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The Accounting for Inventory from a Commercial Point of View

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Abstract

Inventory control is a very important managerial function because the physical inventory of many companies involves the largest investment in current assets. The main purpose of inventory accounting is to determine periodic profit and loss through the process of bringing together the cost of goods sold with the sales proceeds in one accounting period and determining the amount of inventory to be presented in the balance sheet. This paper aims to describe the accounting for inventory from a commercial point of view. The method used in this study is qualitative in nature with a descriptive approach. The results showed that the main functions of inventory are to avoid delays in goods, loss of goods and with the presence of inventory, the company's operations can continue to run so that services to consumers can be carried out as well as possible. More specifically, the main functions of inventory are the decoupling function, economic lot-sizing function, and anticipation function. As the inventories become subject to regulations in Indonesia, the study also highlights the purposes of calculating the income tax of inventories. Article 10 paragraph (6) of the Income Tax Law states that inventories must be valued at cost. Therefore, if the taxpayer makes an assessment based on a method other than cost, an adjustment is required.

Keywords

Accounting, Inventory, Organizational Efficiency, Tax Law

1. Introduction

Inventory is anything or organizational resources that are stored in anticipation of meeting the demand for a set of physical products at various stages of the transformation process from raw materials to work in process, and then finished goods. Inventory is one of the most expensive assets in many companies, representing as much as 40% of the total invested capital. Assets available for sale in the normal course of business, both merchandise for trading businesses and finished goods for manufacturing; are in production (work in process and work in progress for contractors); and in the form of raw materials or equipment (auxiliary materials) for use in the production process or providing services (Kieso et al., 2019). The main purpose of inventory accounting is to determine periodic profit and loss through the process of bringing together the cost of goods sold with the sales proceeds in one accounting period and determining the amount of inventory to be presented in the balance sheet. As one of the non-monetary assets, the problem that arises is how to report the ending inventory value on the balance sheet (Yamazaki et al., 2016).

Inventory control is a very important managerial function because the physical inventory of many companies involves the largest investment in current assets. If a company invests too much of its funds in inventory, it causes excessive holding costs and may have a higher opportunity cost (Marand et al., 2019). Likewise, if the company does not have sufficient inventory, it can result in costs for material shortages. Operations managers around the world have long recognized that good inventory management is essential. On the one hand, a company can reduce costs by lowering the level of inventory on hand. On the other hand, consumers will feel dissatisfied when a product is out of stock. Therefore, companies must strike a balance between inventory investment and customer service levels (Axsäter, 2015). The purpose of this paper is to understand inventory accounting from a commercial point of view.

2. Inventory and Its Functions

Inventories can be grouped according to the type and position of the item in the product work order according (Hynes & Naba, 2012), namely raw material stock, product parts inventory (purchased parts), supplies of auxiliary materials (supplies stock), Inventory of Semi-Finished Goods (Work in Process) and Finished Goods Inventory.

The first is raw material stock. Inventory of goods needed for the production process. These goods can be obtained from natural sources, or purchased from suppliers who produce these goods (Handani, 2021). The second is product parts inventory (purchased parts). It represents inventory of goods consisting of parts received from other companies, which are directly assembled with other parts without going through the production process. The third is supplies of auxiliary materials (supplies stock). It represents inventory of goods needed in the production process to help smooth production, but are not part of finished goods. The fourth is inventory of semi-finished goods (work in process). They are goods that are not yet in the form of finished goods, but are still further processed so that they become finished goods. The fifth is finished goods inventory. It refers to goods that have been processed or processed in factories and are ready to be distributed to distributors, retailers, or directly sold to customers.

By types, according to Toplak et al. (2008), inventories include purchase fee, conversion fee and additional costs. Purchase fee covers the purchase price, import duties, and other taxes except those that are refundable to the tax office, while conversion fee includes costs directly related to units produced and fixed and variable manufacturing overhead costs that are allocated on a systematic basis. Lastly, additional costs incurred until the inventory is in a condition and place that is ready for sale or use (present location and condition).

3. Results

3.1 Inventory Determination and Reporting in Financial Statements

For the purposes of calculating income tax, Article 10 paragraph (6) of the Income Tax Law (Law No. 36 of 2008) states that inventories must be valued at cost. Therefore, if the taxpayer makes an assessment based on a method other than cost, an adjustment is required. Determining the amount of inventory value or usage value is very important because it affects the cost of production.

