Chapter 35 - Inventories

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35.10.10 Policies in this chapter are minimum standards

The purposes of an inventory system are: 1) to provide control and accountability over inventories, and 2) to gather and maintain information needed to prepare financial statements.

The policies and procedures in this chapter are the minimum requirements that State agencies must meet. An agency may maintain its inventory system(s) in greater detail, or use additional supporting documentation, as long as the agency meets the required minimum standards.

35.10.15 Authority for these policies

The Office of the State Controller is required by Title 5, Chapter 143, Section 1541, to establish a Generally Accepted Accounting Principles (GAAP) based accounting system and procedures to ensure the State's assets, including inventories, are properly accounted for, and that the State of Maine prepares and completes all financial statements in accordance with all governing rules, statutes and GAAP.

35.10.20 Applicability

All agencies of the State of Maine must comply, unless otherwise exempted by statute.

Agencies may request a waiver from complying with specific requirements of this chapter. Refer to Subsection 1.10.40 for information on how to request a waiver.

35.10.25 Agency responsibilities

The administrative head of each agency is responsible for developing internal policies and procedures to protect and control the use of all fixed assets. Agencies are to consider the cost vs. benefit in developing their individual policies and procedures. The agency head must designate, in writing, one or more Agency Inventory Officers who are responsible for maintaining and safeguarding the agency's inventories. The Inventory Officers must be independent of the receiving and accounts payable functions to provide the proper segregation of duties. These responsibilities include:

- Selecting appropriate inventory accounting methods and systems from acceptable alternatives (refer to Subsection 35.10.35 and Section 85.56);
- Defining and documenting the inventory control points;
- Developing and implementing policies and procedures to safeguard, control, and account for inventories;
- Planning, conducting, and reconciling the physical inventory with inventory records;
- Documenting selected inventory valuation methods;
- Documenting physical inventory procedures; and,
- Performing other duties necessary to account for and report inventories.

35.10.35 Agencies may select among inventory alternatives

This chapter, in conjunction with Section 85.56, offers alternatives to account for and report inventories. Agencies may:

1. Adopt an inventory valuation method from the methods defined in Subsection 35.10.45;
2. Use either the periodic or perpetual inventory system as defined in Subsection 35.10.50; and,
3. Use either manual or automated inventory systems.

Refer to Section 85.56 for instructions on accounting for inventories by fund type.

35.10.40 Reporting requirements for inventories

35.10.40.a All merchandise and donated inventories must be physically counted, valued, and recorded in the general ledger.

35.10.40.b Consumable inventories must be physically counted, valued, and recorded in the general ledger when the balance on-hand at an inventory control point is estimated to exceed $25,000 in value. In calculating the balance on-hand, agencies may exclude those items characterized by high turnover rates and extremely low unit costs; such as nuts, bolts, screws, washers, etc. These items are sometimes referred to as “bench stock” items. The Agency Inventory Officer must define, in writing, the items which they consider bench stock.

35.10.45 Inventory valuation methods

35.10.45.a An agency may select different inventory valuation methods for different inventories; however, the selected methods must be applied consistently to the inventories for which they are chosen. Agencies must document the methods selected to account for and report inventories to ensure they are consistently applied.

35.10.45.b Agencies must include changes in inventory valuation methods, and the financial effects of those changes on an agency’s financial statements, in fiscal year-end financial disclosures reported to OSC.

Acceptable inventory valuation methods include:

35.10.45.c **First-in, First-out (FIFO) –** The FIFO method allocates costs on the assumption that goods are consumed or sold in the order in which they were acquired. The first goods purchased are assumed to be the first used or sold. Inventory on hand is assumed to represent the most recent acquisitions.

35.10.45.d **Last-in, First-out (LIFO) –** The LIFO method allocates costs on the assumption that the last units acquired are the first units consumed/sold. Inventory on-hand is assumed to come from earlier acquisitions.

35.10.45.e **Weighted Average (W.A.) –** The W.A. method values ending inventory based on the average cost per unit for the period.

35.10.45.f **Other** - An agency may use an inventory valuation method other than those described above, as defined in writing by the Agency Inventory Officer.

