#1-191A

EASY INTERMEDIATE HARD

CFA® SAMPLE QUESTION – LEVEL I

Financial Reporting and Analysis

Q: Under U.S. GAAP, when accounting for inventory, are the first-in, first-out (FIFO) and last-in, first-out (LIFO) cost flow assumptions permitted?

CORRECT ANSWER:

	FIFO	LIFO
ⓐ	Yes	Yes

LIFO and FIFO are both permitted under U.S. GAAP. **However LIFO is prohibited under IFRS**.

The Last-In-First-Out (LIFO) method of inventory valuation, while permitted under the US Generally Accepted Accounting Principles (GAAP), is prohibited under the International Financial Reporting Standards (IFRS).

As IFRS rules are based on principles rather than exact guidelines, usage of LIFO is prohibited due to potential distortions it may have on a company's profitability and financial statements.

In principle, LIFO may create a distortion to net income when prices are rising (inflation), LIFO inventory amounts are based on outdated and obsolete numbers, and LIFO liquidations may provide unscrupulous managers with the means to artificially inflate earnings.

CFA Society Hong Kong Candidate Services

Mr. Zap Cheng, CFA
Candidate Services Committee

Date of issue:
1 Jan 2024