The reports in the financial statements regulated in Taxation are Article 10 paragraph (6) of the Value-Added Law stating that inventories and the use of inventories for calculating the cost of goods are valued based on the average acquisition price or by prioritizing the inventories obtained first. The explanation of the paragraph stated that in general there are three classes of goods inventory, namely finished goods or merchandise, goods in the production process, raw materials and auxiliary materials. The provisions in this paragraph stipulate that the valuation of inventories may only use cost. The valuation of inventory usage for calculating the cost of goods may only be carried out by means of an average or by prioritizing the inventory obtained first.

For example, in December 2007 PT A had purchased goods with an agreement at a price of IDR 300,000,000. The goods were received in March 2018 and in December 2017 the price fell to IDR 100,000,000. according to commercial accounting practice a loss of IDR 100, 000,000 is charged as a loss in 2017 with the journal entry: Ending inventory at cost of cost Ending inventory by retail Goods available for sale at cost Goods available for sale Loss on Changes in Price IDR 200,000,000, Inventory IDR 200,000,000 Accounting practices the tax does not recognize a loss of IDR 200,000,000 because the tax looks at the real facts and does not accept the anticipated loss. The tax will recognize as a loss if the goods sold are actually experiencing a loss.

3.2 Inventory Management and Organizational Efficiency

The function of inventory is to avoid delays in goods, loss of goods and with the presence of inventory, the company's operations can continue to run so that services to consumers can be carried out as well as possible. According to Lawi et al. (2017) the main functions of inventory are decoupling function, economic lot sizing function, and anticipation function.

The operational efficiency of an organization can be increased due to various important inventory functions. First, it must be remembered that inventory is a collection of physical products at various stages of the transformation process from raw materials to work in process, and then finished goods. The functions of the inventory include some ways (Wahyuni & Ginting, 2017).

The fist is decoupling function. It is an important function of inventory is to allow the company's internal and external operations to have freedom (Fakhimuddin, 2018). This supply of decouples allows companies to fulfill their subscriptions without being interrupted by suppliers. Inventory of raw materials is held so that the company will not be completely dependent on its procurement in terms of quantity and delivery time. Work-in-process inventory is maintained to keep individual departments and processes of the company free. Inventories of finished goods are needed to meet uncertain product demand from customers. Inventories held to deal with unpredictable or predictable fluctuations in consumer demand are called fluctuation stocks (Jeong, 2011).

The second is economic lot sizing function. Through inventory holding, companies can produce and purchase resources in quantities that can reduce unit costs. This Lot Size inventory needs to consider savings in terms of purchasing, transportation costs per unit are cheaper because the company makes purchases in larger quantities, compared to the costs incurred due to the large inventory (building rental costs, investment, risk, and so on) (Wahyuni & Praninta, 2021).

The third is anticipation function. Often companies face demand fluctuations that can be estimated and forecasted based on experience or past data, namely seasonal demand. In this case, the company can hold seasonal inventory. In addition, companies also often face uncertainties in the delivery period and demand for goods during the return request period, thus requiring an extra quantity of inventory which is often called safety stock. In fact, the safety stock is complementary to the “decoupling” function described above. This anticipation stock is important so that the smooth production process is not disrupted (Pasha et al., 2021).

In addition to the above functions, according to Herjanto (1997) there are six important functions contained by inventory in meeting company needs, including eliminating the risk of delays in the delivery of raw materials or goods needed by the company, eliminating the risk if the material ordered is not good so it must be returned, eliminating the risk of rising prices of goods or inflation, to store raw materials that are produced seasonally so that the company will not be difficult if these materials are not available in the market, obtaining benefit from purchases based on quantity discounts and providing services to customers with the availability of the necessary goods.

4. Conclusion

Inventory control is a very important managerial function because the physical inventory of many companies involves the largest investment in current assets. The main purpose of inventory accounting is to determine periodic profit and loss through the process of bringing together the cost of goods sold with the sales proceeds in one accounting period and determining the amount of inventory to be presented in the balance sheet.

By using descriptive analysis, the results of this study demonstrate that one of the main functions of inventory is to avoid delays in goods, loss of goods and with the presence of inventory, the company's operations can continue to run so that services to consumers can be carried out as well as possible. More specifically, the main functions of inventory are decoupling function, economic lot sizing function, and anticipation function. Moreover, as the inventories become subject of regulations in Indonesia, the study also highlights the purposes of calculating income tax of inventories. Article 10 paragraph (6) of the Income Tax Law states that inventories must be valued at cost. Therefore, if the taxpayer makes an assessment based on a method other than cost, an adjustment is required

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