

STATE OF OKLAHOMA
OFFICE OF MANAGEMENT AND ENTERPRISE SERVICES
GAAP CONVERSION MANUAL

G. INVENTORY CONVERSION PACKAGE

June 2021

I. PURPOSE AND OBJECTIVES

The ACFR presents the dollar value of inventories on hand at the close of business on June 30. There are two basic types of inventories which are addressed in this package: 1) materials and supplies, and, 2) goods for resale or distribution.

The state's accounting system records inventory items as expenditures when purchased, rather than when consumed. Therefore, the dollar value of inventories at fiscal year end must be recorded on the state's financial statements. There are several acceptable inventory valuation methods. In accordance with the accounting principles applicable to inventories, agencies must price their inventories at the lower of cost or market. See the key terms in Part III.

Agencies may complete the Inventory Summary form using either a periodic or a perpetual inventory system. Perpetual systems provide better control than do periodic systems but require more resources to maintain.

II. AGENCY ACTION REQUIRED

- A. Carefully read the key terms in Part III.
- B. The Inventory Summary form (summary) should reflect amounts as of close of business on June 30.
- C. Round all dollar amounts to the nearest whole dollar.
- D. All working papers are subject to audit by the State Auditor & Inspector (SA&I). The agency is required to keep a copy of the completed summary form and all associated working papers for three years after the completion of the SA&I audit.
- E. The person who completes and signs the summary form should keep a copy. OMES will contact this person if there are any questions.
- F. If needed, call your agency's financial reporting analyst for guidance.
- G. Return the completed summary form to your OMES financial reporting analyst by e-mail **no later than the due date shown on the form**. **If you can return it earlier, please do so.**
- H. If the summary form does not apply to your agency, check the box in the upper left portion of the summary, complete item (2) and return it to OMES.

III. KEY TERMS

- A. Inventory - Inventories are assets that have a short useful life, usually less than one year, and do not include: land, buildings, improvements, construction in progress, and machinery and equipment which are considered capital assets.

Inventory has been classified into the following two categories:

Inventory of Materials and Supplies - represents the dollar value of materials and supplies on hand at June 30 that will be used or consumed in the normal course of operations.

Inventory of Goods for Resale or Distribution - represents the dollar value of goods on hand at June 30 that are being held by the agency for resale or distribution to the public or to other agencies rather than held for consumption in the normal course of operations.

B. Inventory Systems - There are two types of inventory systems:

Periodic Inventory System - Under a periodic inventory system, an agency updates its inventory account only periodically (perhaps just once each year, at fiscal year-end). At that time, the agency would take a physical count of inventory items on hand and apply one of the acceptable valuation methods to arrive at a total value of inventory.

Perpetual Inventory System - Under a perpetual inventory system an agency updates its record of inventory quantities on hand every time it purchases or issues (sells, distributes, or consumes) an inventory item. The agency must still take a physical count of inventory items on hand at fiscal year-end and adjust its records to actual. Usually only the larger agencies with computerized inventory systems would elect to use this system.

C. Inventory Valuation Methods - Acceptable methods of valuing or "costing" inventories include:

Average Cost - Inventory items are valued at the average cost of similar items purchased during the fiscal year. This method is commonly used with computerized perpetual inventory systems.

First-In, First-Out (FIFO) - This method assumes that agencies use inventory items in the order in which they were purchased. That is, items on hand represent the most recent purchases. It is the cost of these most recent purchases that would be used to value the inventory.

Last-In, First-Out (LIFO) - This method is based on the concept that the latest acquisition cost should be matched with current operations. The units remaining in the ending inventory are valued at the oldest units' cost.

Specific Identification - This method matches the specific units of inventory on hand to their specific invoices. The actual cost shown on the invoice is used to value the inventory items.

D. Lower of Cost or Market Value - To determine which is lower, the cost or an inventory item or its current market value, complete the following steps:

1. Determine the cost of each type of inventory item based on one of the above Inventory Valuation Methods. Cost is defined as the price paid or the consideration given to acquire the inventory item. Included in the cost are all direct and indirect costs incurred during transportation.
2. Determine the "estimated" market value of each type of inventory item at June 30.
3. Determine which is lower, cost or market, for each type of inventory item. The total of these amounts is to be recorded as the agency's "Dollar Value of Inventories." Only in unusual instances would an inventory item's market value be lower than its cost (i.e., old, or obsolete items).

E. Market Value - The item's current replacement cost by either purchase or reproduction.

IV. SPECIFIC INSTRUCTIONS

A. Preparation of the Data - Prior to completing the Inventory Summary form, it is necessary to:

1. Take a physical count of inventory items on hand at the end of the fiscal year. Do this as close to June 30 as possible. The date of the physical count should not vary significantly from year to year, and should be observed by the SA&I.
2. Compute the cost of each type of inventory item counted using one of the acceptable valuation methods. The valuation method should be used consistently from year to year. Any change in valuation method should be reported to OMES.
3. Compare the cost of each inventory item to its "estimated" market value as described in the key terms in Part III. The lower of cost or market is the value to be used. Normally market value would be higher, not lower. Only in unusual instances would the market value be lower than cost.
4. After preparing the data, transfer the totals to the summary form. Complete the summary form and submit it to OMES.

B. Completing the Inventory Summary Form

Complete only one inventory summary form for your entire agency unless you are specifically requested to report some data separately.

1. Enter the agency ACFR code, name, and funds/accounts to be included on the summary.
2. Provide the name, title, phone number and date for each person who completes and approves this summary form. The finance officer or executive director should approve and sign the form before sending it to OMES. Keep a copy of the form. *When submitting the form via email it should come from the address of the approving officer.* This will act as an implicit electronic signature verifying the form has been reviewed and approved for validity, accuracy, and completeness.
3. Enter the date of your physical count and the inventory valuation method your agency uses. State whether this method is the same as last year's method and enter last year's method if different. Place a check mark in one of the spaces to indicate which inventory system your agency uses.
4. Enter the total dollar value at the lower of cost or market for each category of inventory. Then total the two categories.
5. Provide comments or explanations as needed for any unusual items or circumstances.

C. Working Papers

The agency should keep all worksheets and any documents that support data on the summary form. For example:

- * Completed physical count schedules.
- * Cost vs. market value data.