

Inventory and Cost of Goods Sold

You are the accounting manager of a specialty electronics retailer. The company uses AI to assist with inventory valuation and financial reporting. As manager, you must review AI outputs for accuracy. The following is an exchange between you (manager) and AI.

Manager: The following table shows inventory purchases and per unit costs for December. This is the company's first month of operation, and it had no beginning inventory. Considering the trend of falling per-unit cost of inventory purchases, which inventory costing method results in the lowest reported income and the lowest taxes?

Date	Units Purchased	Cost per Unit
December 5	200 units	\$12
December 12	220 units	\$11
December 21	180 units	\$10

AI Chatbot: During a period of falling costs, the Weighted Average method typically smooths out price fluctuations and may produce lower net income and lower tax expense as compared to FIFO and LIFO. Therefore, the Weighted Average method is the inventory costing method that results in the lowest reported income and lowest taxes.

Question 1

We discover a hallucination in the AI response. How do we correct it?

- The LIFO method should be identified as resulting in the lowest reported income and lowest taxes.
- The FIFO method should be identified as resulting in the lowest reported income and lowest taxes.
- Inventory costs should be described as increasing during the month of December.
- There is no error (hallucination) in the AI response.

Question 2

Which method would result in the lowest reported income when costs are *decreasing*?