

Chapter 01 Test Bank – Static Key

Multiple Choice Questions

1. The firm's information system:

- A. is always a single integrated system
- B. includes only financial information
- C. may include other information such as customer satisfaction surveys, in addition to financial information**
- D. is less important as a firm grows in size
- E. none of the above

The firm's information system includes many kinds of financial and non-financial information.

AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Leveraging Technology
Blooms: Remember
Difficulty: 1 Easy
Topic: Managerial Accounting: Decision Making and Control

2. Identify all the correct statements:

- A. Managers naturally seek to maximize shareholders' wealth
- B. Managers act in their own interests, and so there is no way to align their interests with those of the owners
- C. To motivate managers in non-profit firms, no employee incentives are needed
- D. To align the interests of managers and owners, owners must design systems to monitor and reward management behavior that increases the firm's profits**
- E. none of the above

To minimize conflicts between the economic interests of managers and owners, the owners need both systems to monitor the manager's performance and systems of rewards or incentives.

AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Decision Making
AICPA: FN Risk Analysis
Blooms: Remember
Difficulty: 1 Easy
Topic: Management Accountant's Role in the Organization
Topic: Managerial Accounting: Decision Making and Control

3. An internal accounting system should:

- A. provide information to enable costs to be minimized
- B. provide financial accounting data for external reporting purposes
- C. provide management accounting information for decision-making
- D. provide data for tax purposes
- E.** all of the above

A well designed internal accounting system should provide data for external purposes, such as financial reporting and tax, as well as internal purposes such as cost control, assessing performance and determining rewards. It is economically inefficient to maintain multiple accounting systems.

AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Remember
Difficulty: 1 Easy
Topic: Design and Use of Cost Systems

4. Economic Darwinism:

- A. explains why firms persist in inefficient behavior
- B.** explains why some inefficient accounting practices persist
- C. explains why marmots eat bears
- D. explains why bears eat marmots
- E. none of the above

Inefficient accounting systems may continue to exist either because they have proved better than other systems or because better systems have not been yet discovered.

AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Marketing
AICPA: FN Risk Analysis
Blooms: Remember
Difficulty: 1 Easy
Topic: Marmots and Grizzly Bears

5. Management accountants mainly are:

- A. Internal consultants
- B. Scorekeepers
- C. Focused on calculating product costs
- D. Corporate cops
- E. Internal consultants and corporate cops.**

While score-keeping and product costing are tasks performed by today's management accountants, these usually are considered minor. The major roles they perform are internal consultant in terms of providing information to aid other's decision making and corporate cop in terms of providing control systems to prevent fraud and performance measures for incentive systems.

AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Understand
Difficulty: 2 Medium
Topic: Management Accountant's Role in the Organization

6. Internal control systems:

- A. are the responsibility of the external auditor
- B. include anti-fraud measures**
- C. are designed to allow financial misrepresentation
- D. require that one person perform all aspects of a task
- E. all of the above

The internal control system is designed to safeguard assets, protect the integrity of the accounting information system, and to prevent fraud. A key practice is the separation of duties to ensure that critical tasks are performed by two or more people.

AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Understand
Difficulty: 2 Medium
Topic: Management Accountant's Role in the Organization

7. Performance measures:

- A. are critical in designing a reward system
- B. are unimportant in designing a reward system
- C. always influence people to achieve them
- D. are always worded vaguely
- E. are not needed to provide incentives because employees always want to do the right thing

Performance measures are critical in designing a reward system. If poorly specified, they may promote dysfunctional behavior or encourage managers to undertake actions not in the best interest of the organization. If managers' performance is not measured and not rewarded, it is unlikely that managers will focus on enhancing the owner's wealth.

AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Understand
Difficulty: 2 Medium
Topic: Evolution of Management Accounting: A Framework for Change

8. Micro Enterprises has the capacity to produce 10,000 widgets a month, and currently makes and sells 9,000 widgets a month. Widgets normally sell for \$6 each, and cost an average of \$5 to make, including fixed costs. The monthly fixed costs are \$18,000. Coyote Corp. has offered to buy 1,000 widgets at \$4 each.

What is the "cost" per unit in the context of evaluating the offer from Coyote Corp.?

- A. \$2
- B. \$3
- C. \$4
- D. \$5
- E. \$6

The "cost" per unit in this case is the variable cost that must be covered. Since Micro has excess capacity, the only cost the firm incurs to produce an additional 1,000 widgets is the variable cost. The average cost of \$5 includes the fixed cost per widgets of \$2 (\$18,000/9000 widgets). Hence, the variable cost per widget is just the average cost of \$5 less the fixed cost per widget of \$2, or \$3.

AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Measurement
Blooms: Apply
Difficulty: 3 Hard
Topic: Vortec Medical Probe Example

9. Micro Enterprises has the capacity to produce 10,000 widgets a month, and currently makes and sells 9,000 widgets a month. Widgets normally sell for \$6 each, and cost an average of \$5 to make, including fixed costs. The monthly fixed costs are \$18,000. Coyote Corp. has offered to buy 1,000 widgets at \$4 each.

On this information alone, should Micro accept the offer?

- A. No, because it will lose \$1 per unit
- B. No, because it will lose \$2 per unit
- C. No, because it will exceed capacity
- D.** Yes, because it makes \$1 per unit in the short run
- E. Unable to determine

The average fixed cost is NOT relevant, as fixed costs will not change in the short run. The offer's contribution margin (sales price \$4 minus variable cost \$3) is positive, and in the absence of other information should be accepted.

