

Policy 4210
Valuation of Inventory

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Policy Sections	2
4210.1 Definition and Purpose of Inventory	2
4210.2 Items to be Included in Inventory	2
4210.3 Valuation	2
4210.4 Recording of Inventory	3
4210.5 Proper Safeguarding	3
4210.6 Management of Inventory Levels	3
4210.7 Inventory Verification	3
4210.8 Purchasing	4
4210.9 Unusable Inventory	4

Scope

This policy provides accounting guidance for: determining items that should be inventoried; valuing of inventory; recording the inventory in our accounting system; and managing the inventory.

Policy Statement

The inventory of the University, as defined in this policy, should be valued in a consistent manner and accurately reflected in the University's financial statements, in accordance with Financial Accounting Standards Board (FASB) guidelines and Generally Accepted Accounting Principles (GAAP). Inventory is a valuable University asset and should be properly safeguarded. Consistent compliance with the provisions of this policy reduces cost and ensures that supplies are available when needed.

Reason for the Policy

The purpose of this policy is to:

- promote consistency and accuracy in the valuation and recording of the University's inventory
- promote compliance with specific FASB guidelines and conformity with GAAP
- ensure that the University's inventory is properly safeguarded.

Definitions

Cycle counting

An inventory verification method that counts the more valuable items more frequently than the less valuable items. Typically the more valuable items are counted more than once a year and the less valuable items are counted over the course of two years. In certain circumstances use of this method increases accuracy and reduces administrative effort.

First-in First-Out (FIFO) method

This is a method of costing the inventory where you determine the final quantity on hand, then look at the most recent vendor invoices until you sum up to the quantity on hand. The method is based on the assumption that the first goods purchased are the first to be sold, and that the goods which remain are the last purchased.

Policy Sections

4210.1 Definition and Purpose of Inventory

Inventory consists of items purchased for resale to external customers or other departments or for subsequent use by a department, as further specified in Section 4210.2.

University departments and units maintain inventories for one or both of the following purposes:

- to provide items in a more timely manner than individual purchases from an outside vendor
- to provide items at a lower cost by purchasing larger quantities at one time.

4210.2 Items to be included in Inventory

The following items should be included in inventory. The alternative is to expense at the time of purchase.

- A. Items purchased with the intent of resale to other departments or external customers. Examples of such purchases are:
- supplies purchased by a stockroom for subsequent purchase by other departments
 - food and other consumables to be used in University dining halls
 - items to be sold in University museum stores.
- B. Items purchased in quantity for subsequent use by service departments such as Facilities (e.g., plumbing parts), if:
- the total value of the items in stock is greater than \$50,000, or
 - the use of the supplies (i.e., the specific account to which items should be charged) cannot be determined at the time of purchase, e.g., Telecommunications supplies that will be consumed in a variety of projects throughout the University.

Departments should not include any other items in inventory without prior approval from the Controller's Office. The Policy does not pertain to Movable Equipment Inventory (MEI) which is classified as Property, Plant and Equipment.

4210.3 Valuation

The University uses the first-in first-out (FIFO) method for valuation of inventory. In cases where the quantity on hand includes purchases at different prices, different prices should be used for valuation. Example of FIFO method for one of the items in the Stockroom:

- On August 1st, we received 250 packages of item ABC at \$60.00 per package.
- During August, 15 packages at \$60.00 per package are sold. Also during August 150 packages are received at \$65.00/package.
- The August 31 inventory is 385 items.
- The August 31 valuation of inventory is 150 items @ \$65.00 = \$9,750 plus 235 items @ \$60.00 = \$14,100 for a total of \$23,850. Therefore the 385 items in stock on August 31 are valued at a unit price of \$61.95 (\$23,850/385).

To simplify the valuation process, lower dollar items may be valued at the most recent price if this does not result in a significant difference, (greater than 3%) from the calculated FIFO.

Department overhead should not be added to the inventory cost. If freight costs or vendor discounts are material, these should be included in the inventory cost. Departments should maintain adequate records to substantiate the inventory cost with the appropriate vendor invoice, in case of audit. See Policy [1105](#) Retention of University Financial Records and [record retention schedules](#).

