



Research Article

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The Enactment and Critique of International Accounting Standard Two

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Abstract

Harmonising the International Accounting Standards/International Financial Reporting Standards (IAS/IFRS) globally has been the objective of national boards that seek to eliminate existing differences. The harmonisation project has been substantially efficient in realising the IFRS in emerging economies. However, concerning the international accounting standard two, the existence of different inventory valuation methods in literature is one of the dilemmas confronting the application of IAS 2 in many nations globally. This study through a comprehensive literature review discusses and present a critique on the international accounting standard two to afford insight that will be beneficial to both scholar and standard setters. The findings reveal a formidable contribution of the current asset inventory on companies and compliance levels in South Africa. Furthermore, these findings supplement prevailing body knowledge on IAS two and the value relevance of accounting inventories. Highlighting key critiques on the IAS 2 prescriptions and application internationally and also revealing the standards own crucial flaws and strengths and on companies.

Keywords: Asset, Inventory, IAS2, Financial Reporting, Compliance

1. Introduction

International financial reporting standards (IFRS) has been well-thought-out for decades to be the most significant regulatory change affecting financial reporting globally (Doukakis, 2014; Epizitone, 2021). This change is mainly attributed to the adoption of the IFRS regardless of the concept and underlying challenges. In many developing nations, the adoption of IFRS has been marred with many glitches resulting from differences in the interpretations and application of the international accounting standards (IAS). Daraghma, (2018), alluded to the need to further probe into the understanding of these standards especially in developing countries with emerging economies. The call for more studies on the IFRS has been herald in literature with authors positing the

implementation of the IFRS to be a challenging undertaken globally allude in literature (Daraghma, 2018). Extant literature reveals the diverse effect on aspects such as the end worth of inventory and cost of goods sold as a result of inconsistency of inventory valuation techniques (Chen and Zheng, 2012; Needles and Powers, 2012; Daraghma, 2018).

Prior literature reveals the IAS 2 shortcomings attributed to inept accountants, capital markets' ineptitude, and the United States generally accepted accounting principles (U.S GAAP) solicitation over the IAS (Daraghma, 2018). According to Daraghma, (2018), there is a misuse of the application due to accountants' unfamiliarity with the IFRS. Also, the inadequate understanding in the application of IAS especially standard two and IFRS has also been alluded in literature (Obaidat and Al-Hajaia, 2013). Furthermore, the gap of application is asserted to mislead financial statements readers (Daraghma, 2018) defeating the International Accounting Standard Board (IASB) objective to "develop in the public interest, a single set of high quality, understandable, enforceable and globally accepted financial standards that are based on clearly articulated principles which accord transparency, comparability and quality information in other to aided stakeholders. Previous studies also echo the same sentiments on the poor application of IAS 2 prescription (Al-Daoor, 2008; Obaidat and Al-Hajaia, 2013; Asiri, 2014; Kral, 2014; Onyekwelu, 2014; Daraghma, 2018).

Given the practical application challenges and inconsistency of inventory valuation techniques highlighted in literature, this study seeks to explore the IAS and IFRS in relation to inventories (IAS2). Hence, filling the existing gap and contributing to the body of knowledge surrounding the IAS 2 application. The overarching objectives for this study are as follows: "to examine the effects IAS 2 prescription and prescription rollout and evaluate if IAS 2 prescription influence the financial reporting of entities". This paper is presented in the following sequence based on the aforesaid introduction which references extant literature. The next section provides the study method and the literature review. Findings and discussion are thereafter presented, whilst the paper is concluded by summarizing the study results.

2. Methodology

This paper probes in the IAS 2 standards, focusing solely on the discussed inventories reported in organisations. The use of secondary data from existing literature is utilised in this paper and financial information of South African base company for contextualisation. The authors adopt an interpretivism-oriented approach that gear towards constructivism and interpretivism. This paradigm is based on the belief and meaning that the simple phenomenon is appropriate for every research issue as the real essence of reality is constructed or interpreted through perception (Epizitone and Olugbara, 2020). Exploring the standards in relation to inventories (IAS 2) this study is attained through different phases. A systematic content review of existing prescriptions and examination of the body of knowledge on inventories are conducted to achieve the research question and objectives in a cross-sectional study model. Furthermore, this paper uses the keywords, **IAS 2**, **Inventories**, **IAS 2 critiques**, **IFRS** on online databases and compressively analyse the journals, books and scholastic articles. Hence the IAS 2 standard is analysed from an academic, practitioners and standards setter point of view to attain this paper objective.

