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GNB 12e Practice Exam – Chapter 1

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. For each of the following, indicate whether the description more closely relates to managerial accounting or financial accounting:

	Managerial Accounting	Financial Accounting
Focuses on external uses of information		
Is typically bound by the requirements of GAAP		
Is generally more detailed information produced frequently		
Typically focuses on segments of the organization		
Often uses estimation in order to meet needs for timeliness		
Focuses on the historical performance of the company		
Objectivity and reliability of information foremost		
GAAP not mandatory		
Oriented toward future decision making		
Often mandatory information		
Prepared primarily for internal users		

2. Indicate beside each statement below whether it is True (T) or False (F):
- Informal as well as formal relationships within an organization are usually depicted on an organization chart.
 - ♦ If an organization delegates decision making authority throughout the organization, it is said to be a decentralized organization.
 - Persons who directly make decisions are said to have line positions, while persons indirectly providing support toward the organization's objectives are in staff positions.
 - In today's organizations, the CFO (Chief Financial Officer) is often a key person in top management whose role is considered critical in providing accounting and financial leadership and information for the organization.
 - The CFO may have both the accounting (controller) and the treasury/cash functions reporting to him or her.

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3. For each of the following, indicate whether the description most closely relates to the concepts of Lean Thinking Model (LTM), Six Sigma (SS), or the Theory of Constraints (TOC):

	(LTM)	(SS)	(TOC)
A method one might describe as often trying to improve (rather than remove) "the weakest link"			
Common framework is known as DMAIC, which stands for Define, Measure, Analyze, Improve, and Control			
Five-step management approach that organizes resources around the flow of business processes			
Management approach that emphasizes the importance of managing constraints			
Management of "bottlenecks" which might delay or stop progress			
Minimizes inventories			
Pulls units through the business processes in response to customer orders			
Process improvement method that relies on customer feedback and fact-based data gathering and analysis techniques to drive process improvement			
Strives to continuously pursue perfection in the business process			

4. Indicate beside each statement below whether it is True (T) or False (F):
- _____ It isn't really important that accountants behave ethically since what they do will always be specifically bound by accounting rules such as GAAP.
 - _____ Many accounting professional organizations, such as the IMA and the AICPA have standards of ethical behavior their members should follow.

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- c. _____ Being ethical and making ethical choices is part of the integrity of a person's character, which can be very important to CEOs hiring CFOs.
- d. _____ The IMA Code of Conduct consists of two major parts: general ethical guidelines and specific guidance for unethical situations.

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GNB 12e Practice Exam Solutions – Chapter 1

1. Solution (Learning Objective 1):

	Managerial Accounting	Financial Accounting
Focuses on external uses of information		X
Is typically bound by the requirements of GAAP		X
Is generally more detailed information produced frequently	X	
Typically focuses on segments of the organization	X	
Often uses estimation in order to meet needs for timeliness	X	
Focuses on the historical performance of the company		X
Objectivity and reliability of information foremost		X
GAAP not mandatory	X	
Oriented toward future decision making	X	
Often mandatory information		X
Prepared primarily for internal users	X	

2. Solution (Learning Objective 2):

- False; formal relationships only are typically included.
- False; delegation of authority would be considered a decentralized organization.
- True
- True
- True

Solution (Learning Objective 3):

	(LTM)	(SS)	(TOC)
A method one might describe as often trying to improve (rather than remove) "the weakest link"			X
Common framework is known as DMAIC, which stands for Define, Measure, Analyze, Improve, and Control		X	

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Five-step management approach that organizes resources around the flow of business processes	X		
Management approach that emphasizes the importance of managing constraints			X
Management of "bottlenecks" which might delay or stop progress			X
Minimizes inventories	X		
Pulls units through the business processes in response to customer orders	X		
Process improvement method that relies on customer feedback and fact-based data gathering and analysis techniques to drive process improvement		X	
Strives to continuously pursue perfection in the business process	X		

4. Solution (Learning Objective 4):

- False; accountants are often faced with pressure to ignore or otherwise "bend" the rules and must decide proactively to be ethical in such situations as well as in situations where clear-cut "rules" do not exist and judgment must be exercised heavily.
- True
- True
- True

GNB 12e Practice Exam – Chapter 2

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

- The following data (in thousands of dollars) have been taken from the accounting records of Kovach Corporation for the just completed year.

