CHAPTER 9

Inventories: Valuation and Estimation Concepts

TRUE-FALSE—Conceptual

Answer	No.	Description
T	1.	When to use lower-of-cost-or-market.
F	2.	Lower-of-cost-or-market and conservatism.
F	3.	Purpose of the “floor” in LCM.
T	4.	Lower-of-cost-or-market and consistency.
F	5.	Reporting inventory at net realizable value.
T	6.	Valuing inventory at net realizable value.
T	7.	Valuation using relative sales value.
F	8.	Definition of a basket purchase.
F	9.	Recording purchase commitments.
T	10.	Loss on purchase commitments.
F	11.	Recording noncancelable purchase contract.
T	12.	Gross profit method.
F	13.	Gross profit percentage.
T	14.	Disadvantage of gross profit method.
F	15.	Conventional retail method.
F	16.	Definition of markup.
T	17.	Accounting for abnormal shortages.
F	18.	Computing inventory turnover ratio.
T	19.	Average days to sell inventory.
T	20	LIFO retail method.

MULTIPLE CHOICE—Conceptual

Answer	No.	Description
d	21.	Knowledge of lower-of-cost-or-market valuations.
d	22.	Appropriate use of LCM valuation.
c	23.	Definition of "market" under LCM.
b	24.	Definition of "ceiling."
a	25.	Definition of "designated market value."
c	26.	Application of lower-of-cost-or-market valuation.
d	27.	Effect of inventory write-down.
d	[S]28.	Recording inventory loss under direct method.
c	[S]29.	Recording inventory at net realizable value.
b	30.	Net realizable value under LCM.
d	31.	Definition of "net realizable value."
a	32.	Valuation of inventory at net realizable value.
d	33.	Appropriate use of net realizable value.
a	34.	Material purchase commitments.
a	35.	Loss recognition on purchase commitments.
b	[P]36.	Reporting purchase commitments loss.

MULTIPLE CHOICE—Conceptual (cont.)

Answer	No.	Description
d	S37.	Gross profit method assumptions.
d	38.	Appropriate use of the gross profit method.
b	39.	Appropriate use of the gross profit method.
d	40.	Advantage of retail inventory method.
c	41.	Conventional retail inventory method.
a	42.	Assumptions of the retail inventory method.
d	43.	Appropriate use of the retail inventory method.
b	44.	Markdowns and the conventional retail method.
a	45.	Markups and the conventional retail method.
b	*46.	Knowledge of the cost ratio for retail inventory methods.
a	S47.	Information needed in retail inventory method.
d	S48.	Reasons for using retail inventory method.
b	P49.	Inventory cost flow assumptions.
a	P50.	Computing average days to sell inventory.
c	51.	Inventory turnover ratio.
c	*52.	Dollar-value LIFO retail method.

MULTIPLE CHOICE—Computational

Answer	No.	Description
a	53.	Value inventory at LCM.
b	54.	Lower-of-cost-or-market.
b	55.	Lower-of-cost-or-market.
c	56.	Determining net realizable value.
c	57.	Determining net realizable value.
b	58.	Relative sales value method.
b	59.	Relative sales value method.
c	60.	Relative sales method of inventory valuation.
c	61.	Entry for purchase commitment loss.
c	62.	Recognizing loss on purchase commitments.
b	63.	Recognizing loss on purchase commitments.
a	64.	Estimating ending inventory using gross profit method.
a	65.	Estimating ending inventory using gross profit method.
d	66.	Calculate cost of goods sold given a markup on cost.
d	67.	Calculate merchandise purchases given a markup on cost.
a	68.	Calculate total sales from cost information.
a	69.	Markup on cost equivalent to a markup on selling price.
b	70.	Estimate ending inventory using gross profit method.
c	71.	Calculate ending inventory using gross profit method
. b	72.	Calculate ending inventory using gross profit method.
a	73.	Estimate cost of inventory destroyed by fire.
a	74.	Determine items to be included in inventory.
b	75.	Calculate cost of retail ratio to approximate LCM.
b	76.	Calculate ending inventory at retail.
a	77.	Calculate cost to retail ratio approximating LCM.
b	78.	Calculate cost of inventory lost using retail method.
b	*79.	Calculate ending inventory at cost using LIFO retail.
c	*80.	Determine cost to retail ratio using LIFO retail.
a	81.	Calculate ending inventory at retail.

MULTIPLE CHOICE—Computational (cont.)