3. Literature Review

In many companies' reporting there must be disclosures of the different types of inventories and assisting in the financial statement reports is the IAS 2 prescription which affords the right way to recognise, measure and disclose inventories. This section discusses the theoretical background and overview of IAS 2, provides a theoretical review of the standards, highlights the empirical literature review on the value relevance of IAS 2 scope, recognition, measurement, disclosure and indicate the key critique and propositions for the study.

3.1 Theoretical Background

The IAS 2 prescription details the requirement for inventories accountability. This standard necessitates the deployment of the lower of cost (LC), net realisable value (NRV) and an approved means of cost determination to be layout with specific identification inclusion, first-in-first-out (FIFO) and weighted average cost (iasplus, 2020). Literature reports the revision of the IAS 2 in December 2003, which considers the annual periods that begin on or after the 1 of January 2005 (IASplus, 2020). The emergence and the history of the IAS 2 can be seen in the summarised figure 1. The overview of all the development is indicated above in the figure with the accompanying comments below the timeline.

IAS 2 development history timeline

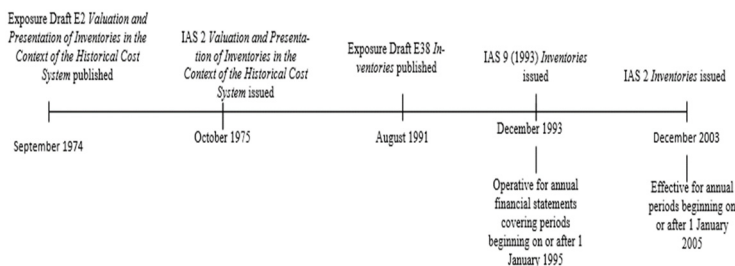


Figure 1: IAS 2 Development History Timeline

The IASplus, revealed IAS 2's objective to be the prescribed treatment of inventories that serves as a guide in the determination of the cost of inventories which is inclusive of any write-down to NRV for succeeding recognition in the expense, and the cost formulas used to assign costs to inventories. Section 2.6 of the IAS 2 provides the scope of inventories to be accounted for. Whilst the scope afforded may directly imply the inclusion of a vast category of inventories to be recognised and accounted for. The prior section of IAS 2.2 explicitly excludes certain inventories within this scope. These include certain assets such as construction contracts, financial instruments, biological assets related to agriculture and agricultural produce at the point of harvest that may be categorised as inventories to be reported separately (IAS11, IAS39 and IAS 41). Other exclusion also includes but is not limited to certain inventories such as minerals and forest products that are measure at net realizable value in relation to established practices in the industries and also, inventories of dealers and brokers measured at fair value minus the cost. Subsequently, any changes that occurred in these measures are recognised in the profit and loss section when they occurred.

Notwithstanding the fundamental principle of the IAS 2 as stated in IAS 2.9 obligate inventory within the scope to be specified at the LC and NRV. The measurement of the cost of inventories is stated in the IAS 2.10 and those costs that are not included are found in the IAS 2.16 and IAS 2.18 as shown in the table below (Table 1). The IAS 2 accommodate two different methods namely: the standard cost (*predetermined standards are used to determine the cost*) and retail method (*cost is deducted from the selling price using the gross profits*) for cost measurement for results that approximate to the actual cost (IAS 2.21-22). For non-interchangeable items of inventories, specific costs are to be attributed individually (IAS 2.23). Whereas for interchangeable items, according to IAS 2 permits the FIFO (First-In-First-Out) or weighted average cost formulas to be used (IAS 2.25). The last-in-first-out (LIFO) formula, prior allowed under the 2003 IAS 2 review was barred. IAS 2.25 further states that "identical cost formula should be employed for inventories with comparable physiognomies pertaining to their nature and function in an entity, and a different cost formula that

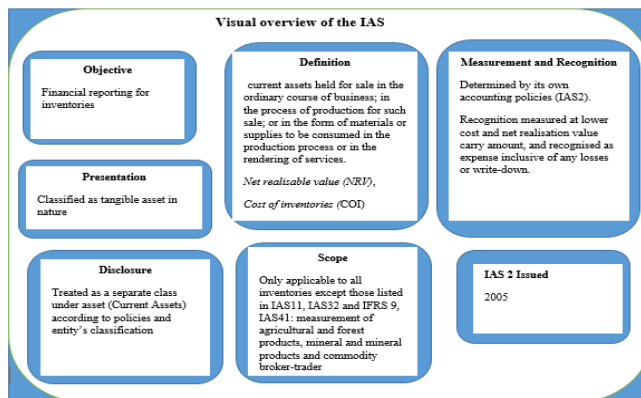
may be justified for groups of inventories that have different characteristics”.