Raw materials inventory, beginning	\$ 80
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Raw materials inventory, ending	140
Work in process inventory, beginning	140
Work in process inventory, ending	100
Finished goods inventory, beginning	240
Finished goods inventory, ending	320
Administrative expenses	300
Direct labor	400
Manufacturing overhead	460
Purchases of raw materials	240
Sales	1,980
Selling expenses	280

Part (a) What was the cost of the raw materials used in production during the year (in thousands of dollars)?

Part (b) What was the cost of goods manufactured (finished) for the year (in thousands of dollars)?

Part (c) What was the cost of goods sold for the year (in thousands of dollars)?

Part (d) What was the net income for the year (in thousands of dollars)?

2. For each of the following, indicate whether the cost would typically be variable or fixed.

	Variable	Fixed
Direct materials		
Direct labor		
Rent on building		
Supervisor salaries		
Sales commissions based on units sold		

3. For each of the following, indicate whether the cost would typically be considered direct or indirect cost for the cost object given.

	Direct	Indirect
The direct labor factory costs for the manufacturing division.		

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The factory supervisor's salary for the product produced.		
The factory supervisor's salary for the manufacturing division.		
The manufacturing overhead costs for the products produced.		
The manufacturing overhead costs for the manufacturing division.		

4. For each of the following, indicate whether the cost or example would typically be considered an example of a differential cost, an opportunity cost, or a sunk cost.

	Differential Cost	Opportunity Cost	Sunk Cost
The decision to go to graduate school to earn an MBA versus taking a second part-time job. <i>(The foregone profits from the part-time job wages not earned.)</i>			
The cost of accepting a special order from a customer at a reduced selling price due to reduced packaging and delivery services.			
The cost of equipment purchased five years ago which is no longer usable.			
The cost of making a part compared with the cost of buying the part from a supplier.			
The use of factory equipment to produce an item when it could be used to produce another item that sells for a profit. <i>(The foregone profits from the product that is not produced.)</i>			

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GNB 12e Practice Exam Solutions – Chapter 2

1. Part (a) Solution (Learning Objective 4):

The cost of the raw materials used in production during the year is determined as follows:

Raw materials inventory, beginning	\$ 80
Purchases of raw materials	240
Less raw materials inventory, ending	<u>(140)</u>
Raw materials used in production	<u>\$180</u>

Part (b) Solution (Learning Objective 4):

The cost of goods manufactured (finished) during the year is determined as follows:

Raw materials used in production (calculated in the previous question)	\$ 180
Direct labor	400
Manufacturing overhead	<u>460</u>
Total manufacturing costs	1,040
Work in process inventory, beginning	<u>140</u>
	1,180
Less: work in process inventory, ending	<u>(100)</u>
Cost of goods manufactured	<u>\$1,080</u>

Part (c) Solution (Learning Objective 3):

The cost of goods sold for the year is determined as follows:

Finished goods inventory, beginning	\$ 240
Cost of goods manufactured (calculated in the previous question)	1,080
Less finished goods inventory, ending	<u>(320)</u>
Cost of goods sold	<u>\$1,000</u>

Part (d) Solution (Learning Objective 3):

The net income for the year is determined as follows:

Sales		\$1,980
Cost of goods sold (calculated in the previous question)		<u>1,000</u>
Gross profit		980

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Operating expenses:		
Administrative expenses	\$300	
Selling expenses	280	(580)
Net income		\$ 400

2. Solution (Learning Objective 5):

	Variable	Fixed
Direct labor	X	
Direct materials	X	
Rent on building		X
Supervisor salaries		X
Sales commissions based on units sold	X	

3. Solution (Learning Objective 6):

	Direct	Indirect
The direct labor factory costs for the manufacturing division.	X	
The factory supervisor's salary for the product produced.		X
The factory supervisor's salary for the manufacturing division.	X	
The manufacturing overhead costs for the products produced.		X
The manufacturing overhead costs for the manufacturing division.	X	

