1. Answer: A – When prices are rising, LIFO will produce the highest cost of goods sold because cost of goods sold will come from the most recent, highest prices.

2. Answer: B – When prices are rising, FIFO will produce the highest gross margin because it produces the lowest cost of goods sold, coming from the oldest, lowest prices.

3. Answer: B – Because FIFO produces the lowest cost of goods sold when prices are rising, it will result in the highest taxable income and highest income tax expense and cash outflow to pay those taxes.

4. Answer: A – When prices are declining, ending inventory will be highest if LIFO is used because the older, higher prices will be assigned to ending inventory.

5. Answer: B – When prices are declining, FIFO will produce the lowest gross margin because older, higher prices will be assigned to cost of goods sold.

6. Answer: B – FIFO is the most frequently used cost flow assumption, making up about 2/3 of companies.

7. Answer: A – LIFO assigns most recent costs to cost of goods sold, so those costs will be closest to current market value.

8. Answer: D – Weighted average cost per unit = [(1 x $50) + (1 x $55) + (2 x $60)]/4 = $56.25; Cost of goods sold = $56.25 x 3 = $168.75. FIFO cost of goods sold = [(1 x $50) + (1 x $55) + (1 x $60)] = $165. LIFO cost of goods sold = [(2 x $60) + (1 x $55)] = $170.

9. Answer: A – There were 55 units available for sale. If 35 were sold, using FIFO, the 20 remaining would have come from the second purchase. 20 x $115 = $2,300.

10. Answer: B – LIFO cost of goods sold = (25 x $115) + (10 x $110) = $3,975; Sales = 35 x $175 = $6,125; $6,125 - $3,975 = $2,150 gross margin

11. Answer: C – Weighted average cost per unit = [(10 x $100) + (20 x $110) + (25 x $115)]/55 units = $110.45; 35 x $110.45 = $3,866

12. Answer: B – When prices are rising, LIFO will produce the highest cost of goods sold; therefore, it will result in the lowest income tax expense.

13. Answer: B – When prices are falling, FIFO will produce the highest cost of goods sold, followed by weighted average, followed by LIFO.

14. Answer: A – Weighted average cost per unit = [(10 x $100) + (20 x $110) + (25 x $115) + (20 x $125)]/75 units = $114.33

15. Answer: C – Weighted average cost per unit = [(100 x $5) + (200 x $5.50) + (250 x $6.50)]/550 = $5.86; $5.86 x 50 = $293 cost of goods sold; 50 units x $10 = $500 sales revenue

16. Answer: A – LIFO cost of goods sold = [(250 x $4.50) + (20 x $3.50)] = $1,195; 270 x $8 = $2,160 sales revenue

17. Answer: D – In a period of declining prices ($160 to $150), FIFO will result in an ending inventory than LIFO. In this case, ending inventory would be $150, the cost of the second unit purchased.

18. Answer: C – Total cost = [(15 x $250) + (10 x $180) + (18 x $160) + (24 x $275)] = $15,030; Total LCM = [(15 x $240) + (10 x $180) + (18 x $160) + (24 x $275)] = $14,880; Write-down = $15,030 - $14,880 = $150; The entry is a debit to cost of goods sold and a credit to inventory.

19. Answer: D – Total cost = [(15 x $250) + (10 x $180) + (18 x $160) + (24 x $275)] = $15,030; Total Market = [(15 x $240) + (10 x $195) + (18 x $160) + (24 x $280)] = $15,150. Because total market is higher than total cost, there is no journal entry necessary.

20. Answer: C – When the lower-of-cost-or-market rule is applied in aggregate, items with market values above cost will offset items with lower market values; therefore, write-downs will general be smaller than if the rule were applied to individual lines of inventory.