*AACSB: Communication
AACSB: Knowledge Application
Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Apply
Difficulty: 3 Hard
Topic: Vortec Medical Probe Example*

10. Micro Enterprises has the capacity to produce 10,000 widgets a month, and currently makes and sells 9,000 widgets a month. Widgets normally sell for \$6 each, and cost an average of \$5 to make, including fixed costs. The monthly fixed costs are \$18,000. Coyote Corp. has offered to buy 1,000 widgets at \$4 each.

What other factors should be taken into consideration?

- A. The impact on the normal selling price of \$6
- B. Will an additional shift be needed to complete the order?
- C. Are future orders from Coyote likely?
- D. Does the special price comply with the Robinson-Patman Act?
- E.** All of the above

All of the factors mentioned are relevant. Answers to A, B and D could have a negative effect on the decision to accept the offer. Future orders from Coyote could be viewed favorably, provided that they do not utilize factory resources devoted to the regular, more profitable, customers.

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Accessibility: Keyboard Navigation
Accessibility: Screen Reader Compatible
AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Understand
Difficulty: 2 Medium
Topic: Vortec Medical Probe Example*

11. Micro Enterprises has the capacity to produce 10,000 widgets a month, and currently makes and sells 9,000 widgets a month. Widgets normally sell for \$6 each, and cost an average of \$5 to make, including fixed costs. The monthly fixed costs are \$18,000. Coyote has offered to buy 1,500 widgets (all or nothing) for \$4 each.

Should the offer be accepted?

- A. No, because it will lose \$1 per unit
- B. No, because the opportunity costs are less than the gains
- C. No, (indifferent or worse) because the opportunity costs equal the gains
- D. Yes, because it makes \$1 per unit in the short run
- E. Unable to determine

At 1500 widgets, Coyote's offer brings in a total of \$1,500 (contribution margin of \$1 per unit $\times$ 1,500 widgets). To accept the order, 500 regular customers must be displaced (9,000 normal + 1500 Coyote widgets exceeds the maximum capacity of 10,000 widgets). Each displaced customer costs the firm \$3 (\$6 normal selling price minus \$3 variable costs), so the firm must give up \$1,500 from the regular customers. At best, the firm is indifferent between the two choices. In practice, the negative impact on existing customers, sacrificed for no financial gain, would lead to a rejection of the offer.

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AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Apply
Difficulty: 3 Hard
Topic: Vortec Medical Probe Example

12. Micro Enterprises has the capacity to produce 10,000 widgets a month, and currently makes and sells 9,000 widgets a month. Widgets normally sell for \$6 each, and cost an average of \$5 to make, including fixed costs. The monthly fixed costs are \$18,000. Coyote has offered to buy 1,500 widgets (all or nothing) for \$4 each. The accountant has determined that the excess production (beyond capacity) can be accommodated in the short term by incurring an incremental (fixed) cost of \$800.

Should Coyote's offer be accepted?

- A. No, because it will lose \$1 per unit
- B. No, because the opportunity costs are less than the gains
- C. Yes, because the contribution from the sale exceeds the incremental costs
- D. Yes, because it makes \$1 per unit in the short run
- E. Unable to determine

At 1500 widgets, Coyote's offer brings in a total of \$1,500 (contribution margin of \$1 per unit $\times$ 1,500 widgets). The contribution from the offer is greater than the incremental fixed cost of \$800 by \$700.

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AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Apply
Difficulty: 3 Hard
Topic: Vortec Medical Probe Example

Essay Questions

13. Accounting and Control

The controller of a small private college is complaining about the amount of work she must do at the beginning of each month. The president of the university requires the controller to submit a monthly report by the fifth day of the following month. The monthly report contains pages of financial data from operations. The controller was heard saying, "Why does the president need all this information? He probably doesn't read half of the report. He's an English professor and probably doesn't know the difference between a cost and a revenue."

Required:

- a. What is the probable role of the monthly report?
- b. What is the controller's responsibility with respect to a president who doesn't know much accounting?

Feedback:

- a. There are two possible roles for the monthly report: facilitating planning decisions and control. Monthly reports provide more timely information than annual reports. With monthly reports the president can identify problem areas more quickly and make corrective actions. The president may also use the monthly reports to evaluate the work of his managers. The monthly reports provide information about how managers are performing.
- b. If the president of the university is unfamiliar with accounting numbers, the controller must adapt the monthly report to make it more comprehensible. The controller may even want to highlight areas in the report that might need attention.

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AICPA: BB Industry
AICPA: FN Decision Making
Blooms: Understand
Difficulty: 2 Medium
Topic: Design and Use of Cost Systems
Topic: Management Accountant's Role in the Organization

14. The Chief Accountant was overheard saying, “Our accounting system is based on GAAP and is geared towards external reporting. We use the same accounting systems for internal decision-making and performance evaluation and control. If the system is good enough for our shareholders and the SEC, it is good enough for our managers.”

Critically evaluate the Chief Accountant’s statement.

Feedback:

No single accounting system can adequately meet the needs of external reporting and internal decision-making and performance evaluation. For instance, while average cost per unit is appropriate to value inventory and determine cost of goods sold under GAAP, it is not useful for decision-making. Average costs tell managers little about how costs will vary with changes in volume. Similarly, while classifying costs into fixed and variable costs is not essential under GAAP, it can provide useful information for decision-making and performance evaluation.

While it is true that a large number of US firms use the same accounting system for internal and external reporting, most firms reclassify, recombine, reorganize, and recalculate data and perform further analyses to provide information to managers that is useful for decision-making and performance evaluation.

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Topic: Design and Use of Cost Systems
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