notify the possible inadequacies within 5 days from the reception of the inventory lists. If no confirmation is received within **this** term, the recognition of the accuracy of the data written in the inventory lists is implied. In case of inadequacies, the respective company has the obligation to clarify the situation of the respective differences and to communicate its findings to the private person of legal entity who owns the respective goods, within 5 days from the reception of the notification.

For the depreciated, unusable or deteriorated stocks, still stocks or stocks that are hard to sell, orders that are being manufactured, abandoned or suspended, separate inventory lists are drafted.

The stocks **that are being dispatched** are inventoried by the supplying companies, while **the stocks purchased that are in course of being supplied** are inventoried by the purchasing company and are specified on separate inventory lists.

Before starting the stocktaking of the production **in course of being manufactured, and that of the semifinished articles internally manufactured**, it is necessary that:

- all the parts, assemblies and aggregates the processing of which has been completed should be delivered to warehouses on the basis of documents;
- all the residual products and waste should be collected from sections or workshops, and all the recording documents should be drawn up;
- all the recording documents should be drawn up and the situation of the semifinished products the usage of which is doubtful should be clarified.

In the case of **the production in course of being manufactured** both the products that have not yet passed through all the phases (stages) of the processing required by the production operating process as well as the products that although finished, have not passed the technical acceptance tests or have not been completed with all their parts and accessories will be inventoried.

Raw materials, materials, prefabricated parts, spare parts, semifinished products, etc., **that are found in the work places and are not being processed, are not** considered production in course of being manufactured. They are inventoried separately and are returned to the accounts from which they have come, while the costs are diminished, and after completing their stocktaking their accounting will be performed in the initial expense accounts.

As I have mentioned before, the inventory evaluation, on the occasion of the stocktaking, is made at the **current value** of each article, called **book value**, set function of **de the usage, condition and market price of the goods**.

When the book value of the stocks is set the **principle of prudence** will be applied, according to which all the value adjustments due to depreciation will be taken into consideration. Consequently:

- If it is found that **the book value**, set function of the goods usefulness for the company and of the market price, **is higher** than **the value with which it is recoded in the accountancy, the accounting values will be recorded** in the inventory lists;
- If the **book value** of the goods **is lower than** the accounting value, *the book value will be specified in the inventory lists.*

Stock type assets are evaluated at their accounting value, except for the found depreciations. If the **accounting value of the stocks is higher than their book value**, the value of the stocks is **diminished down to their net realizable value** by the **establishment of a depreciation adjustment**. The depreciation

adjustment is recorded irrespective of the economic situation of the company, even if the company has book losses.

For the stocks for which depreciations were found, on the basis of the separately drafted inventory lists, **the inventory committee makes proposals concerning the establishment of depreciation adjustments**, while also mentioning all the causes that led to these depreciations.

For all the overs, shorts and depreciations that have been found concerning stocks, the inventory committee must receive written justifications from the persons responsible for their management. On the basis of the received justifications and of the analysed documents, the inventory committee establishes the nature of the shortages, losses, damages and depreciations that have been found, as well as the nature of the excess, proposing, in compliance with the applicable legal provisions, the method of settlement of the differences between the book data and the real ones, resulted following the stocktaking.

- If **overs** are found in the accountancy, the respective goods will be evaluated at their **just value**.
- If **shorts** are found in the accountancy **that are imputable**, the managers will take the measure of imputing them at their replacement value.

By **replacement value** one understands the acquisition cost of goods (including the stock type ones) with characteristics and wear that similar to the one that is short at the date when the damage is found, comprising the purchase price on the market to which all the non refundable taxes, including the VAT and the transport, supply and other costs necessary in order to record the respective goods in the accountancy are added. In the case of stocks that are short and that are to be imputed and **cannot** be purchased on the market, the imputing value is set by a specialist committee.

Moreover, we must take into consideration that, when the value of the debt is assessed, in the cases I which the shorts are not considered offences, the **compensation of shorts with the possible overs** will be taken into account, provided the following conditions are fulfilled:

- that there is the risk of mistaking one sort of the same goods, due to the resemblance of the physical aspect: colour, pattern, model, sizes, packages or other elements;
- the found shorts or overs should concern the same accounting period and the same account.

Compensation is not admitted if there is proof that the shorts found are due to theft or degradation of the respective goods from fault of the persons who are responsible for managing these goods.

The lists with the sorts of product, merchandise, semifinished products, raw materials, packages and other material values that meet the compensation conditions due the risk of being mistaken are approved by the administrators and are used for internal purposes within the respective entity.

Example concerning the compensation of overs with shorts (for the accounting period 01.01.2006 – 01.01.2007, at Account “PFL Warehouse”, bookkeeper Ionescu Dan in an entity in the wood industry.

Overs	Shorts
PFL 2.8 mm thick → 7m ³ x 4 lei = 28 lei	PFL 3 mm thick → 10m ³ x 5 lei = 50 lei
PFL 4 mm thick → 5m ³ x 6 lei = 30 lei	PFL 5 mm thick → 3m ³ x 6.3 lei = 18.9 lei
TOTAL 12 m ³ 58 lei	13 m ³ 68.9 lei

The case: quantity “+” < quantity “-”
value “+” < value “-”

In order to compensate the found overs, first we must make sure that this type of stock (PFL) is included into the list with the sorts of stocks that meet the compensation conditions, internally approved within the entity by the administrator. After the verification, if the other conditions related to the risk of being mistaken, to the accounting period and the actual accounting are also met, we observe the following rules:..