Answer	No.	Description
a	82.	Calculate ending inventory at retail.
c	83.	Average days to sell inventory.
c	84.	Average days to sell inventory.
b	85.	Calculate inventory turnover ratio.
d	86.	Determine cost to retail ratio to approximate LCM.
d	87.	Calculate ending inventory at retail.
a	88.	Calculate ending inventory using conventional retail.
c	*89.	Determine cost to retail ratio using LIFO cost.
a	*90.	Calculate ending inventory cost using dollar-value LIFO.
b	*91.	Calculate cost of ending inventory using LIFO retail.
a	*92.	Calculate ending inventory cost using dollar-value LIFO.

[P] These questions also appear in the Problem-Solving Survival Guide.
[S] These questions also appear in the Study Guide.
* This topic is dealt with in an Appendix to the chapter.

MULTIPLE CHOICE—CPA Adapted

Answer	No.	Description
d	93.	Recognizing a loss due to LCM.
b	94.	Appropriate use of replacement costs in LCM.
b	95.	Identification of the designated market value.
a	96.	Estimate cost of inventory lost by theft.
a	97.	Determine cost of ending inventory using retail method.
d	98.	Determine cost of ending inventory using retail method.
a	*99.	Calculate ending inventory using LIFO retail.

EXERCISES

Item	Description
E9-100	Lower-of-cost-or-market.
E9-101	Lower-of-cost-or-market.
E9-102	Lower-of-cost-or-market.
E9-103	Lower-of-cost-or-market.
E9-104	Lower-of-cost-or-market.
E9-105	Relative sales value method.
E9-106	Gross profit method.
E9-107	Gross profit method.
E9-108	Gross profit method.
E9-109	Comparison of inventory methods.

PROBLEMS

Item	Description
P9-110	Gross profit method.
P9-111	Retail inventory method.
*P9-112	Retail inventory method.
*P9-113	LIFO retail inventory method, fluctuating prices.
*P9-114	LIFO retail inventory method, stable prices.
*P9-115	Dollar-value LIFO retail method.
*P9-116	Retail LIFO.

CHAPTER LEARNING OBJECTIVES

1. Describe and apply the lower-of-cost-or-market rule.
2. Explain when companies value inventories at net realizable value.
3. Explain when companies use the relative sales value method to value inventories.
4. Discuss accounting issues related to purchase commitments.
5. Determine ending inventory by applying the gross profit method.
6. Determine ending inventory by applying the retail inventory method.
7. Explain how to report and analyze inventory.

*8. Determine ending inventory by applying the LIFO retail methods.

*SUMMARY OF LEARNING OBJECTIVES BY QUESTIONS

Item	Type	Item	Type	Item	Type	Item	Type	Item	Type	Item	Type	Item	Type
Learning Objective 1													
1.	TF	21.	MC	25.	MC	53.	MC	94.	MC	102.	E		
2.	TF	22.	MC	26.	MC	54.	MC	95.	MC	103.	E		
3.	TF	23.	MC	27.	MC	55.	MC	100.	E	104.	E		
4.	TF	24.	MC	[S]28.	MC	93.	MC	101.	E	109.	E		
Learning Objective 2													
5.	TF	[S]29.	MC	31.	MC	33.	MC	57.	MC				
6.	TF	30.	MC	32.	MC	56.	MC						
Learning Objective 3													
7.	TF	8.	TF	58.	MC	59.	MC	60.	MC	105.	E		
Learning Objective 4													
9.	TF	11.	TF	35.	MC	61.	MC	63.	MC				
10.	TF	34.	MC	[P]36.	MC	62.	MC						
Learning Objective 5													
12.	TF	38.	MC	66.	MC	70.	MC	74.	MC	108.	E		
13.	TF	39.	MC	67.	MC	71.	MC	96.	MC	110.	P		
14.	TF	64.	MC	68.	MC	72.	MC	106.	E				
[S]37.	MC	65.	MC	69.	MC	73.	MC	107.	E				
Learning Objective 6													
15.	TF	41.	MC	45.	MC	75.	MC	81.	MC	88.	MC	111.	P
16.	TF	42.	MC	46.	MC	76.	MC	82.	MC	97.	MC		
17.	TF	43.	MC	[S]47.	MC	77.	MC	86.	MC	98.	MC		
40.	MC	44.	MC	[S]48.	MC	78.	MC	87.	MC	109.	E		
Learning Objective 7													
18.	TF	[P]49.	MC	51.	MC	84.	MC						
19.	TF	[P]50.	MC	83.	MC	85.	MC						
Learning Objective *8													
20.	TF	79.	MC	90.	MC	99.	MC	113.	P	116.	P		
46.	MC	80.	MC	91.	MC	109.	E	114.	P				
52.	MC	89.	MC	92.	MC	112.	P	115.	P				

Note: TF = True-False
MC = Multiple Choice
E = Exercise
P = Problem

TRUE-FALSE—Conceptual

1. A company should abandon the historical cost principle when the future utility of the inventory item falls below its original cost.