Table 1: Measurement of Inventories

Measurement of Inventories Cost	
Included IAS 2.10	Excluded IAS 2.16 and 2.18
<ul style="list-style-type: none"> • Costs of purchase. • Costs of conversion. • Costs acquired in conveying inventories to their extant premise and condition. • Certain liability costs (interest) [IAS 2.17 and IAS 23.4] IAS 23. 	<ul style="list-style-type: none"> • Irregular waste. • Storing costs. • Administrative outlays disparate to production. • Selling costs. • Foreign exchange differences recent acquisition invoiced in foreign currency. • Interest cost from purchase with tardy settlement conditions.

According to IAS 2.6 inventory write-down should be at NRV. This should be recognised as an expense in the income statement in the period in which they occurred along with any reversal (IAS 2.34). And disclosed as covered in IAS 2.36. Additionally, IAS 2 acknowledges certain organization categorization of elements pertaining to inventories in the income statement. Accordingly, for an instance of cost of goods sold expense, the operating costs disclosure is permitted and documented in the period by cost attribute and the net change in inventories amount (IAS 2.39). Hence maintaining the consistency of the Presentation of Financial Statements, which allows presentation of expenses by function or nature (IAS 1). Figure 2 show an overview of the IAS 2 issued in 2005.

Table 2: Overview of IAS 2



The IAS 2 standard dating back to the seventies has developed and incorporated many standards to deal with inventories treatment. The changes and evolution from the first time of its conception and draft have been to deal with issues that make the standard best applicable. With the incorporation of the IFRIC 20 that deal with the stripping costs in the production phase of a surface mine and SIC-1 that deals with the consistency of different cost formulas for inventories. IAS 2 revision in 2003 incorporated and superseded SIC-1 and was later issued in 2005. Regardless of the evidence of the issues confronting the IAS 2 treatment already manifested and highlighted in the history of the IAS 2 that tackle diverse challenges in the timeline. The IAS 2 promulgation in September 1974 and revision on 18 December 2003, highlighted the existence of challenges with the inventory's treatment despite

the IAS objectives to provide a prescription on the treatment of inventories in accounting and guide in the determination of the cost of inventories. Overall, the IAS 2 standards promote harmonisation that standardises the treatment of inventories across entities and globally. However, from its adoption and application, there are favourable and unfavourable accounts after a closer look at the theoretical view in relation to the IAS 2 and GAAP implementation.

4. Discussion

4.1 Contextual Discussion

The application of IAS 2 has been globally and afforded many benefits to companies. However, there are equal challenges encounter as well with the adoption (Daraghma, 2018). There have been several reasons for these such as the lack of training and major inconsistency (Asiri, 2014; Daraghma, 2018). One of such dilemmas confronting the IAS 2 application globally is the employment of diverse inventory valuation methods (Al-Daoor, 2008; Shusheng, 2014; Monea, 2011; Siyanbola, 2012; Obaidat and Al-Hajaia, 2013; Asiri, 2014; Kral, 2014; Onyekwelu, 2014; Daraghma, 2018). Extant studies reveal the various methods afforded by the IAS 2 for the valuation of inventories (Al-Daoor, 2008; Shusheng, 2014; Monea, 2011; Siyanbola, 2012; Obaidat and Al-Hajaia, 2013; Asiri, 2014; Kral, 2014; Onyekwelu, 2014; Daraghma, 2018). In literature the IAS 2 demand that either the LC or NRV be used for the measurement of inventories (Asiri, 2014; Kral, 2014; Onyekwelu, 2014; Daraghma, 2018; iasplus, 2020). Using these methods necessitates the fair market value and the cost of inventory to be computed. However, while the IAS 2 afford different measurement of cost of inventory. The determination of the cost of purchase is required to employ one of the historical costs-based approaches which are: the first-in-first-out and weighted average (Daraghma, 2018). Additional, concerning the cost determination literature, posit the NRV to be equal to the designated market value (Shusheng, 2014; Monea, 2011; Siyanbola, 2012; Obaidat and Al-Hajaia, 2013; Honkova, 2015; Mia and Qamruzzaman, 2016; Daraghma, 2018). Furthermore, highlighting the exclusion of certain costs associated with inventory in the cost determination (IASplus 2020). However, the capitalization of interest is accommodated in the determination of inventory cost (Doupnik, and Perera, 2015). While the different methods can be flexible in diverse settings it also highlights the presence of inconsistency that arises as a result of these methods.

