

Lower of Cost or Market Example 1

Item	Units	Cost	Current Replacement Cost	Estimated Selling Price	Estimated Completion & Disposal Cost
1	500	\$ 65.00	\$ 68.00	\$ 80.00	\$ 3.00
2	300	\$ 80.00	\$ 72.00	\$ 102.00	\$ 8.00
3	400	\$ 90.00	\$ 105.00	\$ 112.00	\$ 10.00
4	700	\$ 38.00	\$ 42.00	\$ 40.00	\$ 4.00
5	900	\$ 20.00	\$ 21.00	\$ 30.00	\$ 2.00
6	600	\$ 55.00	\$ 45.00	\$ 67.00	\$ 2.00

For all inventory items, Normal Profit Margin is 30% of cost.

Determine the Market

Item	Units	(A) = (C) - (D) Net Realizable Value	(B) = (A) - (E) NRV - Normal Profit Margin	(C) Estimated Selling Price	(D) Estimated Completion & Disposal Cost	(E) Normal Profit Margin (30% of Cost)
1	500	\$ 77.00	\$ 57.50	\$ 80.00	\$ 3.00	\$ 19.50
2	300	\$ 94.00	\$ 70.00	\$ 102.00	\$ 8.00	\$ 24.00
3	400	\$ 102.00	\$ 75.00	\$ 112.00	\$ 10.00	\$ 27.00
4	700	\$ 36.00	\$ 24.60	\$ 40.00	\$ 4.00	\$ 11.40
5	900	\$ 28.00	\$ 22.00	\$ 30.00	\$ 2.00	\$ 6.00
6	600	\$ 65.00	\$ 48.50	\$ 67.00	\$ 2.00	\$ 16.50

Item	(AA) Current Replacement Cost	(BB) Net Realizable Value	(CC) NRV - Normal Profit Margin	Is (AA) in between (BB) and (CC)?	Is (AA) greater than (BB)?	Is (AA) smaller than (CC)?	
1	\$ 68.00	\$ 77.00	\$ 57.50	Yes			(AA) is Market
2	\$ 72.00	\$ 94.00	\$ 70.00	Yes			(AA) is Market
3	\$ 105.00	\$ 102.00	\$ 75.00		Yes		(BB) is Market
4	\$ 42.00	\$ 36.00	\$ 24.60		Yes		(BB) is Market
5	\$ 21.00	\$ 28.00	\$ 22.00			Yes	(CC) is Market
6	\$ 45.00	\$ 65.00	\$ 48.50			Yes	(CC) is Market

Compare Cost and Market

Item	Units	Cost	Market	Lower of Cost or Market (LCM)	Is Cost lower than Market?	Is Market lower than Cost?	
1	500	\$ 65.00	\$ 68.00	\$ 65.00	Yes		Cost is LCM
2	300	\$ 80.00	\$ 72.00	\$ 72.00		Yes	Market is LCM
3	400	\$ 90.00	\$ 102.00	\$ 90.00	Yes		Cost is LCM
4	700	\$ 38.00	\$ 36.00	\$ 36.00		Yes	Market is LCM
5	900	\$ 20.00	\$ 22.00	\$ 20.00	Yes		Cost is LCM
6	600	\$ 55.00	\$ 48.50	\$ 48.50		Yes	Market is LCM

Inventory valuation at Cost, Market and LCM

Item	Units	Inventory at Cost		Inventory at Market		Inventory at LCM
1	500	\$32,500	<	\$34,000		\$32,500
2	300	\$24,000	>	\$21,600		\$21,600
3	400	\$36,000	<	\$40,800		\$36,000
4	700	\$26,600	>	\$25,200		\$25,200
5	900	\$18,000	<	\$19,800		\$18,000
6	600	\$33,000	>	\$29,100		\$29,100
Total		\$170,100	<	\$170,500		\$162,400

LCM applied to each inventory item --> Inventory at LCM = \$162,400

LCM applied to all inventory as one pool

--> Total inventory at cost < Total inventory at market --> Inventory at LCM = \$170,100

Points

Market = Current Replacement Cost

If Current Replacement Cost > Net Realizable Value (NRV), the NRV is Market.

If Current Replacement Cost < (NRV - Normal Profit Margin), then (NRV - Normal Profit Margin) is Market.

Net Realizable Value (NRV) = Estimated Selling Price - Cost of Completion and Disposal

In this example, normal profit margin = 30% of cost.

Rank the following three values, then the one in the middle is Market.

NRV

Current Replacement Cost

NRV - Normal Profit Margin