

3. IND AS 2 - INVENTORIES

Practical Example 1:

At the end of its financial year, company P has 100 units of inventory on hand recorded at a carrying amount of ₹10 per unit. The current market price of ₹8 per unit at which these units can be sold. Company P has a firm sales contract with company Q to sell 60 units at ₹11 per unit, which can not be settled net. Estimated incremental selling cost is ₹1 per unit. Calculate Net Realisable Value of the inventory of company P.

Solution:

Calculation of Total NRV:

Sr.No.	Particulars	Amount
1	Goods to be sold to company Q (60 units X ₹ 10)	600
2	Remaining goods (40 units X ₹ 7)	280
	Total NRV	880

WN 1: Calculation of NRV per unit= Expected selling price - Estimated incremental

NRV per unit= Expected Selling Price - Estimated Incremental Selling Cost

Sr. No.	Particulars	Amount
1	Goods to be sold to company Q (11 - 1)	10
2	Remaining goods (8-1)	7

Practical Example 2:

Pluto Ltd. has a plant with the normal capacity to produce 5,00,000 unit of a product per annum and the expected fixed overhead is ₹ 15,00,000. Fixed overhead on the basis of normal capacity is ₹ 3 per unit (15,00,000/5,00,000).

Case 1:

Actual production is 5,00,000 units. Fixed overhead on the basis of normal capacity and actual overhead will lead to same figure of ₹ 15,00,000. Therefore, it is advisable to include this on normal capacity.

Case 2:

Actual production is 3,75,000 units. Fixed overhead is not going to change with the change in output and will remain constant at ₹ 15,00,000, therefore, overheads on actual basis is ₹ 4 p/u (15,00,000/3,75,000).

Hence by valuing inventory at ₹ 4 each for fixed overhead purpose, it will be overvalued and the losses of ₹ 3,75,000 will also be included in closing inventory leading to a higher gross profit than actually earned.

Therefore, it is advisable to include fixed overhead per unit on normal capacity to actual production ($3,75,000 \times 3$) ₹ 11,25,000 and balance ₹ 3,75,000 shall be transferred to Profit & Loss Account.

Case 3:

Actual production is 7,50,000 units. Fixed overhead is not going to change with the change in output and will remain constant at ₹ 15,00,000, therefore, overheads on actual basis is ₹ 2 ($15,00,000 / 7,50,000$). Hence by valuing inventory at ₹ 3 each for fixed overhead purpose, we will be adding the element of cost to inventory which actually has not been incurred. At ₹ 3 per unit, total fixed overhead comes to ₹ 22,50,000 whereas, actual fixed overhead expense is only ₹ 15,00,000. Therefore, it is advisable to include fixed overhead on actual basis ($7,50,000 \times 2$) ₹ 15,00,000.