The mandatory requirement to report the inventory in the financial position statement according to the LC and the NRV by the IAS 2 is an issue highlighted in studies (Doupnik, and Perera, 2015; Honkova, 2015; Mia and Qamruzzaman, 2016; Daraghma, 2018). Some authors highlighted the flaws that exist within the execution of these measurements when reported on the balance sheet (Foley and Comm, 2015; Daraghma, 2018). These authors posit a false representation resulting from the comparisons of these methods when incorrectly applied (Foley and Comm, 2015; Daraghma, 2018). A clear indication of this is highlighted in the practical illustration given below that shows a company measuring its inventory incorrectly and correctly. Using the NRV of R 3165 after comparison with the cost of R 3590 is an incorrect application. Conversely, employing the use of the LC of R 3095 as indicated at the bottom of the table over the cost and NRV is the right application according to IFRS.

INCORRECT WAY OF APPLYING THE LC OR NRV

Inventory Item	Cost	NRV
1	R540.00	R450.00
2	R500.00	R495.00
3	R550.00	R620.00
4	R2,000.00	R1,600.00
Total	R3,590.00	R3,165.00

CORRECT WAY OF APPLYING THE LC OR NRV

Inventory Item	Cost	NRV	LC or NRV
1	R540.00	R450.00	R450.00
2	R500.00	R495.00	R495.00
3	R550.00	R620.00	R550.00
4	R2,000.00	R1,600.00	R1,600.00
Total	R3,590.00	R3,165.00	R3,095.00

Similarly, the treatment of inventory under US' GAAP over IFRS also highlighted several discrepancies such as related to inventory valuation cost, inventory fair market value, inventory value, conservative and loss reversal (Daraghma, 2018).

Many authors pointed out the contention on inventories written down (Monea, 2011; Siyanbola, 2012; Doupnik, and Perera, 2015; Honkova, 2015; Kral, 2014; Daraghma, 2018). According to the IAS 2, when the NRV is lower than the cost of inventories resulting from the inventories being damage, obsolete, market demand changes and physical deterioration, written down should be allowed in the accounting period it was evaluated (Siyanbola, 2012; Kral, 2014; Honkova, 2015; IAS 2). However, regardless of the inventories being unsold the written-down amount has to be reversed when there is an increase in the NRV in the period they occurred and must be restricted to the original written-down values (Monea, 2011; Foley and Comm, 2015; IAS 2; Daraghma, 2018). Also, necessitating the written-down losses which were expenses recognised in the period of the write-down in the income statement to be reverse (IAS 2). Conversely, the US GAAP forbid any reversal but rather recognised the write-down value as cost for subsequent accounting purposes regardless of the inventory being sold or written off (Daraghma, 2018). From the aforementioned company illustration, the journal entry with respect to this contrary stand of GAAP for the first item will be as follows.

Inventory Item	Cost	NRV	
Date	Journal Entry	DR	CR
1	R540.00	R450.00	
28 th February 2020	Loss on Write-Down of Inventory Inventory	90	90

Furthermore, the existence of differences in the valuation is evidence in literature with studies asserting the different methods to measure inventory under GAAP (Needles and Powers, 2012; Gray and Ehoff, 2014; PWC, 2015; Kieso, 2016). According to Kieso (2016), inventory cost purchase value can be determined using the historical cost-based approach such as first-in-first-out, Last-in-First-out and weighted average. However, the US GAAP considers three possibilities that use the designated market value that falls within the range of replacement cost, NRV on the ceiling, and NRV excluding the normal profit margin on the floor or lower limit (Sepe, and Nelson, 2012; PWC, 2015; Kieso, 2016; Daraghma, 2018). Also, the decision to eliminate the LIFO method has been justified in extant literature (Emmanuel and Abdullahi, 2015; Daraghma, 2018). Many literatures applaud the International Accounting Standards Board (IASB) for the riddance of LIFO which was posited to have resulted in companies decrease in reported earnings. On the contrary, the FIFO is herald literature to afford essential information over the LIFO (Daraghma, 2018).

IAS 2 espousal and bearing on the firms' performance has been evident in literature. The commitment to IAS 2 has been highlighted in extant literature (Daraghma, 2018). The adoption of the IAS 2 is asserted to have positive impacts on the overall company performance and adoption accuracy. Many studies allude the enhancement of the accounting numbers' value relevance and organisations' performance. Table 2 summarised these benefits derive from the adoption of IAS 2 in countries that employed the prescription and implemented the application.