4. Solution (Learning Objective 7):

	Differential Cost	Opportunity Cost	Sunk Cost
The decision to go to graduate school to earn an MBA versus taking a second part-time job. (The foregone profits from the part-time job wages not earned.)		X	
The cost of accepting a special order from a customer at a reduced	X		

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selling price due to reduced packaging and delivery services.			
The cost of equipment purchased five years ago which is no longer usable.			X
The cost of making a part compared with the cost of buying the part from a supplier.	X		
The use of factory equipment to produce an item when it could be used to produce another item that sells for a profit. (The foregone profits from the product that is not produced.)		X	

GNB 12e Practice Exam – Chapter 3

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. When is job-order costing typically used by a company? How does it differ from process costing? What documents are typically used in a job-order system?
2. Stephens, Inc. had the following estimated costs for next year:

Advertising expense	\$ 88,000
Direct materials	120,000
Direct labor	440,000
Indirect materials	40,000
Rent on factory equipment	128,000
Sales commissions	600,000
Salary of production	280,000

The company estimates that 80,000 direct labor hours will be worked and 64,000 machine hours will be incurred during the year. If overhead is applied on the basis of machine hours, what will be the overhead rate per hour?

3. Scotch Company uses a predetermined overhead rate based on direct labor hours to

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apply manufacturing overhead to jobs. At the beginning of the year, the company estimated manufacturing overhead would be \$400,000 and direct labor hours would be 40,000. The actual figures for the year were \$430,000 for manufacturing overhead and 42,000 direct labor hours. Is manufacturing overhead underapplied or overapplied for the year? By how much?

4. VirtualTech Company's predetermined overhead rate is based on direct labor hours. At the beginning of the current year, the company estimated that its manufacturing overhead would total \$440,000 during the year. During the year, the company incurred \$400,000 in actual manufacturing overhead costs. The Manufacturing Overhead account showed that overhead was underapplied by \$16,000 during the year. If the predetermined overhead rate was \$40.00 per direct labor hour, how many hours were worked during the year?
5. Wagner Company's job-order costing system, manufacturing overhead is applied to Work in Process inventory using a predetermined overhead rate. Wagner had no beginning or ending inventories in April. During April, the company's transactions included the following:

Direct materials issued to production	\$ 720,000
Indirect materials issued to production	64,000
Direct labor cost incurred	856,000
Manufacturing overhead cost applied	904,000
Manufacturing overhead cost incurred	1,000,000

Part (a) What was the cost of goods manufactured for April?

Part (b) What was the amount of cost of goods sold for April?

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GNB 12e Practice Exam Solutions – Chapter 3

1. Solution (Learning Objectives 1 and 2):

A job-order costing system is used in situations where many different products are produced each period. A process costing system is used in situations where the company produces many units for a single product for long periods.

When job-order costing is used, the costs for each job (or production order) are captured and the documents used to record each job's costs typically include a bill of materials, production order, materials requisition form, job cost sheets, and time tickets (or other source of information on the direct and indirect labor related to the job). Manufacturing overhead is allocated to the job using predetermined overhead rates which are entered on the job cost sheet.

2. Solution (Learning Objective 3):

If overhead is applied on the basis of machine hours, the overhead rate per hour would be determined as follows:

Indirect materials	\$ 40,000
Rent on factory equipment	128,000
Salary of production supervisor	<u>280,000</u>
Estimated manufacturing overhead costs	448,000
Estimated machine hours	<u>÷ 64,000</u>
Predetermined overhead rate	<u>\$7.00/MH</u>

Note that direct materials and direct labor are product costs, but are not a part of manufacturing overhead costs, which only include indirect factory costs. Sales commissions and advertising expenses would be considered a part of selling and administrative expenses, and are thus period rather than product costs.