2. The lower-of-cost-or-market method is used for inventory despite being less conservative than valuing inventory at market value.

3. The purpose of the “floor” in lower-of-cost-or-market considerations is to avoid overstating inventory.

4. Application of the lower-of-cost-or-market rule results in inconsistency because a company may value inventory at cost in one year and at market in the next year.

5. GAAP requires reporting inventory at net realizable value, even if above cost, whenever there is a controlled market with a quoted price applicable to all quantities.

6. A reason for valuing inventory at net realizable value is that sometimes it is too difficult to obtain the cost figures.

7. In a basket purchase, the cost of the individual assets acquired is determined on the basis of their relative sales value.

8. A basket purchase occurs when a company agrees to buy inventory weeks or months in advance.

9. Most purchase commitments must be recorded as a liability.

10. If the contract price on a noncancelable purchase commitment exceeds the market price, the buyer should record any expected losses on the commitment in the period in which the market decline takes place.

11. When a buyer enters into a formal, noncancelable purchase contract, an asset and a liability are recorded at the inception of the contract.

12. The gross profit method can be used to approximate the dollar amount of inventory on hand.

13. In most situations, the gross profit percentage is stated as a percentage of cost.

14. A disadvantage of the gross profit method is that it uses past percentages in determining the markup.

15. When the conventional retail method includes both net markups and net markdowns in the cost-to-retail ratio, it approximates a lower-of-cost-or-market valuation.

16. In the retail inventory method, the term markup means a markup on the original cost of an inventory item.

17. In the retail inventory method, abnormal shortages are deducted from both the cost and retail amounts and reported as a loss.
18. The inventory turnover ratio is computed by dividing the cost of goods sold by the ending inventory on hand.

19. The average days to sell inventory represents the average number of days' sales for which a company has inventory on hand.

*20. The LIFO retail method assumes that markups and markdowns apply only to the goods purchased during the period.

True False Answers—Conceptual

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
1.	T	6.	T	11.	F	16.	F
2.	F	7.	T	12.	T	17.	T
3.	F	8.	F	13.	F	18.	F
4.	T	9.	F	14.	T	19.	T
5.	F	10.	T	15.	F	20.	T

MULTIPLE CHOICE—Conceptual

21. Which of the following is true about lower-of-cost-or-market?
    a. It is inconsistent because losses are recognized but not gains.
    b. It usually understates assets.
    c. It can increase future income.
    d. All of these.

22. The primary basis of accounting for inventories is cost. A departure from the cost basis of pricing the inventory is required where there is evidence that when the goods are sold in the ordinary course of business their
    a. selling price will be less than their replacement cost.
    b. replacement cost will be more than their net realizable value.
    c. cost will be less than their replacement cost.
    d. future utility will be less than their cost.

23. When valuing raw materials inventory at lower-of-cost-or-market, what is the meaning of the term "market"?
    a. Net realizable value
    b. Net realizable value less a normal profit margin
    c. Current replacement cost
    d. Discounted present value

24. In no case can "market" in the lower-of-cost-or-market rule be more than
    a. estimated selling price in the ordinary course of business.
    b. estimated selling price in the ordinary course of business less reasonably predictable costs of completion and disposal.
    c. estimated selling price in the ordinary course of business less reasonably predictable costs of completion and disposal and an allowance for an approximately normal profit margin.
    d. estimated selling price in the ordinary course of business less reasonably predictable costs of completion and disposal, an allowance for an approximately normal profit margin, and an adequate reserve for possible future losses.

25. Designated market value
    a. is always the middle value of replacement cost, net realizable value, and net realizable value less a normal profit margin.

b. should always be equal to net realizable value.
c. may sometimes exceed net realizable value.
d. should always be equal to net realizable value less a normal profit margin.

26. Lower-of-cost-or-market
a. is most conservative if applied to the total inventory.
b. is most conservative if applied to major categories of inventory.
c. is most conservative if applied to individual items of inventory.
d. must be applied to major categories for taxes.