Table 2: Benefits of IAS 2 adoption and applications

Benefits of IAS 2 adoption and applied	Authors	Country
“Value relevance of accounting numbers and the performance”	Barth, Landsman and Lang, 2006	Diverse countries
“Relevance of accounting numbers”	Athanasios, Kanellos and Konstantinos, 2007	Greek
“Positive impact on quality of financial statements”	Mutai, 2014	Greek
“Positive influence on the quality of accounting information.”	Siyanbola, 2012	Nigeria
“FIFO method gives an additional realistic cost of closing stock”	Emmanuel and Abdullahi, 2015	Nigeria

Additionally, extant literature reveals the increase of commitments levels of emerging economics to the application of IAS 2 prescription. Correct application of the IAS 2 in many emerging counties has upsurge (Obaidat and Al-Hajaia, 2013; Kral, 2014; Shusheng, 2014; Honkova, 2015; Nisha, 2015; Mia and Qamruzzaman, 2016). However, despite the commitment literature reports a parallel incorrect IAS 2 application in literature (Al-Daoor, 2008; Monea, 2011; Asiri, 2014; Onyekwelu, 2014; Daraghma, 2018). Table 3 show the IAS 2 problems and areas explore in diverse countries and the application status. Further relevance of the IAS 2 application is reported is the availability of mandatory and useful information to stakeholders (Honkova, 2015; Shusheng, 2014). Despite this, there still exist difficulties in accounting for inventories due to certain aspects for instance: the elevated activity capacity, several accepted cost flow substitutes, and inventories classification (Monea, 2011. Daraghma, 2018). The poor application of IAS 2 is also coupled with the practitioner choice of US GAAP over the IAS (Al-Daoor, 2008; Obaidat and Al-Hajaia, 2013; Asiri, 2014; Kral, 2014; Onyekwelu, 2014: Daraghma, 2018). Daraghma, (2018), attributed the misapplication of IAS 2 in developing and emerging economies to lack of expert accountant, nature of the entity, uncontrolled published financial statements and auditor incompetency. The same study also reveals a better application of the IAS 2 in public held and industrial corporations in contrast to private and commercial corporations.

Table 3: IAS 2 identified aspects examine in different countries.

IAS 2 aspects	Correctly/incorrectly	Countries	Author
Uses all methods W.A, FIFO, and LIFO	incorrectly	Palestinian	Al-Daoor, 2008
“A lack of harmonization between the IAS and Saudi Arabia accounting standards. Inconsistency”	incorrectly	Saudi Arabia	Asiri, 2014
“Corporation apply the IAS 2”	Incorrectly. RECOMMEND “intensive training for their accounting staff to get them to become IFRS compliant”	Nigerian	Onyekwelu, 2014
“Difficulty of accounting for inventories arises from several factors.”	incorrect	Romania	Monea, 2011
“Poor application of the IAS 2”	incorrect	Palestine	Daraghma, 2018
“The study of reveals listed corporations inventory measure as explained in the IAS 2.”	correctly	Bangladesh	Nisha, 2015
“Inventory valuation and the compliance with IAS 2”	correctly	Bangladesh	Mia and Qamruzzaman, 2016
“IAS 2 is respected and applied in the Czech accounting legislation.”	correctly	Czech	Kral, 2014
“Prepare financial statements in accordance with IAS/ IFRS.”	correctly	Czech	Honkova, 2015
“Explores the value relevance resulting from the selections of inventory valuation techniques over China GAAP.”	correctly	China	Shusheng, 2014
“Explores the reality of applying IAS in industrial corporations.”	correctly	Jordan	Obaidat and Al-Hajaia, 2013

4.2 Discussion on IAS 2 Practicality

From the discussion, it is evident that although the definitions and scope provide a clear interpretation of the standards for practitioners with a clear indication of what fits in the current assets classified as inventories. There exist positive and negative critiques on the IAS 2 prescription and application as indicated above. As well as there are equal benefits and challenges on the application of the IAS 2 standards. Substantiating these critiques based on the IAS 2 practicality.

Many organisations strive for a balance in the globalization era with the intention to attract investors from within and outside a country borders that will boost their company's performance. Investors on the other hand gained valuable information from a company annual statement that enables them to make an informed decision of whether to invest or not. Amidst globalization of the world economy the IFRS present a convergence and harmonise financial statements that afford valuable insights to stakeholders (Chand and White, 2007; Maisuradze, 2018).

