

Can it classify as Inventory or PPE?

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Introduction

ABC shipping (private) Limited is a limited liability company incorporated in Sri Lanka and registered under the companies Act no 7 of 2007. It is a transportation Company. Company owns a ship which is called as "Meritine". The principle activity of this Company is transporting gas & fuel by using this ship.

Generally there are two cylinders in every ship in order to balance the ship. Most of the ships have filled these cylinders by using oil but here, this ship has used gas to fill these cylinders. Normally this ship is repaired once per every four years. When repairing ship, the gas filled in the cylinders will release to the air which would be a loss to the company.

Discussion of the Issue

During the year Company has identified this Gas stock in cylinder as Inventory under LKAS 02. Value of Gas Stock is 4 million.

The issue is whether this gas stock in cylinder should be recognized under LKAS 02 "inventory" or LKAS 16 "Property Plant and Equipment".

According to the definitions of LKAS 02 (paragraph 6), inventories are assets:

- **Held for sale in the ordinary course of business;**
- **In the Process of production for such sale; or**
- **In the form of material or suppliers to be consumed in the production process or rendering of service.**

Above mentioned Gas stock in cylinder is not held for sale in the ordinary course of business or consumed in the transport process. That means this inventory does not meet the definition of the inventory.

According to LKAS 16 (paragraph 6 & 7), the cost of an item of Property Plant and Equipment shall be recognized as an asset if, and only if:

- **It is probable that future economic benefit associated with the item will flow to the entity; and**
- **The cost of item can be measured reliably**
- **Expected to be used more than one period.**

Since above mentioned Gas stock is providing facility to do company operation, so without this Gas stock in cylinder ship cannot do its operations. So this Gas stock generates future economic benefit to company. The cost of this Gas stock can be measured reliably. At the same time this Gas stock in cylinder is expected to be used

four years. Therefore this Gas stock in cylinder should be recognized as Property Plant and Equipment under LKAS 16.

Implication of the Issue

Since the company has identified this Gas stock in cylinder as the inventory there would be an overstatement of profit before tax and understatement of non-current assets for the year ended 31 March 2015.

Recommendation

Based on the above analysis, it is recommended to recognize this gas stock in cylinder as property plant and equipment and it should be depreciated component vice separately over four years under LKAS 16. Following entries are recommended to adjust the financial statements.

Reversed the stock

1. Property plant and equipment A/C	Dr.	4,000,000	
Inventory A/C		Cr.	4,000,000

Depreciation for the year.

2. Depreciation Expense A/C	Dr.	1,000,000	
Accumulated Depreciation A/C		Cr.	1,000,000

(During the year charge for the depreciation, charged to the Statement of Comprehensive Income)