- initially, we **equalize the quantities, by eliminating the overs from calculation** (consequently we must have the quantity of 12 m³, we will eliminate 1 m³ from the quantities that are found as being “-“).

The elimination of the overs from the calculation is made starting with the sorts that have the lowest unit prices, in increasing order.

Overs			Shorts	
PFL 4 mm thick	→ 5m ³ x 6 lei	= 30 lei	PFL 5 mm thick	→ 3m ³ x 6.3 lei = 18.9 lei
PFL 2.8 mm thick	→ 7m ³ x 4 lei	= 28 lei	PFL 3 mm thick	→ 10m ³ x 5 lei = 50 lei
TOTAL	12 m³	58 lei	13m³	68.,9 lei

↓

↓

I will eliminate

1 m³ from

the quantities “-“

Starting from the lowest

prices “5 lei”

Following the elimination we will have:

Overs			Shorts	
PFL 4 mm thick	→ 5m ³ x 6 lei	= 30 lei	PFL 5 mm thick	→ 3m ³ x 6.3 lei = 18.9 lei
PFL 2.8 mm thick	→ 7m ³ x 4 lei	= 28 lei	PFL 3 mm thick	→ 9m ³ x 5 lei = 45 lei
	12 m³	58 lei	12m³	63.9 lei

Consequently, I have eliminated, from the quantities found as being “-“, 1m³ x 5 lei = 5 lei

- we compare the total value of “+“ with the total value of “-“

Overs	Shorts
58 lei	63.9 lei → value > value of the shorts of the overs 63.9 lei 58 lei

- 5.9 lei that will be a minus value of 5.9 lei
- the entity must not incur damages:
- the quantity shortage, eliminated by compensation (1 m³ x 5 lei = 5 lei) will be imputed to the bookkeeper
- the minus value, found following the compensation, that is 5.9 lei, will also be imputed to a person found responsible.

Consequently, the estimated minus difference found following the and the application of all the deduction quotas representing the damage incurred to the company is retrieved from the persons found responsible in compliance with the applicable law.

Note: If there were excess quantities or values at the application of the first two rules , they were recorded.

The proposals included in the record of the inventory committee are presented within 3 days from the completion of the stocktaking operations, to the administrator of the entity. The administrator, with the approval of the finance and accounting department manager and of the legal department manager, decides, within maximum 5 days upon the reception of the record, on the solution of the proposals that are made in compliance with the law. The stocktaking results must be registered in the technical and operating records within maximum 3 days from the date of the approval of the inventory record by the administrator.

A specialized paper presents **the evaluation of stocks at inventory**, according to the **American system**. For example, when stocks are inventoried, they must be evaluated at their **lowest value between the cost and the market value**, with the exception of some cases in which they can be evaluated at a higher price.

When it is obvious that a goods value that is used within the current operations of the company has become lower than their cost (the acquisition or production cost) as a result of their becoming obsolete or deteriorated, or of changes in prices or of any other cause, the difference must be registered to the losses of the respective accounting period. In these cases, the estimation to the lowest value between the cost and the market price is used.

In the expression “the lowest value between the cost and the market price” the notion “**market price**” is **the equivalent of** that of **current replacement price**, provided the following two **conditions** are observed:

- The market value must not be higher than the net realization value (i.e. the estimated price from which the costs predicted for the completion of the product and the ones necessary for making it available to the customer are deduced);
- The market value must not be lower than the net realization value, decreased by a provision related to a normal margin.

Function of the nature and composition of stocks, the rule of the lowest value between the cost and the market price can be directly applied at the level of the item, on categories of stocks or for the entire stock.

In exceptional circumstances, the stocks pot can be **evaluated** to a **value that is higher than the acquisition or production cost**. For example, precious metals that have a fixed monetary value without a significant trade cost can be evaluated at their monetary value at the date of the inventory. Other exceptions concern the case when it is practically impossible to estimate a low approximate cost and when it is possible to immediately sell the goods to a (rated) market value and the goods are unidentifiable (fungible).

When stocks are evaluated to a higher value than the sale price, this should be mentioned in the attachment.

In **France**, at the moment of the stocktaking, **the current value** is used as evaluation basis.

The general case (with the exception of bonds) presents a current value:

Current value = Venal value

The venal value (PCG): is the price presumed to be accepted by the possible purchaser, in the condition and at the place of the goods; this value must be assessed function of the situation of the company.

The venal value, a value always difficult to assess, must take into account:

- The price “reference”: the market
- The usefulness of the goods for the company, function of its future “exploitation” (the “exploitation continuity” principle is taken into account)

In practice, its assessment is difficult, but also indispensable.

On the basis of the inventory register²⁸⁷ and of the trial balance drawn up on 31 December **the balance is drawn**, as part of the annual financial statements, the items of which correspond to the recorded data, harmonized with the real situation of the asset and liability items set for the inventory.

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3. OMFP no. 1753/22 November 2004 concerning the norms related to the organization and performance of the stocktaking of asset and liability items, published in Official Monitor no. 1174/13.12.2004 with its amendments by Order 1752/2005 for the approval of the accounting regulations in conformance with the European Directives.

²⁸⁷ The inventory register is the compulsory accounting document where the results of the asset and liability item stocktaking are recorded, on groups set function of their nature, according to the balance items. The asset items (including **stocks**) and the liability ones recorded in the day-book are based on the inventory lists, the inventory records and the analytical statements, on a case-by-case basis, justifying the content of each balance item (**including the ones specific to stocks**) .

4. Order no. 1752 from 17 November 2005 for the approval of the Accounting Rules in compliance with the European Directives, published in Official Monitor no. 1080 A/30 November 2005, amended and completed