As part of current assets, inventory is required to meet the criteria for definition and recognition. And as aforesaid diligence needs to take into the preparation of the financial statement that reports the companies' inventory. Valuing inventory according to IAS 2 at the LC or NRV, many aspects are to be considered since it affects the cash flow and cash equivalents. This justifies why some companies include unsold inventory in the inventory cost. Moreover, companies' solvency is directly impacted by the unsold inventory which becomes an expense when it is sold. Hence, the need for the IAS 2 prescription is highlighted by the significant impact on the entities state of solvency and performance. Furthermore, indicating the detrimental consequences of underestimating the valuation of inventory in companies.

Companies have two inventory systems to select from namely: perpetual and periodic to record inventory. The inventory accounts also include costs that are permitted in the IAS 2 such as transportation cost. Prior to the presentation in the annual financial statements, there are transaction and event that needs to be accounted for. If a perpetual system is used by a company the purchase cost and related cost as permitted by the IAS 2 and accounted for in the inventory account, and for every sale made the inventory accounts and cost price is updated by credit, while the cost of sales is debited. On the other hand, when the periodic system is used the cost of sale is only determined at the end of the financial period. In this system, the purchase cost and related inventory cost is added to the opening inventory and the closing inventory value after the physical count is subtracted. A framework of the determination of inventory in practice entails: physical count /stocktaking that can be done severally or once in a year, determination of cost price to be recognized as expense in the income statement, application of selected formula and the net realizable value to be reported in the financial statement.

Furthermore, IAS 2 allow valuation methods WA, FIFO and NRV to independently present credible information in the determination of inventory cost to be reported. The WA is advantageous for companies that purchase huge quantities of goods at low values and diverse prices. Also, for companies that retain inventories for a long time. However, this method does not report on the financial statement the latest replacement cost given that it does not use the current cost in the determination of the inventory. Hence, a company like Shoprite holding Ltd that retained their stock for a longer period of time in most of their outlets uses this method. And their financial position statement will not represent the latest replacement value. For example, if they present the following for a certain item in one of their supermarket Item X.

Table 4:

Date of Purchase	Purchases units	Unit price R	Cost of Sales R
15 FEBRUARY 2020	250	5.00	1250
25 FEBRUARY 2020	300	4.50	1350
28 FEBRUARY 2020	800	4.05	3240
30 FEBRUARY 2020	150	5.20	780
	2000		8670

*Sales for the month of FEBRUARY 20 1350 ; *On-hand 31 FEBRUARY 20 650

The Weighted average cost that will be used will be R4.34 (8670 /2000) and resultantly the cost of

sale will be R5852.25. The closing inventory will then be R2821. There is a clear contrast in the value of the inventory of R4.34 that will be on the financial position and the latest replacement cost of R5.20. Similarly, the FIFO method of valuation measures the inventory on hand lower than the replacement cost. Using the above illustration value for the FIFO it is clearly evident that the in both case the profit will be superficial. According to the FIFO the closing inventory is R2805 whereas to replace the remaining 650 units is R3380. While the difference of R575 (3380-2805) will be referred to as paper profit attributed to the directors or shareholders and retained to replace inventory.

Date of Purchase	Purchases units	Unit price R	Sales	On Hand	Cost of Sales R	Cost of goods on hand
1 FEBRUARY 2020	500	4.10	500		2050	
15 FEBRUARY 2020	250	5.00	250		1250	
25 FEBRUARY 2020	300	4.50	300		1350	
28 FEBRUARY 2020	800	4.05	300	500	1215	2025
30 FEBRUARY 2020	150	5.20		150		780
	2000				5865	2805

Furthermore, there is also going to be a difference in the gross profit for both methods. Supposing the selling price is R7 then the gross profit will be as follows:

	Weighted Average	FIFO
Sales (1350 x 7)	R9450	R9450
Cost of Sales	(R5852.25)	(R5865)
Gross Profit	R3597.75	R3585

While unsold inventory is valued at NRV or the LC which is logical and in the financial statement reports other inventories are obsolete and damage at are valued at NRV. It will be misleading if this is not accounted for properly. The importance of correct valuation is herald in the illustration in study that present evidence of the IAS 2 inventory in the annual financial statements. Many financial elements measure and reports will be grossly affected by an incorrect valuation. This will subsequently lead to incorrect analysis and interpretation of the information on both the financial position and performance of the company. Also, it will lead to wrong and unfavourable management decisions.

