

Tutorial 7 (Week 8): Understanding FS – Inventories

- (a) What types of inventories does SBS Transit hold, and what costing method does it use in determining the cost of inventories? For the year 2024, how much inventory expense did SBS Transit record in its Income Statement, and under what type of expense classification was it reported?
- (b) Assume that at the start of 2024, SBS Transit had 6,250 units of spare part Z in beginning inventory valued at \$10 million. During the year, the company made monthly purchases of 500 units (total 6,000 units). Purchase prices of spare part Z had declined steadily over the year, and by the year end they were about 30% lower than at the beginning of the year. During 2024, 5,700 units of spare part Z were consumed.
- (i) Assuming SBS Transit is on the *periodic* inventory system, estimate and compare the effect on ending inventory and reported profit under (1) FIFO, and (2) weighted average cost.
- (ii) Assuming SBS Transit is on the *perpetual* inventory system, estimate and compare the effect on ending inventory and reported profit under (1) FIFO, and (2) weighted average cost.

Clearly state all assumptions you make.

- (c) Did SBS Transit record a write down of inventories due to obsolescence in the year 2024? If so, what journal entry would SBS Transit have recorded for the write-down? How does SBS Transit determine inventory obsolescence?
- (d) If you are an auditor reviewing SBS Transit's inventory obsolescence allowance, what types of evidence would you request to assess whether the allowance is reasonable? If you suspect management has overstated the allowance, what possible motives might they have for doing so, and how would it affect reported profits?

~ End of Tutorial 7 ~