27. An item of inventory purchased this period for $15.00 has been incorrectly written down to its current replacement cost of $10.00. It sells during the following period for $30.00, its normal selling price, with disposal costs of $3.00 and normal profit of $12.00. Which of the following statements is *not* true?
a. The cost of sales of the following year will be understated.
b. The current year's income is understated.
c. The closing inventory of the current year is understated.
d. Income of the following year will be understated.

S28. When the direct method is used to record inventory at market
a. there is a direct reduction in the selling price of the product that results in a loss being recorded on the income statement prior to the sale.
b. a loss is recorded directly in the inventory account by crediting inventory and debiting loss on inventory decline.
c. only the portion of the loss attributable to inventory sold during the period is recorded in the financial statements.
d. the market value figure for ending inventory is substituted for cost and the loss is buried in cost of goods sold.

S29. Recording inventory at net realizable value is permitted, even if it is above cost, when there are no significant costs of disposal involved and
a. the ending inventory is determined by a physical inventory count.
b. a normal profit is not anticipated.
c. there is a controlled market with a quoted price applicable to all quantities.
d. the internal revenue service is assured that the practice is not used only to distort reported net income.

30. When inventory declines in value below original (historical) cost, and this decline is considered other than temporary, what is the maximum amount that the inventory can be valued at?
a. Sales price
b. Net realizable value
c. Historical cost
d. Net realizable value reduced by a normal profit margin

31. Net realizable value is
    a. acquisition cost plus costs to complete and sell.
    b. selling price.
    c. selling price plus costs to complete and sell.
    d. selling price less costs to complete and sell.

32. If a unit of inventory has declined in value below original cost, but the market value exceeds net realizable value, the amount to be used for purposes of inventory valuation is
    a. net realizable value.
    b. original cost.
    c. market value.
    d. net realizable value less a normal profit margin.

33. Inventory may be recorded at net realizable value if
    a. there is a controlled market with a quoted price.
    b. there are no significant costs of disposal.
    c. the inventory consists of precious metals or agricultural products.
    d. all of these.

34. If a material amount of inventory has been ordered through a formal purchase contract at the balance sheet date for future delivery at firm prices,
    a. this fact must be disclosed.
    b. disclosure is required only if prices have declined since the date of the order.
    c. disclosure is required only if prices have since risen substantially.
    d. an appropriation of retained earnings is necessary.

35. The credit balance that arises when a net loss on a purchase commitment is recognized should be
    a. presented as a current liability.
    b. subtracted from ending inventory.
    c. presented as an appropriation of retained earnings.
    d. presented in the income statement.

P36. In 2006, Lucas Manufacturing signed a contract with a supplier to purchase raw materials in 2007 for $700,000. Before the December 31, 2006 balance sheet date, the market price for these materials dropped to $510,000. The journal entry to record this situation at December 31, 2006 will result in a credit that should be reported
    a. as a valuation account to Inventory on the balance sheet.
    b. as a current liability.
    c. as an appropriation of retained earnings.
    d. on the income statement.

S37. Which of the following is not a basic assumption of the gross profit method?
    a. The beginning inventory plus the purchases equal total goods to be accounted for.
    b. Goods not sold must be on hand.
    c. If the sales, reduced to the cost basis, are deducted from the sum of the opening inventory plus purchases, the result is the amount of inventory on hand.
    d. The total amount of purchases and the total amount of sales remain relatively unchanged from the comparable previous period.

38. The gross profit method of inventory valuation is *invalid* when
    a. a portion of the inventory is destroyed.
    b. there is a substantial increase in inventory during the year.
    c. there is no beginning inventory because it is the first year of operation.
    d. none of these.

39. Which statement is *not* true about the gross profit method of inventory valuation?
    a. It may be used to estimate inventories for interim statements.
    b. It may be used to estimate inventories for annual statements.
    c. It may be used by auditors.
    d. None of these.

40. A major advantage of the retail inventory method is that it
    a. provides reliable results in cases where the distribution of items in the inventory is different from that of items sold during the period.
    b. hides costs from competitors and customers.
    c. gives a more accurate statement of inventory costs than other methods.
    d. provides a method for inventory control and facilitates determination of the periodic inventory for certain types of companies.

41. An inventory method which is designed to approximate inventory valuation at the lower of cost or market is
    a. last-in, first-out.
    b. first-in, first-out.
    c. conventional retail method.
    d. specific identification.

