



Buckingham Commons
3503 York Road
Furlong, PA 18925

Part of How-To Series:
Inventory Adjustments

For further information on Integrated Management Solutions and our **FoodConnex** software and services, call **1-800-366-3836** ext **18**, email sales@foodconnex.com, or visit our website www.foodconnex.com

Food Connex Inventory Procedures

Inventory Adjustments

When do I make an inventory adjustment?

Inventory Adjustments must be made for several different reasons, and the way the adjustments are made will affect your inventory costs differently.

Inventory adjustments can generally be categorized as follows:

Stock Quantity Adjustments due to spoilage, damage, theft, samples, etc.

These adjustments are made when stock in the warehouse is taken out of the warehouse for a known reason. Stock quantity adjustments are the most common adjustments made. These adjustments are made at the current cost of the item.

Quantity Adjustments due to a Receiving Error

The adjustments are made when it is discovered after the post that the quantity entered on the computer as received does not match the actual quantity received. These stock adjustments are made at the cost at which the items were received, and will cause the average cost of the item to be re-calculated at the time of the post.

Cost Adjustments due to a Receiving Error

These adjustments are made when it is discovered after the post that a cost was incorrectly entered. The adjustment will affect the value of you inventory, and will cause the average cost of the item to be re-calculated at the time of the post.

One of the biggest problems encountered when incorrectly processing stock adjustments lies in the re-calculation of **average** costs, and the update of **last** and **invoice** costs. These issues are as follows:

If an inventory receipt is used to adjust quantities into stock instead of a stock adjustment, the **last** and **invoice** costs will be updated, when in fact, an adjustment should not affect these costs at all.

If an inventory adjustment is used to receive inventory into stock, the new inventory 'received' will have no affect on average cost and will not update the last cost and the invoice cost. Receipts should affect all three of these costs.

If an incorrect quantity or cost was entered when an item was received into stock, the adjustment must be made to the quantity or cost of the receipt transaction that was in error. This is because the **average cost** of an item is based on the current quantity in stock and the costs of the most recent receipts inventory transactions; if the receipt transaction is not corrected, the average cost will become skewed. An explanation of the **average cost calculation** is on the following page.

Each of the above adjustment categories is handled differently by Food Connex. These procedures, and why it is important to follow them, are discussed in this document. A special emphasis has been placed on the average calculation; **invoice costs and last costs can be manually updated by the user** via the Inventory File Maintenance Cost option; **average costs cannot**.

Food Connex Inventory Procedures

Inventory Adjustments

Average Cost Calculation

The **average cost** of your in-stock items is based on the quantity in stock, calculated on a FIFO (first in / first out) basis, and is re-calculated when any of the following transaction types are posted.

- Inventory receipts
- Purchase order receipts
- Stock Adjustments
- Receiving error quantity adjustments
- Receiving error cost adjustments
- Stock Transfers from warehouse to warehouse

This cost is calculated by finding the last inventory history RECEIPT record and working backwards through inventory transaction history, accumulating receipt quantities until the accumulated receipt quantity is equal to the quantity currently in stock. Note that adjustments and transfers are ignored when this calculation is performed.

In the following example, you have an item that you stock, sell and price by the case. Over the past 5 weeks, you have received 100 cases of this item each week, and have sold none. The receipt transactions are reflected below, showing the most recent receipt first:

Date Received	Cases Received	Cases Sold	Cases Remaining in Stock	Cost per Case	Value
04/29/06	100	0	100	\$45.22	\$4,522.00
04/22/06	100	0	100	\$42.64	\$4,264.00
04/15/06	100	0	100	\$43.96	\$4,396.00
04/08/06	100	0	100	\$46.75	\$4,675.00
04/01/06	100	0	100	\$41.50	\$4,150.00
	500	0	500		\$22,007.00

If you still had all 500 cases in stock, the average cost of the item would be the total extended cost (value) of all of the cases you received divided by the number of cases in stock.

Average Cost equals total value of what is in stock divided by the quantity in stock
Average Cost equals \$22,007.00 divided by 500 CS
Average Cost equals \$44.014 per CS

Food Connex Inventory Procedures Inventory Adjustments

Average Cost Calculation

continued

If you sell 422 CS of this item, and then receive another 100 CS into stock on May 5th, the average cost will be calculated based on FIFO (first in / first out) method.

First In / First Out means that Food Connex will >sell= the cases received on 04/01/06 first, then the cases received on 04/08/06, then the cases on 04/15/06, etc.