3. Solution (Learning Objectives 3, 5 and 8):

First, calculate the predetermined overhead rate (based on direct labor hours here):

Estimated overhead costs ÷ Estimated direct labor hours = Predetermined rate

\$400,000 ÷ 40,000 direct labor hours = \$10.00/direct labor hour

Then, determine the amount of manufacturing overhead applied during the period:

Predetermined overhead rate x Actual direct labor hours = Overhead applied

\$10.00/direct labor hour x 42,000 direct labor hours = \$420,000

Finally, compare the actual manufacturing overhead costs to the amount applied, and decide whether it is underapplied or overapplied:

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Actual	\$430,000
Applied	<u>420,000</u>
Balance (underapplied)	<u>\$ 10,000</u>

4. Solution (Learning Objectives 5 and 8):

First, determine the amount of overhead applied to production by reference to the information about the Manufacturing Overhead account:

Actual overhead – Amount applied to production = Amount underapplied

\$400,000 – Amount applied to production = \$16,000

Amount applied to production = \$384,000

Then, solve for the direct labor hours here (the activity base for the overhead rate):

Predetermined overhead rate x Direct labor hours = Manufacturing overhead applied

\$40.00 per direct labor hour x Actual direct labor hours = \$384,000 (from above)

Actual direct labor hours = 9,600

5. Solution (Learning Objective 6):

Part (a) The cost of goods manufactured for the month would be determined as follows:

Work in process, beginning of period	\$ 0
Direct materials issued to production	720,000
Direct labor cost incurred	856,000
Manufacturing overhead cost applied	<u>904,000</u>
Total manufacturing costs	2,480,000
Less: work in process, end of period	<u>(0)</u>
Cost of goods manufactured	<u>\$2,480,000</u>

Part (b) First, determine whether overhead was underapplied or overapplied as follows:

Actual overhead costs	\$1,000,000
Overhead costs applied to production	<u>904,000</u>
Amount of underapplied overhead	<u>\$ 96,000</u>

Then, since there are no beginning or ending inventories, the cost of goods sold would be the cost of goods manufactured \$2,480,000 plus the underapplied overhead costs of \$96,000 for a total of \$2,576,000.

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GNB 12e Practice Exam – Chapter 4

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. Golob Company uses the weighted-average method in its process costing system. There is only one processing department. The following data were taken from the company's accounting records. At the beginning of the month, there were no units in the work in process inventory and 150,000 units in the finished goods inventory. The company sold 500,000 units during the month. There were 32,000 units, which were 75% complete as to conversion costs, in the work in process inventory and 120,000 units in the finished goods inventory at the end of the month.

Part (a) How many units were transferred from the processing department to the finished goods department during the month?

Part (b) What were the equivalent units of production for conversion costs for the month?

2. Clarke Company uses the weighted-average method in its process costing system. The following data were taken from the company's accounting records. The company's beginning work in process inventory, which was 100% complete as to materials and 70% complete as to conversion, was comprised of 120,000 units. 360,000 units were started in process during the period. The company's ending work in process inventory, which was 100% complete as to materials and 60% complete as to conversion, was comprised of 80,000 units.

Part (a) How many units were transferred out during the month?

Part (b) What were the equivalent units of production for conversion costs for the month?

3. Hood Company uses the weighted-average method in its process costing system. All materials are added at the beginning of the process. The following information pertains to its third processing department for the current month:

	Number of units	Cost of materials
Beginning work in process	120,000	\$ 40,000
Started during month	320,000	\$108,000
Units completed	340,000	
Ending work in process	100,000	

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Part (a) What were the equivalent units of production for materials for the current month?

Part (b) What is the cost per equivalent unit for materials for the current month?

4. The Carroll Company uses the weighted-average method in its process costing system. The company has only a single processing department. The company's ending work in process inventory consisted of 36,000 units. The units in the ending work in process inventory were 100% complete with respect to materials and 60% complete with respect to labor and overhead. If the cost per equivalent unit for November was \$11.00 for materials and \$17.00 for labor and overhead, what was the total cost assigned to the ending work in process inventory?

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GNB 12e Practice Exam Solutions – Chapter 4

1. Part (a) Solution (Learning Objective 2):

The number of units transferred out during the month would be determined as follows. Account for all units in the finished goods department in order to compute the number of units that were transferred from the processing department to finished goods during the month.