4.3 IAS 2 application in SA companies

From the onset of the IFRS, many companies have adopted the IAS 2 in a bid to attain a harmonised financial information that offers stakeholders insight. Two South African companies are used in this study are namely: Sasol Ltd and Shoprite Holdings Ltd. Sasol is a global integrated chemicals and energy company spanning 30 countries. SASOL is a public company listed on the Johannesburg Stock Exchange in South Africa and the New York Stock Exchange in the United States. Sasol source manufacture and market chemical, and energy products globally. Shoprite Holdings Limited is registered and incorporated in the Republic of South Africa with Registration number 1936/007721/06 and ISIN no: ZAE00012084 is also on the Johannesburg Stock Exchange in South Africa with JSE share code: SHP, and the New York Stock Exchange with NSX share code: SRH. Shoprite Holdings” or the “Company is a retail company that emerged in 1979 with their first stores and has grown to own many subsidiaries. Shoprite Holdings present its daring vision for the future as one that would see the Group expand its strength, to eventually becoming today premier food retailer. Also, list their investors online with other relevant information pertaining to the company. In the past 40 years, Shoprite Holdings Limited has continually created its brand trust, recognition and goodwill in all the resident countries. And with over 141 000 people and over 2 829 stores in 15 African nations, Shoprite Holdings Limited strives to seize fresh prospects for growth in the years ahead.

These companies published their annual statement online to provide the stakeholder with

information regarding their interest in the company. The published annual reports of these companies are required to present policies that are used in the preparation of their audited annual financial reports. The designated portion relating to the IAS 2 and the financial statements was explored in this study and access links of the complete report are reference below. The reports as mandated by the company Act, of 2008 needs to be audited and it begins with the auditor reports to the directors whilst stating the auditor responsibility to be based on the International Standards on Auditing. Hence all the financial statements are prepared to be in compliance with the IFRS and the Company Act, 71 of 2008. These companies use the auditor, Price Water House Cooper Incorporated (PwC) to audit their annual financial report.

On both reports, the auditor states the compliance of IAS as part of their duties to ensure that the statements and reports are in accordance with the required standards and guidelines. PwC presents references to all standards, interpretations, pronouncements and act commitments adherence with the Directors of the respective boards' approval of the issues. The two reports use are for the 2020 financial year. In the report on the financial statements report the inventories value, cost of sales and other inventory aspects. Which is a clear indicator that South African companies are IFRS and IAS2 compliant. They determine their inventories according to the prescription and accounting policies related to IAS 2. SASOL disclosed how their inventories methods and inventory changes are also accounted for in materials, energy and consumables used in SASOL. Also, inventories are write-down to NRV as required by IAS 2 Figure 2.

Similarly, Shoprite Holding Ltd also discloses and report inventory according to the IAS 2 and with compliance to the IFRS. Inventories are written off to the statement of comprehensive income along with the related items as per the accounting policies for the respective items. Furthermore, from management views the cost of inventories sold are provided with a consistent complete measure of the income statement impact of the overall supplier relationship. Hence highlighting the role and need for prudent accounting for inventories. Their valuation of inventories also follows the weighted average cost and NRV taking into consideration the cost of their merchandise to consist of the invoice price; insurance; freight; customs duties; appropriate distribution between centres and stores; trade discounts; advertising and other rebate and settlement discounts.

	Group		Company	
	2020	2019	2020	2019
for the year ended 30 June	Rm	Rm	Rm	Rm
4 Inventories				
Carrying value				
Raw materials	321	273	254	218
Process material	1 407	1 454	1 404	1 452
Maintenance materials	3 636	3 759	3 469	3 583
Work in process	737	693	737	693
Manufactured products	3 876	4 236	4 041	4 424
Consignment inventory	40	67	39	66
	10 017	10 462	9 944	10 416

The impact of lower chemical product prices has resulted in a net realisable value write-down of R37 million in 2020 (2019 – R68 million) for the group and company. No inventories are encumbered. Inventory of R78 million (2019 - R72 million) is held at net realisable value for the group and company.

Accounting policies:

Inventories are stated at the lower of cost and net realisable value. Cost includes expenditure incurred in acquiring, manufacturing and transporting the inventory to its present location. Manufacturing costs include an allocated portion of production overheads which are directly attributable to the cost of manufacturing such inventory. The allocation is determined based on the greater of normal production capacity and actual production. The costs attributable to any inefficiencies in the production process are charged to the income statement as incurred.

By-products are incidental to the manufacturing processes, are usually produced as a consequence of the main product stream, and are immaterial to the group and company. Revenue from sale of by-products is offset against the cost of the main products.

