

**International Accounting Standard 2****Inventories**

*This version includes amendments resulting from IFRSs issued up to 31 December 2008.*

IAS 2 *Inventories* was issued by the International Accounting Standards Committee in December 1993. It replaced IAS 2 *Valuation and Presentation of Inventories in the Context of the Historical Cost System* (originally issued in October 1975).

The Standing Interpretations Committee developed SIC-1 *Consistency—Different Cost Formulas for Inventories*, which was issued in December 1997.

Limited amendments to IAS 2 were made in 1999 and 2000.

In April 2001 the International Accounting Standards Board (IASB) resolved that all Standards and Interpretations issued under previous Constitutions continued to be applicable unless and until they were amended or withdrawn.

In December 2003 the IASB issued a revised IAS 2, which also replaced SIC-1.

Since then IAS 2 has been amended by the following IFRSs:

- IFRS 8 *Operating Segments* (issued November 2006)\*
- *Improvements to IFRSs* (issued May 2008).\*

The following Interpretation refers to IAS 2:

- SIC-32 *Intangible Assets—Web Site Costs* (issued March 2002 and subsequently amended).

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\* Effective date 1 January 2009

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*paragraphs*

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International Accounting Standard 2 *Inventories* (IAS 2) is set out in paragraphs 1–42 and the Appendix. All the paragraphs have equal authority but retain the IASC format of the Standard when it was adopted by the IASB. IAS 2 should be read in the context of its objective and the Basis for Conclusions, the *Preface to International Financial Reporting Standards* and the *Framework for the Preparation and Presentation of Financial Statements*. IAS 8 *Accounting Policies, Changes in Accounting Estimates and Errors* provides a basis for selecting and applying accounting policies in the absence of explicit guidance.

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## Introduction

- IN1 International Accounting Standard 2 *Inventories* (IAS 2) replaces IAS 2 *Inventories* (revised in 1993) and should be applied for annual periods beginning on or after 1 January 2005. Earlier application is encouraged. The Standard also supersedes SIC-1 *Consistency—Different Cost Formulas for Inventories*.

## Reasons for revising IAS 2

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- IN2 The International Accounting Standards Board developed this revised IAS 2 as part of its project on Improvements to International Accounting Standards. The project was undertaken in the light of queries and criticisms raised in relation to the Standards by securities regulators, professional accountants and other interested parties. The objectives of the project were to reduce or eliminate alternatives, redundancies and conflicts within the Standards, to deal with some convergence issues and to make other improvements.
- IN3 For IAS 2 the Board's main objective was a limited revision to reduce alternatives for the measurement of inventories. The Board did not reconsider the fundamental approach to accounting for inventories contained in IAS 2.

## The main changes

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- IN4 The main changes from the previous version of IAS 2 are described below.

### Objective and scope

- IN5 The objective and scope paragraphs of IAS 2 were amended by removing the words 'held under the historical cost system', to clarify that the Standard applies to all inventories that are not specifically excluded from its scope.

### Scope clarification

- IN6 The Standard clarifies that some types of inventories are outside its scope while certain other types of inventories are exempted only from the measurement requirements in the Standard.
- IN7 Paragraph 3 establishes a clear distinction between those inventories that are entirely outside the scope of the Standard (described in paragraph 2) and those inventories that are outside the scope of the measurement requirements but within the scope of the other requirements in the Standard.

## Scope exemptions

### Producers of agricultural and forest products, agricultural produce after harvest and minerals and mineral products

- IN8 The Standard does not apply to the measurement of inventories of producers of agricultural and forest products, agricultural produce after harvest, and minerals and mineral products, to the extent that they are measured at net realisable value in accordance with well-established industry practices. The previous version of IAS 2 was amended to replace the words 'mineral ores' with 'minerals and mineral products' to clarify that the scope exemption is not limited to the early stage of extraction of mineral ores.

