Inventories

Accounting Policy Manual

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1 PURPOSE

The objective of this policy is to prescribe the accounting treatment for inventories. This policy complies with the requirements of AASB 102 *Inventories*.

The principal accounting issues addressed by this policy are the determination of the cost of inventories, the formula used to assign cost to inventories and their subsequent recognition as an expense.

This policy also includes the accounting treatment for rotatable assets, meter returns, and critical spares.

2 SCOPE

This policy shall be applied to the accounting for all inventories held for the purpose of maintenance, repairs and operations.

In addition to the general inventory categories, this policy also applies to the accounting treatment of rotatable assets, meter returns, and critical spares.

3 DEFINITIONS

Inventories are assets in the form of stores, strategic spares, general purpose materials and maintenance stocks that will be consumed in the process of maintenance, repairs and operations. Inventory also includes assets that are held for sale in the ordinary course of business.

Cost is the amount of cash or cash equivalents paid or the fair value of other consideration given to acquire an asset at the time of its acquisition or construction.

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.

Rotatable assets are items of property, plant and equipment that are taken out of service and stored as a spare part (to be used in less than 12 months).

Critical spares are specific items of inventory that are essential for the continued operation of assets or machinery, held in reserve for future use in projects or asset maintenance. These spares are not part of ongoing operations but are reserved for unforeseen or emergency situations and are incorporated into a project or asset when required.

4 FUNDAMENTAL CONCEPTS

Inventories are purchased at different times and at different prices. Cost is determined using the costing method outlined in section 4.2 which takes into account these differences.

Inventories shall be measured at the lower of cost and net realisable value. That is, inventories should not be carried at a value that exceeds the value expected to be realised from their use or sale.

4.1 COST OF INVENTORIES

The cost of inventories includes all costs of purchase, conversion and any other costs incurred in bringing the inventories to the location and condition necessary for it to be capable of operating in the manner intended by management. The cost of conversion includes direct materials, direct labour costs and allocated overheads.

Cost includes all import duties and other non-refundable purchase taxes, transport and handling costs and any other directly attributable acquisition costs (refer to section 4.3 of accounting policy FIN 10-11 *Capex vs. Opex* for further examples).

Cost excludes any trade discounts, rebates and other similar items and any abnormal amounts of wasted material, labour or other resources.

Administrative overheads and storage costs are not included in the costs of inventories.

4.2 COSTING METHOD

AusNet Services adopts a weighted average cost formula for each inventory category, except as noted below.

The weighted average cost formula is as follows:

Total cost of inventories at the beginning of the period + cost of inventories purchased during the period

divided by Total units outstanding at the beginning of the period + units purchased during the period.

This costing method applies across AusNet Services without regard for the location of the item of inventory.

4.3 NET REALISABLE VALUE

Inventories shall be measured at the lower of cost and net realisable value, to ensure inventories are not carried at values in excess of the amounts expected to be realised from their sale or use.

The cost of inventories may not be recoverable if those inventories are damaged or if they have become wholly or partially obsolete.

Net realisable value is determined using the most reliable evidence available at the time, such as the latest market price.

4.4 RECOGNITION AS AN EXPENSE

When inventories are consumed for maintenance, repair or operational purposes, or sold, the relevant cost is expensed immediately in the P&L using the formula below:

Number of units consumed X weighted average cost per unit

The exception to this is where a specific cost has been assigned to an item of inventory that specific cost shall be recognised as an expense.

4.5 INVENTORY WRITE-DOWN

If the cost of an item of inventory exceeds its net realisable value, the item of inventory shall be written-down by the amount of the excess and an expense recognised immediately in the P&L.

Write-downs usually occur on an item-by-item basis, unless it is appropriate to group similar or related items.

New assessments of net realisable value are made in each subsequent period. If the circumstances that previously caused inventories to be written-down no longer exist, the write-down shall be reversed (however the reversal is limited to the amount of the original write-down) and offset against any inventories recognised as an expense in that period.

Write-downs are initially recorded in the provision for inventory write-downs, and the cost is de-recognised when the inventory is disposed of.

4.6 STOCK COUNT

Stock counts can be conducted on a rolling basis, however, all inventories are to be physically counted at least once a year.

Any item of inventory that cannot be located during a stock count or any item of inventory that is in excess of the inventory system quantity shall be written off as an expense or written up as income in the P&L immediately after a thorough investigation process has been conducted by Procurement.

Procurement will complete their investigation within one month of the issue being identified. If the investigation is not completed within one month, the item will be written up or down as appropriate unless an extension of time to complete the investigation is formally approved by the Group Financial Controller.

