CAMBRIDGE

Study & Master

Support Pack | Grade 12

CAPS

Accounting

Inventories

This revision pack for **Accounting Grade 12** provides support for learners revising the most important concepts and principles covered in the CAPS curriculum. These include concepts relating to companies, the acquisition of Fixed assets, inventories, VAT, Manufacturing and cost accounts, and budgeting. Summaries of the GAAP principles, theory of Accounting, and the format of Debtors and Creditors control accounts are provided. Furthermore, a detailed table to summarise the interpretation of Financial Statements is provided.

Cambridge University Press Africa is a proudly South African publisher – we are providing this material in response to the need to support teachers and learners during the school shutdown and for the remainder of the 2020 school year.

For more information on our *Study & Master* CAPS-approved textbooks and valuable resource material, visit ***www.cambridge.org***

We are all in this together!

www.cambridge.org

Revision 6
Inventories

Inventory valuations

A business buys stock with the intent to resell that stock at a profit. So the owner should always know exactly how much stock is on hand (left over), and what the cost price is of this stock. All stock is recorded in an inventory/inventory program on a computer.

A businessapplies one of two methods to determine the cost of stock on hand:

- **First-in-first-out (FIFO) method:** The stock purchased first is sold first
- **Weighted average method:** Costs are assigned to stock on hand using averages

Inventory validations

Stock (inventory) needs to be physically counted to establish whether the values on the financial records agree with the actual stock on hand. A physical stocktaking must take place as regularly as possible.

Stock systems

This is how stock is managed and controlled in the financial records. There are two systems that can be used.

Perpetual stock system

- *Trading Stock* and *Cost of Sales* accounts are updated each time stock is bought and sold.
- The cost price of goods sold (cost of sales) can be determined when stock is sold.
- The physical stocktaking can therefore be compared to the financial records (*Trading Stock* account).
- Stock deficits can easily be determined.

Periodic stock system

- The *Purchases* account is used to record stock bought.
- The *Sales* account is used to record stock sold.
- The cost price of goods sold (cost of sales) is not available when stock is sold.
- So, no ongoing record of stock is kept in the *Trading Stock* account.
- Cost of sales is only calculated at the end of a financial year.
- It is important to perform regular stocktaking to validate stock.
- It is very difficult to determine stock deficits.

Ethics and ethical behaviour in stock control

- The business must disclose its stock valuation method in the notes to the financial statements.
- Discrepancies can arise if the valuation method is not calculated correctly. This could affect the financial results of the business.
- The stock registers must be updated regularly and proper records kept.
- Proper documentation must be available to support the information recorded in the books of the business.
- The business must ensure that the stock valuation method chosen is correctly implemented and controlled, so that opportunities for theft are minimal.
- The business cannot change to a different stock valuation method during a particular financial year. This will affect the financial reporting.

Internal control of stock

- The business must ensure that division of duties is applied when receiving, pricing, distributing and returning stock.
- Stock registers must be updated and checked by senior management.
- Regular stocktaking must be done.
- Ledger accounts must be updated when stock is bought and sold.
- Stock deficits must be identified and reasons for the losses must be investigated.
- Stock records must be internally audited regularly.
- Staff must be trained how to administer their business's particular stock valuation method.

GAAP and stock control

Two GAAP principles apply to stock:
Historical cost: Stock will remain in the books at its historical cost. This method applies especially to the FIFO method but not to the weighted average method.
Prudence: The adjustment for Trading Stock Deficit is made at the end of the financial year in order to bring the book value of stock in line with the value of stock on hand. In this way the missing stock is taken into account and the value of stock in the books is not overstated and the Net Realisable Value is determined.