ASBJ Statement No. 9

Accounting Standard for Measurement of Inventories

July 5, 2006

Accounting Standards Board of Japan

Remarks on the Release

The Accounting Standards Board of Japan (ASBJ) has deliberated the revision of the current measurement method of inventories which allows entities to apply either the cost method or the lower-of-cost-or-market method, in light of consistency with other accounting standards which has developed recently in Japan as well as harmonization with international accounting standards.

The ASBJ has classified inventories as those held for sale in the ordinary course of business and those held for trading purposes. Specifically, the ASBJ has deliberated the measurement method and the disclosure of the former in connection with write-downs due to decreased profitability of assets. On the other hand, the ASBJ has deliberated to treat the latter in accordance with accounting for trading securities in "The Accounting Standards for Financial Instruments."

Preceding the public release of this Standard, the ASBJ requested comments as widely as possible releasing the discussion paper on "Measurement of Inventories" in October 2005. The comments received were reflected in an exposure draft released in April 2006. The queries raised and further comments given to the exposure draft were reviewed to revise the draft. The ASBJ approved the above-captioned accounting standard (hereinafter referred to as the Standard) for public release at the 107th ASBJ meeting of June 30, 2006.

Outline of the Standard

Objective

The objective of this Standard is to prescribe the measurement method of inventories at the end of the period and their disclosure. Accordingly, cost formulas such as the first in, first out (FIFO) method or the last in, first out (LIFO) method are not set out in this Standard.

Accounting Treatment

Measurement Method of Inventories Held for Sale in the Ordinary Course of Business

(1) Writing inventories down below cost to net selling value

Inventories held for sale in the ordinary course of business in principle, shall be carried at the acquisition cost on the balance sheet. However, in the case that the net selling value falls below the acquisition cost at the end of the period, inventories shall be carried at the net selling value on the balance sheet, regarded as decreased profitability of assets.

The net selling value in this context is defined as the selling price less additional estimated manufacturing costs and estimated direct selling expenses. Under certain conditions, the usage of replacement cost or any appropriate value that reflects decreased profitability of assets are accepted on behalf of the net selling value.

(2) Reversal of write-downs of inventories

Entities have a choice of applying the reversal method or the non-reversal method provided that they continue to apply the same method in the following periods. The reversal method allows reversal of write-downs of inventories recognized in the previous period by related items, and/or by causes of write-downs (damage, obsolescence, and decrease in the selling price due to the fluctuation of the market). The non-reversal method prohibits reversal of write-downs of inventories.

Measurement Method of Inventories Held for Trading Purposes

Inventories held for trading purposes shall be carried at the market price on the balance sheet. The amount of difference between the market price and the book value shall be treated as profit or loss of the period.

Disclosure

Disclosure of Inventories Held for Sale in the Ordinary Course of Business

(1) Presentation on the income statement

The Standard treats the write-downs due to changes in price level with the same accounting treatment as the loss of deterioration and obsolescence based on the former accounting standards. Thus, the write-downs of inventories due to decreased profitability of assets shall be recognized as cost of goods sold, whereas they shall be recognized as manufacturing costs if the decreased profitability of assets is arisen inescapably in the course of production.

(2) Footnote on the income statement

The Standard requires the write-downs resulted from the decreased profitability of assets shall be indicated in the category of cost of goods sold or in a footnote. However, this is not necessarily applied to the case in which the write-downs of inventories are not significant.

Disclosure of Inventories Held for Trading Purposes

The Standard requires any profit or loss arisen from inventories held for trading purposes shall be presented in sales on net.

Effective Date

Entities shall apply this Standard for the fiscal year beginning on or after April 1, 2008. This Standard may also be applied to fiscal years prior to April 1, 2008.

Treatment for the First-time Application of This Standard

In the fiscal year when entities apply this Standard for the first time, they may recognize the write-downs as extraordinary loss based on either of the following methods if the amount of the write-downs is extremely large and is related to inventories at the beginning of the period.

(1) By assuming this new Standard is applied to the inventories at the beginning of the period, the amount difference included in the beginning inventories is regarded as extraordinary loss.

(2) By applying this new Standard to the inventories at the end of the period, the amount difference included in the ending inventories and attributed to the prior periods is regarded as extraordinary loss.

(Reference)

Criteria of valuation for decreased profitability of assets and for the threshold amount of the write-downs

Valuation		Definition	Note
Net selling value (paragraph 5)	Based on market price	• Net selling value = Selling price - Additional estimated manufacturing cost - Estimated selling expenses • Selling price is used in this Standard with the meaning specified: market price of the resale market, when resale and purchasing markets are separate.	• Market price observable in the resale market shall be considered as selling price.
	Based on rationally calculated amount	Same as above	• If the market price is unobservable in the resale market, a rationally calculated amount shall be considered as selling price. • The above price shall be estimated as the market price of the resale market. (paragraph 48) • This includes the amount based on the actual sales around the year-end period or the amount based on the contract. (paragraphs 8, 48)

Valuation	Definition	Note
Alternatives for net selling value (Paragraph 9)	・ Writing carry amount down below cost to estimated disposal value. ・ Regularly writing carry amount down when the inventories are held over a certain turn-over period.	Applied to inventories that are either slow-moving and out of operating cycle, or expected to be disposed, whose selling values are difficult to be calculated rationally.
Replacement cost (Paragraph 6)	Amount including the cost incurred on the market price of the purchasing market, when resale and purchasing markets are separate.	Applied to inventories whose net replacement costs are easily calculated and also expected to be linked with their net selling values ; such as raw materials etc. (Paragraph 10)