Date Received	Cases Received	Cases Sold	Cases Remaining In Stock	Cost per Case	Value
05/05/06	100	0	100	\$44.89	\$4,489.00
04/29/06	100	22	78	\$45.22	\$3,527.16
04/22/06	100	100	0	\$42.64	\$0.00
04/15/06	100	100	0	\$43.96	\$0.00
04/08/06	100	100	0	\$46.75	\$0.00
04/01/06	100	100	0	\$41.50	\$0.00
	600	422	178		\$8,016.16

In the above example, you can see that you sold 422 cases and have 78 cases left in stock before you post the receipt for 100 cases on 05/05/06, at a cost of \$44.89 per case. After the receipt of the 100 cases on 05/05/06, you have a total of 178 cases in stock.

To calculate the average cost of the item when the 05/05/06 receipt is posted, Food Connex will use the 78 cases left in stock from the 04/29/06 receipt, and average their value with the value of the 05/05/06 receipt of 100 cases to re-calculate the average cost.

Average Cost equals total value of what is in stock divided by the quantity in stock

Average Cost equals \$8016.16 divided by 178 CS

Average Cost equals \$45.03 per CS

In the above examples, you can see how important it is that the quantities and costs on each receipt transaction are correct. If errors are made during the receiving process, the user must use the Receiving Error adjustment routines to correct costs and quantities received.

Food Connex Inventory Procedures

Inventory Adjustments

Stock Quantity Adjustments

Stock Adjustments should be used to remove items from stock due to damage, spoilage, samples, or other types of losses.

Generally speaking, there should never be a reason to use stock adjustments to put items into stock. That should be done using the **Inventory Receiving** option or the **PO Receiving** option so that your costs are updated correctly.

If there was a receiving error and additional stock must be received to bring your in stock quantity into balance with the actual count of the item, use the **Quantity Adjustment - Receiving Error** procedure.

Using the example from the previous page, let's say that on 04/29/06, in error, the user only received 10 cases instead of 100 cases. If you had sold 422 cases before you received 100 cases on 05/05/06, you would have had -12 cases in stock. After the 05/05/06 receipt, the average cost calculation would look like this, where the system considers 12 of the last 100 cases already sold when the receipt is posted.

Date Received	Cases Received	Cases Sold	Cases Remaining	Cost per Case	Value
05/05/06	100	12	88	\$44.89	\$3,950.32
04/29/06	10	10	0	\$45.22	\$0.00
04/22/06	100	100	0	\$42.64	\$0.00
04/15/06	100	100	0	\$43.96	\$0.00
04/08/06	100	100	0	\$46.75	\$0.00
04/01/06	100	100	0	\$41.50	\$0.00
	510	422	88		\$3,950.32

*Average Cost equals total value of what is in stock divided by the quantity in stock
 Average Cost equals \$3950.32 divided by 88 CS
 Average Cost equals \$44.8864 per CS*

The average cost of \$44.8864 is \$.1436 less than the correct average cost of \$45.03 we found in our calculation on the previous page where the quantity received was correct on the 04/29/06 receipt.

Food Connex Inventory Procedures Inventory Adjustments

Quantity Adjustment - Receiving Error

Adjustments to in-stock quantities that need to be made due to a receiving error will allow the user to change the quantity received on the original receiving transaction. After selecting the **Quantity Adjustment ▾ Receiving Error** option, the user will be prompted to enter the item to be adjusted, and then a variety of information that will help identify the specific receipt transaction in question.

After the user has selected the receipt transaction to be corrected, the system will allow the user to change the quantity received for that transaction.

When the above adjustment is posted, the system will re-calculate average costs based on the **corrected** received quantity.

What happens if I use a standard stock adjustment to correct the quantity in stock for this item?

Using the standard stock adjustment will result in an incorrect average cost, because the average cost calculation does not take adjustment transactions into account.

After adjusting the 90 cases back into stock, the average cost would be re-calculated as follows:

Date Received	Cases Received	Cases Adjusted	Cases Sold	Cases Remaining	Cost per Case	Value
05/05/06	0	90	N/a	90	n/a	n/a
05/05/06	100		12	88	\$44.89	\$3,950.32
04/29/06	10		10	0	\$45.22	\$0.00
04/22/06	100		100	0	\$42.64	\$0.00
04/15/06	100		100	0	\$43.96	\$0.00
04/08/06	100		100	0	\$46.75	\$0.00
04/01/06	100		100	0	\$41.50	\$0.00
	510	90	422	178		\$3,950.32

*Average Cost equals total value of what is in stock divided by the quantity in stock
Average Cost equals \$3950.32 divided by 178 CS
Average Cost equals \$22.1928 per CS*

The average cost of \$22.198 is \$22.8372 less than the correct average cost of \$45.03 we found in our calculation on the page 3 where the quantity received was correct on the 04/29/06 receipt.