42. The retail inventory method is based on the assumption that the
    a. final inventory and the total of goods available for sale contain the same proportion of high-cost and low-cost ratio goods.
    b. ratio of gross margin to sales is approximately the same each period.
    c. ratio of cost to retail changes at a constant rate.
    d. proportions of markups and markdowns to selling price are the same.

43. Which statement is true about the retail inventory method?
    a. It may not be used to estimate inventories for interim statements.
    b. It may not be used to estimate inventories for annual statements.
    c. It may not be used by auditors.
    d. None of these.

44. When the conventional retail inventory method is used, markdowns are commonly ignored in the computation of the cost to retail ratio because
    a. there may be no markdowns in a given year.
    b. this tends to give a better approximation of the lower of cost or market.
    c. markups are also ignored.
    d. this tends to result in the showing of a normal profit margin in a period when no markdown goods have been sold.

45. To produce an inventory valuation which approximates the lower of cost or market using the conventional retail inventory method, the computation of the ratio of cost to retail should
   a. include markups but not markdowns.
   b. include markups and markdowns.
   c. ignore both markups and markdowns.
   d. include markdowns but not markups.

*46. When calculating the cost ratio for the retail inventory method,
   a. if it is the conventional method, the beginning inventory is included and markdowns are deducted.
   b. if it is the LIFO method, the beginning inventory is excluded and markdowns are deducted.
   c. if it is the LIFO method, the beginning inventory is included and markdowns are not deducted.
   d. if it is the conventional method, the beginning inventory is excluded and markdowns are not deducted.

S47. Which of the following is not required when using the retail inventory method?
   a. All inventory items must be categorized according to the retail markup percentage which reflects the item's selling price.
   b. A record of the total cost and retail value of goods purchased.
   c. A record of the total cost and retail value of the goods available for sale.
   d. Total sales for the period.

S48. Which of the following is not a reason the retail inventory method is used widely?
   a. As a control measure in determining inventory shortages
   b. For insurance information
   c. To permit the computation of net income without a physical count of inventory
   d. To defer income tax liability

P49. Which of the following statements is false regarding an assumption of inventory cost flow?
   a. The cost flow assumption need not correspond to the actual physical flow of goods.
   b. The assumption selected may be changed each accounting period.
   c. The FIFO assumption uses the earliest acquired prices to cost the items sold during a period.
   d. The LIFO assumption uses the earliest acquired prices to cost the items on hand at the end of an accounting period.

P50. The average days to sell inventory is computed by dividing
   a. 365 days by the inventory turnover ratio.
   b. the inventory turnover ratio by 365 days.
   c. net sales by the inventory turnover ratio.
   d. 365 days by cost of goods sold.

51. The inventory turnover ratio is computed by dividing the cost of goods sold by
   a. beginning inventory.
   b. ending inventory.
   c. average inventory.
   d. number of days in the year.

*52. When using dollar-value LIFO, if the incremental layer was added last year, it should be multiplied by

a. last year's cost ratio and this year's index.
b. this year's cost ratio and this year's index.
c. last year's cost ratio and last year's index.
d. this year's cost ratio and last year's index.

Multiple Choice Answers—Conceptual

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
21.	d	26.	c	31.	d	36.	b	41.	c	*46.	b	51.	c
22.	d	27.	d	32.	a	37.	d	42.	a	47.	a	*52.	c
23.	c	28.	d	33.	d	38.	d	43.	d	48.	d		
24.	b	29.	c	34.	a	39.	b	44.	b	49.	b		
25.	a	30.	b	35.	a	40.	d	45.	a	50.	a		

Solutions to those Multiple Choice questions for which the answer is "none of these."

38. The gross profit percentage applicable to the goods in ending inventory is different from the percentage applicable to the goods sold during the period.

43. Many answers are possible.

MULTIPLE CHOICE—Computational

53. Marr Corporation has two products in its ending inventory, each accounted for at the lower of cost or market. A profit margin of 30% on selling price is considered normal for each product. Specific data with respect to each product follows:

	Product #1	Product #2
Historical cost	$40.00	$ 70.00
Replacement cost	45.00	54.00
Estimated cost to dispose	10.00	26.00
Estimated selling price	80.00	130.00

In pricing its ending inventory using the lower-of-cost-or-market, what unit values should Marr use for products #1 and #2, respectively?
a. $40.00 and $65.00.
b. $46.00 and $65.00.
c. $46.00 and $60.00.
d. $45.00 and $54.00.