5 FINANCIAL STATEMENT CLASSIFICATION

Inventories shall be classified as current if the item is expected to be issued from stock in the next twelve months. If expected issuances have not been forecast, an assessment of expected issuances can be based on past usage rates or other appropriate drivers.

Inventory that is not expected to be utilised in the next twelve months is classified as non-current.

6 ROTATABLE ASSETS

Assets taken out of service and transferred to inventory are considered to be rotatable assets.

Assets taken out of service can only continue to be recognised as an asset (in the form of inventory) if they satisfy the asset recognition criteria described in FIN 10-11 *Capex vs. Opex.*

(a) it is probable that future economic benefits associated with the item will flow to AusNet Services; and

(b) the cost of the item can be measured reliably.

That is, there has to be a future benefit expected from the asset, either from its future use, or subsequent disposal in order to continue to recognise the item as an asset.

Assets taken out of service that do not meet these criteria shall be immediately written-off and recognised as an asset de-recognition in line with FIN 10-10 *Property, Plant & Equipment.* Furthermore, rotatable assets can only be classified as such if they are expected to be used in less than 12 months. If this is not the case, they should be classified as property, plant & equipment.

6.1 ACCOUNTING TREATMENT

Where an asset is taken out of service and it continues to meet the recognition criteria outlined above, it shall be removed from the Fixed Asset Register and transferred to inventory at its carrying value at the date it is taken out of service. This will be a direct transfer to the respective balance sheet accounts.

Where an asset is returned to service, it is removed from inventory and added to the Fixed Asset Register at its carrying value at the date it is returned to service. Similar to the capitalisation of new assets, the asset returned to service will be recorded as part of Work In Progress until it is formally cleared to an asset in service category. Rotatable assets are not depreciated as they form part of inventory.

Relocation costs associated with transferring property plant and equipment to and from rotatable assets cannot be capitalised. Although this type of cost would normally be capitalised as part of the cost of property plant and equipment under FIN 10-11 *Capex vs. Opex* and for inventory under this policy, given that the nature of a rotatable asset means it may be moved many times over its life, the costs of relocation do not form the cost of bringing it to the location and condition necessary to be capable of operating as management intends.

Costs to refit or repurpose the asset when being taken out of inventory and put into Property, Plant & Equipment can be capitalised if they are required for the asset to operate in its new function.

7 METER RETURNS

When a functional meter is returned from active use back into inventory our policy is to derecognise the meters from property, plant and equipment and recognise in inventory at written down value. For meters that are no longer functional the transaction is transaction is treated as a retirement of property, plant and equipment. There is a methodology in place to estimate the amount of meters that have been returned to inventory versus those that must be retired.

CRITICAL SPARES

Critical spares refer to physical assets, such as isolating transformers, that are held in reserve for future use in projects or asset management. These items are not part of ongoing operations and do not provide economic benefits or contribute to the production of goods or services until they are incorporated into a project or asset.

In accordance with AASB 116, items such as spare parts, stand-by equipment, and servicing equipment are recognised as property, plant, and equipment only when they meet the definition of such assets. If they do not meet the recognition criteria for property, plant & equipment, these items are classified as inventory under AASB 102.

For regulatory accounting purposes critical spares shall be classified as inventory under AASB 102 until they are required for use. They will not be recognised as property, plant & equipment unless they meet the asset recognition criteria as outlined in FIN 10-11 Capex vs. Opex.

Critical spares can only be recognised as assets (in the form of inventory) if they satisfy the following conditions:

(a) it is probable that future economic benefits associated with the item will flow to AusNet Services; and

(b) the cost of the item can be measured reliably.

That is, there has to be a future benefit expected from the asset, either from its future use, or subsequent disposal in order to continue to recognise the item as an asset.

Where a critical spare meets the recognition criteria in FIN 10-10 Property, Plant & Equipment, it shall be removed from inventory and transferred to the Fixed Asset Register at its carrying value at the date it is first used in a project or incorporated into an operational asset. This will be a direct transfer to the respective balance sheet accounts.

Until they are used, critical spares shall remain classified as inventory. Critical spares that do not meet the above criteria or are not expected to provide future economic benefits shall be written off and recognised as inventory adjustments, in line with FIN 10-10 Property, Plant & Equipment.

9 TAX TREATMENT

The writing down of inventory for book purposes is not immediately deductible for tax purposes. A tax deduction is only available when the assets have been physically disposed of. Any proceeds received on disposal will be treated as assessable income when received.

10 SCHEDULE OF REVISIONS

Issue	Date	Author	Details of Change
1	01/03/2017	Heath Preston	Published
2	13/08/2018	Sasha Marinicheva	Addition of Section 7 Meter Returns.