If the user had opted to use the **Receiving Error ▾ Quantity Adjustment** process, the system would have corrected the 04/29/06 receipt, changing the quantity for that receipt from 10 to 100, and the average cost calculation would have been correct, as reflected on page 3.

Food Connex Inventory Procedures Inventory Adjustments

Cost Adjustment - Receiving Error

Cost Adjustments that need to be made due to a receiving error will allow the user to change the cost at which the stock was received on the original receiving transaction. After selecting the **Cost Adjustment B Receiving Error** option, the user will be prompted to enter the item to be adjusted, and then a variety of information that will help identify the specific receipt transaction in question.

After the user has selected the receipt transaction to be corrected, the system will allow the user to change the cost of the item received for that transaction.

When the above transaction is posted, the system will re-calculate average costs based on the new receiving cost, and if the corrected receipt transaction is the **last** receipt transaction, will update the **invoice cost** and the **true cost** for this item.

What happens if I simply adjust out the incorrect receipt and then re-enter the receipt with the corrected cost?

Adjusting out the stock and re-receiving it at the correct cost will result in an incorrect average cost because the original receipt transaction still has the incorrect cost, which may be used by the system to re-calculate the average cost.

The following table shows us that on 04/29/06, 100 cases were received at a cost of \$4.22 per case instead of \$45.22 per case, resulting in the following costing problems:

Date Received	Cases Received	Cases Sold	Cases Remaining	Cost per Case	Value
04/29/06	100	0	100	\$4.22	\$422.00
04/22/06	100	0	100	\$42.64	\$4,264.00
04/15/06	100	0	100	\$43.96	\$4,396.00
04/08/06	100	0	100	\$46.75	\$4,675.00
04/01/06	100	0	100	\$41.50	\$4,150.00
	500	0	500		\$17,907.00

*Average Cost equals total value of what is in stock divided by the quantity in stock
Average Cost equals \$17,907.00 divided by 500 CS
Average Cost equals \$35.814 per CS*

The average cost of \$35.814 is \$8.20 less than the correct average cost of \$44.014 we found in our calculation on the original average cost calculation on page 2.

Food Connex Inventory Procedures Inventory Adjustments

Cost Adjustment - Receiving Error

continued

To correct this error, the user may think that adjusting out the stock that was received with the incorrect cost, and then receiving it back in with the correct cost will correct the error. It will not, because the incorrect cost still exists in the receiving history for this item, as the following example shows us.

Date Received	Cases Received	Cases Adjusted	Cases Sold	Cases Remaining	Cost per Case	Value
04/29/06	100		0	100	\$45.22	\$4,522.00
04/29/06		-100	n/a	-100	n/a	N/a
04/29/06	100		0	100	\$4.22	\$422.00
04/22/06	100		0	100	\$42.64	\$4,264.00
04/15/06	100		0	100	\$43.96	\$4,396.00
04/08/06	100		0	100	\$46.75	\$4,675.00
04/01/06	100		0	100	\$41.50	n/a
	600	-100	0	500		\$18,279.00

There are 500 cases in stock, so the system looks back through the receipt transactions until it has accumulated 500 cases received, which it hits at the 04/08/06 receipt. It therefore ignores the receipt on 04/01/06 for 100 cases at \$41.50.

*Average Cost equals total value of what is in stock divided by the quantity in stock
Average Cost equals \$1829.00 divided by 500 CS
Average Cost equals \$36.558 per CS*

The average cost of \$36.558 is \$7.456 less than the correct average cost of \$44.014 we found in our calculation on the original average cost calculation on page 2.

If the user had opted to use the **Receiving Error B Cost Adjustment** process, the system would have corrected the 04/29/06 receipt, changing the cost for that receipt from \$4.22 to \$45.22, and the average cost calculation would have been correct, as reflected on page 2.

Food Connex Inventory Procedures Inventory Adjustments

Conclusion

Based on the information presented above, it is obvious how important it is to check your quantities and costs BEFORE you post inventory receipts. Every receipt transaction affects your last cost, your invoice cost, and your average cost, and depending on how you have salesman costs defined, may also affect them.

Although the system will eventually correct itself, you will be processing with bad costs until you find the problem and correct it **using the appropriate adjustment type**, or the transactions become so old that the system no longer considers them when calculating average costs.

However, the costs assigned to orders and invoices during the time period where your costs were wrong will NOT be corrected when you fix your historical inventory receipt quantities and costs. Therefore, there will be an adverse affect on your cost of goods sold in general ledger and the GP percentages and amounts that you see on your sales analysis reports.

If you do have a receiving problem, and are not sure how to fix it, please call the Food Connex support team for direction.

If you are not a Food Connex customer and would like to learn more about Food Connex features and capabilities, please contact our sales team at 1-800-366-3836 ext. 18 for further information.