35.10.50 Inventory systems

35.10.50.a **Perpetual Inventory System** - A perpetual inventory system is one in which the inventory quantities and values, for all purchases and issues, are recorded directly in the inventory system, as they occur. Perpetual inventory balances are verified by means of periodic physical counts. A revolving physical count, where segments of inventories are counted at different times, may be used, provided all inventories are counted at least annually, or every three years for approved agencies with distributed assets.

The Agency Inventory Officer is responsible for developing and implementing procedures to record inventory additions as received and reductions as used.

35.10.50.b **Periodic Inventory System** - A periodic inventory system avoids the necessity of accounting for each addition to and deletion from inventory. Instead, the agency performs a physical count of its inventory every fiscal year end. The agency then values the inventory according to generally accepted accounting principles, and adjusts the accounting records to reflect this value. When this system is used, the agency must maintain a system to document the inventory unit costs used to determine the value.

35.10.54 Physical Inventories

Physical inventories of all items are to be conducted annually. Approved agencies, with assets located in many locations throughout the State (distributed assets), may conduct their inventory on a revolving basis over a three year period.

35.10.55 Who should conduct the physical inventory?

In order to ensure objective reporting of inventory items, physical inventories or inventory counts are to be performed by personnel with no direct responsibility (custody and receipt/issue authority) for the assets subject to inventory count. If it is not feasible to use such personnel for any part of the inventory, those parts are at to be tested and verified by a person with no direct responsibility for the stock.

35.10.60 Physical inventory instructions

Agencies must develop written physical inventory instructions. Distribute and explain these instructions to each person participating in the physical inventory. Include in the instructions: how and where to record each item counted; what information to record, what to do when questions arise, and what procedures to follow when items are located but not listed, or listed but not located. Instructions should include how to find and record those items not being used, in an unusable condition, or in excess quantity. Such information should be used for disposition and future ordering. In most cases, bar coding will be utilized to verify the accuracy of the count. The person counting the assets is to attest to the accuracy of the count by signing their name at the bottom of each inventory page.

35.10.65 Physical inventory reconciliation and documentation

After completing the physical count, the Agency Inventory Officer shall reconcile the inventory by comparing the physical records to the general ledger balance. The inventory is properly reconciled after all differences are identified, explained, and resolved.

Once the inventory is reconciled, the Agency Inventory Officer must certify the reconciliation with a signed, written statement that the inventory is correct. This certification will be reported to the inventory officer's supervisor. If the physical inventory cannot be certified, the inventory officer is to disclose that fact and the supervisor will determine the appropriate action.

35.10.65.a **Perpetual inventory** records must be reconciled with the physical count. The agency must investigate and explain differences, take corrective action when necessary, and adjust the accounting records per Section 85.56. When the reconciliation is complete, the agency inventory officer must certify in writing that the inventory was counted, verified and reconciled.

35.10.65.b Under the **periodic inventory** system, the physical inventory listing, resulting from the physical count, constitutes adequate documentation of the inventory. After the count is complete, the process is one of calculation rather than reconciliation. Assign a cost to the inventory units, according to the method selected, calculate the total cost of the inventory, and process the appropriate accounting adjustments per Section 85.56. The Agency Inventory Officer must certify in writing that the inventory was verified by an actual count.

35.20.70 Retaining physical inventory records

The inventory certification, reconciliation and listing provide support for inventory balances and serve as the basis for accounting adjustments. This documentation must be retained for at least three years after the close of the most recently completed audit. Agencies may adopt a longer record retention policy.

35.10.75 Lost or stolen property

When suspected or known losses of inventories occur, agencies should conduct a reasonable search for the missing inventory. Report any lost or stolen items to your immediate supervisor and the appropriate authorities. Per Title5, Section 1541, subsection 10-A, "All unaccounted for variances, losses, shortages or thefts of funds or property must be immediately reported to the State Controller…"

To dispose of a lost asset, the Agency Property Officer is required to send a signed letter to the Office of the State Controller to delete the asset from the agency's inventory. The letter should indicate the agency, asset type and asset number.