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QUESTION 1

The term that refers to costs incurred in the past that are not relevant to a future decision is?

- A. Discretionary cost
- B. Full absorption cost.
- C. Underallocated indirect cost.
- D. Sunk cost.

Correct Answer: D

A sunk cost cannot be avoided because it represents an expenditure that has already been made or an irrevocable decision to incur the cost.

QUESTION 2

Several surveys point out that most managers use full product costs, including unit fixed costs and unit variable costs, in developing cost-based pricing. Which one of the following is least associated with cost-based pricing?

- A. Price stability
- B. Price justification.
- C. Target pricing.
- D. Fixed-cost recovery.

Correct Answer: C

A target price is the expected market price of a product, given the company's knowledge of its customers and competitors. Hence, under target pricing, the sales price is known before the product is developed. Subtracting the unit target profit margin determines the long-term unit target cost. If cost-cutting measures do not permit the product to be made at or below the target cost, it will be abandoned.

QUESTION 3

Sensitivity analysis, if used with capital projects,

- A. Is used extensively when cash flows are known with certainty.
- B. Measures the change in the discounted cash flows when using the discounted payback method rather than the net present value method.
- C. Is a "what-if" technique that asks how a given outcome will change if the original estimates of the capital budgeting model are changed.
- D. Is a technique used to rank capital expenditure requests.

Correct Answer: C

After a problem has been formulated into any mathematical model, it may be subjected to sensitivity analysis, which is a trial-and-error method used to determine the sensitivity of the estimates used. For example, forecasts of many calculated NPVs under various assumptions may be compared to determine how sensitive the NPV is to changing conditions. Changing the assumptions about a certain variable or group of variables may drastically alter the NPV, suggesting that the risk of the investment may be excessive.

QUESTION 4

The treasury analyst for Garth Manufacturing has estimated the cash flows for the first half of next year (ignoring any short-term borrowings) as follows: Garth has a line of creditor unto \$4 million on which it pays interest monthly ate rate of 1% of the amount utilized. Garth is expected to have a cash balance of \$2 million on January 1 and no amount utilized on its line of credit. Assuming all cash flows occur at the end of the month, approximately how much will Garth pay in interest during the first half of the year?

	Cash (millions)	
	Inflows	Outflows
January	\$2	\$1
February	2	4
March	2	5
April	2	3
May	4	2
June	5	3

- A. \$0
- B. \$61,000
- C. \$80,000
- D. \$132,000

Correct Answer: B

The sum of the beginning balance and inflows exceeds the outflows for the first 2 months. At the end of March, however, Garth must use \$2,000,000 of its line of credit (\$2,000,000 beginning balance + \$6,000,000 inflows--\$10,000,000 outflows). Thus, interest for April is \$20,000 (\$2,000,000 x 1%). The net cash outflow for April (ignoring short-term borrowings) is \$1,000,000 of an additional \$1,000,000 of the line of credit. However, the \$20,000 of interest for April must also be paid, so the amount of the line of credit used in May is \$3,020,000 (\$2,000,000 + \$1,000,000 + \$20,000). Interest for May is therefore \$30,200 (\$3,020,000 x 1%). Given the net cash inflow for May of \$2,000,000 (again ignoring short-term borrowings) and the borrowing of \$30,200 to pay the interest for May, the amount of the line of credit used in June is \$1,050,200. Interest in June is \$10,502 (\$1,050,200 x 1%), and total interest is \$60,702 (\$20,000 + \$30,200 + \$10,502). Consequently, the closest answer is \$61, 000.

QUESTION 5

The marketing communication mix consists of five types of promotional tools or media. Electronic mail belongs to which class of promotional tools or media?

- A. Direct marketing.
- B. Advertising.
- C. Public relations.
- D. Personal selling.

Correct Answer: A

Direct marketing involves sending a promotional message directly to consumers rather through a mass medium. Some examples are email, voice mail, fax, mail, telemarketing, and home shopping by television.

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