Key Terms

Inventories
Inventories are assets:held for sale in the ordinary course of business.

Cost of Inventory
According to the AS-2, the cost of inventories should comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Costs of Conversion
The costs of conversion of inventories include costs directly related to the units of production, such as direct labour. They also include a systematic allocation of fixed and variable production overheads that are incurred in converting materials into finished goods.

Net Realisable Value
According to AS-2, net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Cost of goods sold
COGS is the cost of the goods sold during the period and it is calculated as *COGS = Opening Stock + Purchase or Production – Closing Stock*

Fist-in, first-out (FIFO)
FIFO is one of the methods of inventory valuation mentioned in the AS-2. It is based on the assumption that the goods bought first are sold first. COGS consists of goods bought first. The closing stock or the unsold stock will be from the latest purchase.

Last-in, first-out (LIFO)
LIFO is based on the assumption that the most recently bought goods are sold first. COGS consists of goods purchased last. So under this method the closing stock will consist of goods from the earlier purchases.

Debtor
The person to whom the goods are sold on credit is called a debtor. A group of debtors is generally shown as sundry debtors in the financial statements

Bad Debts
Bad debt is the loss due to the insolvency of the debtors. Bad Debt is shown in the income statement during the year in which the debtors become insolvent.

Provisions for Bad Debts
Some times companies keep aside a profit as provision to meet future bad debts. Such provisions are called *Provisions for Bad and Doubtful Debts*. Such a practice is also backed by the conservative principle of accounting.