54. Paul Konerko Company sells product 2005WSC for $20 per unit. The cost of one unit of 2005WSC is $18, and the replacement cost is $17. The estimated cost to dispose of a unit is $4, and the normal profit is 40%. At what amount per unit should product 2005WSC be reported, applying lower-of-cost-or-market?
a. $8.
b. $16.
c. $17.
d. $18.

55. Remington Company sells product 1976NLC for $40 per unit. The cost of one unit of 1976NLC is $36, and the replacement cost is $34. The estimated cost to dispose of a unit

is $8, and the normal profit is 40%. At what amount per unit should product 1976NLC be reported, applying lower-of-cost-or-market?
a. $16.
b. $32.
c. $34.
d. $36.

56. Joe Crede Corporation sells its product, a rare metal, in a controlled market with a quoted price applicable to all quantities. The total cost of 5,000 pounds of the metal now held in inventory is $250,000. The total selling price is $600,000, and estimated costs of disposal are $10,000. At what amount should the inventory of 5,000 pounds be reported in the balance sheet?
a. $240,000.
b. $250,000.
c. $590,000.
d. $600,000.

57. Pettengal Corporation sells its product, a rare metal, in a controlled market with a quoted price applicable to all quantities. The total cost of 5,000 pounds of the metal now held in inventory is $150,000. The total selling price is $350,000, and estimated costs of disposal are $5,000. At what amount should the inventory of 5,000 pounds be reported in the balance sheet?
a. $145,000.
b. $150,000.
c. $345,000.
d. $350,000.

58. Jermaine Dye Corporation acquired two inventory items at a lump-sum cost of $50,000. The acquisition included 3,000 units of product LF, and 7,000 units of product 1B. LF normally sells for $15 per unit, and 1B for $5 per unit. If Dye sells 1,000 units of LF, what amount of gross profit should it recognize?
a. $1,875
b. $5,625.
c. $10,000.
d. $11,875.

59. Williamson Corporation acquired two inventory items at a lump-sum cost of $40,000. The acquisition included 3,000 units of product CF, and 7,000 units of product 3B. CF normally sells for $12 per unit, and 3B for $4 per unit. If Williamson sells 1,000 units of CF, what amount of gross profit should it recognize?
a. $1,500.
b. $4,500.
c. $8,000.
d. $9,500.

60. At a lump-sum cost of $48,000, Sealy Company recently purchased the following items for resale:

Item	No. of Items Purchased	Resale Price Per Unit
M	4,000	$2.50
N	2,000	8.00
O	6,000	4.00

The appropriate cost per unit of inventory is:

	M	N	O
a.	$2.50	$8.00	$4.00
b.	$2.07	$13.24	$2.21
c.	$2.40	$7.68	$3.84
d.	$4.00	$4.00	$4.00

61. During 2006, Reese Co., a manufacturer of chocolate candies, contracted to purchase 100,000 pounds of cocoa beans at $4.00 per pound, delivery to be made in the spring of 2007. Because a record harvest is predicted for 2007, the price per pound for cocoa beans had fallen to $3.10 by December 31, 2006.

Of the following journal entries, the one which would properly reflect in 2006 the effect of the commitment of Reese Co. to purchase the 100,000 pounds of cocoa is

		Debit	Credit
a.	Cocoa Inventory	400,000	
	Accounts Payable		400,000
b.	Cocoa Inventory	310,000	
	Loss on Purchase Commitments	90,000	
	Accounts Payable		400,000
c.	Estimated Loss on Purchase Commitments	90,000	
	Estimated Liability on Purchase Commitments		90,000

d. No entry would be necessary in 2006

62. AJ Corporation, a manufacturer of ethnic foods, contracted in 2007 to purchase 500 pounds of a spice mixture at $5.00 per pound, delivery to be made in spring of 2008. By 12/31/07, the price per pound of the spice mixture had risen to $5.60 per pound. In 2007, AJ should recognize
   a. a loss of $2,500.
   b. a loss of $300.
   c. no gain or loss.
   d. a gain of $300.

63. DT Corporation, a manufacturer of Mexican foods, contracted in 2007 to purchase 1,000 pounds of a spice mixture at $5.00 per pound, delivery to be made in spring of 2008. By 12/31/07, the price per pound of the spice mixture had dropped to $4.60 per pound. In 2007, DT should recognize
   a a loss of $5,000.
   b. a loss of $400.
   c. no gain or loss.
   d. a gain of $400.