4210.4 Recording of Inventory

Inventory should be recorded in Expenditure Types beginning with **103**. Refer to the [Chart of Accounts Handbook](#) for current object codes.

A separate project and organization combination shall be maintained for each inventory location. The Controller's Office may waive this requirement if the inventory subsystem allows for proper segregation of locations.

See the Standard Inventory Transactions guide for examples of typical inventory entries.

4210.5 Proper Safeguarding

Inventory is a valuable asset of the University. Inventory should only be used for University purposes. Departments should ensure that their storage and management procedures provide appropriate security for inventory, to guard against theft as well as damage.

4210.6 Management of Inventory Levels

The benefits of inventory are often maximized by carrying larger quantities. However, large inventory levels can also result in greater costs to the University in the following ways:

- Inventory may become obsolete or exceed usable shelf life (e.g., items such as computer supplies, pharmacy drugs, lab chemicals)
- Funds used to purchase inventory are not available for other purposes
- Inventory is subject to theft or damage
- Storage and maintenance of goods incurs costs.

Business managers should consider these factors and maintain inventory at levels that maximize the net benefit to the University.

To this end, it is recommended that departments identify slower moving items in their inventory and consider reducing the supply of these items by such methods as:

- returns to the original vendor
- discounted pricing to promote removal from inventory
- smaller purchase quantities in the future.

Some slower moving items may be acceptable if they are critical spare parts or other important items.

4210.7 Inventory Verification

Annual Counting:

A complete physical inventory count should be conducted at least once a year to verify quantities and inventory value. This should be done either at the end of the third quarter or during the fourth quarter, in order to ensure a more accurate valuation at fiscal year end. Exceptions to this schedule may be permitted by the Controller's Office if the department has a practical business purpose for alternative timing.

Inventory balances less than \$10,000 are considered immaterial and departments/schools should seriously consider expensing such amounts and not maintain an inventory.

Quantity Adjustments:

Any net gain or loss resulting from the physical inventory count should be clearly recorded in the General Ledger. In the journal entry description, the department should indicate whether the gain or loss is due to a physical count difference, obsolescence, or damage. Expenditure type 821800 Inventory Adjustment/Loss shall be used to record these transactions.

Inventory adjustments that equal or exceed 5 percent or \$10,000, whichever is greater, are considered significant and must be reported to the University Auditing Department. Departments must investigate the reasons for significant inventory adjustments and take prompt corrective action.

Cycle Counting:

If the annual inventory count does not result in any significant adjustments as defined above, departments may choose to use cycle counting. With this method, the most valuable and important items are counted more frequently, and those of least value and importance are counted less frequently.

Departments that wish to use the cycle counting method must draw up a written procedure and submit it to the Controller's Office for approval. Departments may consult the Controller's Office for assistance in developing a cycle counting procedure.

Advantages of cycle counting include:

- avoids an annual shutdown of operations
- dividing inventory count into smaller segments makes it possible to assign and train specific employees for this function, leading to improved accuracy and accountability
- provides a more frequent count of critical items
- takes advantage of counts already conducted during the year.

4210.8 Purchasing

All purchases for stockrooms supplying laboratories and research facilities shall be made through the University Purchasing Department. This includes purchases made using the Purchasing Card.

4210.9 Unusable Inventory

Inventory items may become damaged or obsolete during storage. These items should be written off via a journal entry. The journal entry description should clearly indicate the reason for the write-off. All disposals, especially of chemicals, must comply with University safety procedures.

If the disposal generates any proceeds (e.g., sale of scrap material), these proceeds should offset the original inventory loss. The journal entry description should clearly describe the sale.

Write-Offs and discounted sales of inventory must be approved by the department Business Manager.

Related Information

[Standard Inventory Transactions guide](#)

[Chart of Accounts Handbook](#)

Policy [1105](#) Retention of University Financial Records

University [Record Retention Schedules](#)

Contacts

Subject	Contact	Phone
Interpretation of policy	Associate Controller for Financial Reporting	432-5527

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