### Inventories of commodity broker-traders

- IN9 The Standard does not apply to the measurement of inventories of commodity broker-traders to the extent that they are measured at fair value less costs to sell.

## Cost of inventories

### Costs of purchase

- IN10 IAS 2 does not permit exchange differences arising directly on the recent acquisition of inventories invoiced in a foreign currency to be included in the costs of purchase of inventories. This change from the previous version of IAS 2 resulted from the elimination of the allowed alternative treatment of capitalising certain exchange differences in IAS 21 *The Effects of Changes in Foreign Exchange Rates*. That alternative had already been largely restricted in its application by SIC-11 *Foreign Exchange—Capitalisation of Losses from Severe Currency Devaluations*. SIC-11 has been superseded as a result of the revision of IAS 21 in 2003.

### Other costs

- IN11 Paragraph 18 was inserted to clarify that when inventories are purchased with deferred settlement terms, the difference between the purchase price for normal credit terms and the amount paid is recognised as interest expense over the period of financing.

## Cost formulas

### Consistency

- IN12 The Standard incorporates the requirements of SIC-1 *Consistency—Different Cost Formulas for Inventories* that an entity use the same cost formula for all inventories having a similar nature and use to the entity. SIC-1 is superseded.

### Prohibition of LIFO as a cost formula

- IN13 The Standard does not permit the use of the last-in, first-out (LIFO) formula to measure the cost of inventories.

### **Recognition as an expense**

- IN14 The Standard eliminates the reference to the matching principle.
- IN15 The Standard describes the circumstances that would trigger a reversal of a write-down of inventories recognised in a prior period.

### **Disclosure**

#### **Inventories carried at fair value less costs to sell**

- IN16 The Standard requires disclosure of the carrying amount of inventories carried at fair value less costs to sell.

#### **Write-down of inventories**

- IN17 The Standard requires disclosure of the amount of any write-down of inventories recognised as an expense in the period and eliminates the requirement to disclose the amount of inventories carried at net realisable value.

## International Accounting Standard 2

### *Inventories*

#### Objective

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- 1 The objective of this Standard is to prescribe the accounting treatment for inventories. A primary issue in accounting for inventories is the amount of cost to be recognised as an asset and carried forward until the related revenues are recognised. This Standard provides guidance on the determination of cost and its subsequent recognition as an expense, including any write-down to net realisable value. It also provides guidance on the cost formulas that are used to assign costs to inventories.

#### Scope

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- 2 **This Standard applies to all inventories, except:**
- (a) **work in progress arising under construction contracts, including directly related service contracts (see IAS 11 *Construction Contracts*);**
  - (b) **financial instruments (see IAS 32 *Financial Instruments: Presentation* and IAS 39 *Financial Instruments: Recognition and Measurement*); and**
  - (c) **biological assets related to agricultural activity and agricultural produce at the point of harvest (see IAS 41 *Agriculture*).**
- 3 **This Standard does not apply to the measurement of inventories held by:**
- (a) **producers of agricultural and forest products, agricultural produce after harvest, and minerals and mineral products, to the extent that they are measured at net realisable value in accordance with well-established practices in those industries. When such inventories are measured at net realisable value, changes in that value are recognised in profit or loss in the period of the change.**
  - (b) **commodity broker-traders who measure their inventories at fair value less costs to sell. When such inventories are measured at fair value less costs to sell, changes in fair value less costs to sell are recognised in profit or loss in the period of the change.**
- 4 The inventories referred to in paragraph 3(a) are measured at net realisable value at certain stages of production. This occurs, for example, when agricultural crops have been harvested or minerals have been extracted and sale is assured under a forward contract or a government guarantee, or when an active market exists and there is a negligible risk of failure to sell. These inventories are excluded from only the measurement requirements of this Standard.
- 5 Broker-traders are those who buy or sell commodities for others or on their own account. The inventories referred to in paragraph 3(b) are principally acquired with the purpose of selling in the near future and generating a profit from