

### 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)<br>Net Realizable Value | (B) = (A) - (E)<br>NRV - Normal Profit Margin | (C)<br>Estimated Selling Price | (D)<br>Estimated Completion & Disposal Cost | (E)<br>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)<br>Current Replacement Cost | (BB)<br>Net Realizable Value | (CC)<br>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