**C7-6** **Interpretation of GAAP and Ethical Issues**
**LO 7.6**

Robin Smith is considering buying shares in Mah Company. The company has reported an increase in net income this year. On careful reading of the notes to the financial statements, Robin learns that the company had a LIFO liquidation this year. Robin understands what caused the liquidation but has asked you for advice about how to interpret it.

**Required:**
1. Prepare a short memo to Robin to answer the question.
2. Could a LIFO liquidation profit create ethical issues?

**C7-7** **Selection of an Inventory Method and Ethical Issues**
**LO 7.6**
**LO 7.8**

Kelly Company uses FIFO. It has experienced rising costs for the last 5 years and expects that trend to continue. King Company increased the number of LIFO pools it uses to account for its inventory.

**Required:**
1. Explain why you think each company follows its policy.
2. Does either practice create ethical issues?

**C7-8** **Analyzing Starbucks's Inventory Disclosures**

Obtain **Starbucks's 2015** annual report either using the "Investor Relations" portion of its web site (do a Web search for Starbucks investor relations) or go to http://www.sec.gov and click "Search for company filings" under "Filings and Forms (EDGAR)."

**Required:**
1. What is the primary cost flow assumption that Starbucks uses? Discuss how the amounts reported under this assumption compare to amounts reported under alternative cost flow assumptions. Explain why you think Starbucks selected this method.
2. What type of inventory system—perpetual or periodic—do you think Starbucks uses?
3. Does Starbucks have any purchase commitments? If so, are they included in inventory?
4. Assume ending inventory for 2013 was \$1,111.2 million. Compute the inventory turnover ratio for 2015 and 2014. What is your evaluation of the difference? (Round your answer to two decimal places).
5. Recreate summary journal entries to record the transactions that affected inventory during 2015. (Assume all inventory purchases were on account.)

**C7-9** **Analyzing Nestlé's Cash and Receivables Disclosures**

Obtain **Nestlé**'s 2013 annual report using the "Investor Relations" portion of its web site (do a Web search for Nestlé investor relations).

**Required:**
1. Which inventory method does Nestlé use? Why doesn't Nestlé use LIFO?
2. Describe the composition of Nestlé's inventory.
3. Assume Nestlé's 2011 ending inventory was CHF 9,255 million. Compute the inventory turnover for 2013 and 2012. What is your evaluation of the difference? (Round your answer to two decimal places).

## USING CODIFICATION

**C7-10** **Researching GAAP**

**Situation**

To pump up sales of all brands, Chapman Inc. is moving aggressively to ship extra cases of inventory into distributors' warehouses and record them as sales, a practice generally known as "trade loading." (Adapted from *Fortune*, April 6, 1992.) Chapman's president has asked you whether these shipments may be recognized as revenue.

**Directions**

Research the related generally accepted accounting principles and prepare a short memo to the president. Cite your references and applicable paragraph numbers.

**C7-11** **Researching GAAP**

**Situation**

Fenimore Manufacturing Company uses the average cost method. It has followed a policy of expensing all its manufacturing cost variances. It is considering a change in its policy that will involve allocating them between cost of goods sold and inventory. Fenimore's president has asked you which of these alternative policies is consistent with GAAP.

**Directions**

Research the related generally accepted accounting principles and prepare a short memo to the president. Cite your references and applicable paragraph numbers.