Cost is determined as follows:

Raw materials	First-in-first-out valuation method (FIFO)
Process, maintenance and other materials	Weighted average purchase price
Work in progress	Manufacturing costs incurred
Manufactured products including consignment inventory	Manufacturing costs according to FIFO

	Note	Group		Company	
		2020 Rm	2019 Rm	2020 Rm	2019 Rm
for the year ended 30 June					
30 Cash flow from operations					
(Loss)/Earnings before interest and tax ((LBIT)/EBIT)		(31 068)	11 885	(30 477)	5 361
Adjusted for					
share of profits of equity accounted investments	22	(29)	(44)	(9)	(8)
equity-settled share-based payment expense	36	1 254	1 053	1 217	1 018
depreciation and amortisation		11 179	11 531	8 116	8 700
effect of remeasurement items	8	42 608	5 907	37 377	8 286
Expected credit losses		99	96	38	61
movement in long-term provisions					
Income statement charge	32	(1 890)	307	(1 888)	312
utilisation	32	(121)	(31)	(121)	(303)
movement in short-term provisions		(88)	199	(90)	222
movement in post-retirement benefits		196	221	195	221
movement in long-term deferred income		233	25	233	26
movement in financial assets and liabilities		1 560	-	1 545	-
write-down of inventories to net realisable value	24	37	68	37	68
other non-cash movements		(129)	241	(225)	207
		23 841	31 178	15 948	24 171

Figure 2: SASOL Inventories determination and accounting policies disclosure

The NRV employed is the selling price in the ordinary course of business. Their subsidiaries also measure inventory in the LC and NRV. And as aforementioned regarding the treatment of inventories, sold inventories are included and recognised in their relevant section such as the cost of sale in the income statement. The financial statement of both companies indicate their disclosure and inventories treatment. And it is evident that compliance and presentation of IAS 2 are instituted and follow by South Africa public companies. A complete report of the annual financial report can be obtained from the following links: “<https://www.sasol.com/investor-centre/financial-reporting/annual-integrated-reporting-set> Accessed 12/11/20 4pm; <https://www.shopriteholdings.co.za/search-results/shopriteholdings-documents/financial-statements.html>, Accessed 12/11/20 5pm”.

5. Conclusion

From the practical illustration, it clearly evident from the published statements in the annual report that IFRS contributes significantly to the information quality reported which is one of the positive impacts of IAS 2 prescription. The inventories discuss in practice coupled with empirical findings provides a sound measure of the IAS 2 prescription rollout and impacts on an entity’s financial statements. The aim of this study was to explore the IAS 2 prescription in light of existing theoretical and empirical studies. Hence, the effects of the IAS 2 implementation on both historical, accounting base and practicality on companies was explored. These effects of the IAS 2 prescribe in inventory determination were examined and findings show the differences that exist particularly in the valuation methods, as well as between the IFRS IAS 2 and GAAP application in the different nations that hinders the harmonisation of standards in achieving globalisation. The impact of the IAS 2 on entity financial reporting was investigated and the findings reveal a significant impact directly and indirectly on the financial position and performance of a company. A keen interest stems from the unsold inventories that are accounted for at a NRV with the reason that they may be sold within a year and subsequently become expense once they are sold. Their disclosure on the financial positions produces a direct impact on the company’s solvency.

Furthermore, the empirical evidence of this study shows the impact of the IAS 2 inventories influences on the financial reporting of companies and the diverse inventory determination method effects on the financial position and performance. This finding also reveals and support prior studies that highlight the most prominent shortcoming of IAS 2, to be the application of the method that varies across organisations. Therefore, in the light of these study findings it is, suggested that in order to enhance the IAS 2 prescription emphasis should be placed IAS 2 prescribe application. Although

the IAS 2 prescription has significant impact and influences on the globalization, harmonisation of IFRS and solvency and profitability of a company. Notwithstanding, unifying the diverse methods of valuations of inventories can afford significant benefits and insight. Hence, it is recommended that standard setters should consider prescribing a unit method for the valuations and treatment and also serve a tangible framework to drive the correct application of IAS 2 application. Furthermore, persistent compliance should be necessitated from companies.

Despite this study being resident on the theoretical nature that is void of a robust pragmatic base. However, the conclusions drawn from this study afford significant acumen to scholars and practitioners to advance the financial reporting in entities. Likewise, the ascertained impact of IAS 2 on the financial statements that incorporated indirect and direct benefits, provides ground for concrete decisions to be made, as well as afford valuable and quality information. Furthermore, established that insight afforded by the inventory disclosed on the financial statement attract investors or dissuade them. Future studies can seek to measure the extends of incorrect application of IAS 2 application, investigate the impact of the IAS 2 compliance on organisational performance, examine of the information content of the application of IFRS and IAS 2 applications, and identify the IAS 2 application compliance impact variables.

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