Beginning finished goods inventory	150,000 (given)	Sold (transferred out of finished goods inventory)	500,000 (given)
Started (transferred in from processing dept.)	<u>470,000</u> (C)	Ending inventory	<u>120,000</u> (given)
Total units to be accounted for	<u>620,000</u> (B)	Total units accounted for	<u>620,000</u> (A)

Calculations:

(A) Units sold + Units in ending inventory = Total units accounted for
 $500,000 + 120,000 = 620,000$ (A)

(B) Total units to be accounted for = Total units accounted for
 $620,000 = 620,000$ (from A)

(C) Units in beginning inventory + Units transferred in = Units to be accounted for
 $150,000 + \text{Units transferred in} = 620,000$
Units transferred in from processing department = 470,000 (C)

Part (b) Solution (Learning Objective 2):

The equivalent units of production for conversion costs in the processing department would be determined as follows:

Units completed and transferred out	470,000
Units in ending inventory (32,000 x .75)	<u>24,000</u>
Equivalent units for conversion costs	<u>494,000</u>

2. Part (a) Solution (Learning Objective 2):

The units were transferred out during the month would be determined as follows. First, account for all units in the processing department in order to determine the units in ending inventory (which is required in order to compute the equivalent units).

Beginning inventory	120,000 (given)	Completed (transferred out)	400,000 (C)
Started (transferred in)	<u>360,000</u> (given)	Ending inventory	<u>80,000</u> (given)

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Total units to be accounted for	<u>480,000</u> (A)	Total units accounted for	<u>480,000</u> (B)
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Calculations:

(A) Units in beginning inventory + Units started = Total units to be accounted for
 $120,000 + 360,000 = 480,000$

(B) Units to be accounted for = Total units accounted for
 $480,000 \text{ (from A)} = 480,000 \text{ (B)}$

(C) Units completed + Units in ending inventory = Total units accounted for
 $\text{Units completed} + 80,000 = 480,000$
 $\text{Units completed (and transferred out)} = 400,000 \text{ (C)}$

Part (b) Solution (Learning Objective 2):

The equivalent units of production for conversion costs would be determined as follows.

Units completed and transferred out	400,000
Units in ending inventory (80,000 x .6)	<u>48,000</u>
Equivalent units for conversion costs	<u>448,000</u>

3. Part (a) Solution (Learning Objective 2):

Recall that materials are added at the beginning of the process; as such, the ending inventory would be 100% complete as to materials. The equivalent units of production for materials for the current month would be determined as follows.

Units completed	340,000
Units in ending inventory (100,000 x 100%)	<u>100,000</u>
Equivalent units	<u>440,000</u>

Part (b) Solution (Learning Objective 3):

The cost per equivalent unit for materials for the current month would be determined as follows.

Beginning inventory	\$ 40,000
Started (materials transferred in)	<u>108,000</u>
Total costs	148,000
Divided by equivalent units	<u>440,000</u>
Cost per equivalent unit (rounded)	<u>\$ 0.34</u>

4 Solution (Learning Objective 4):

The total cost assigned to the ending work in process would be determined as follows:

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Materials (36,000 units x 100% x \$11.00 per unit)	\$396,000
Labor and overhead (36,000 units x 60% x \$17.00 per unit)	<u>367,200</u>
Total cost of ending work in process	<u>\$763,200</u>

GNB 12e Practice Exam – Chapter 5

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. The following information has been provided by the Pond, Inc. for the third quarter of the year:

Sales	\$1,400,000
Cost of goods sold	640,000
Fixed administrative expenses	220,000
Variable administrative expenses	60,000
Fixed selling expenses	100,000
Variable selling expense	140,000

What was the company's contribution margin for the quarter?

2. Lexington Company has provided the following data for the fourth quarter of the most recent year:

Sales	1,200,000
Direct labor	\$ 290,000
Direct materials	206,000
Variable manufacturing overhead	164,000
Fixed selling expense	185,000
Fixed administrative expense	178,000
Variable administrative expense	192,000
Fixed manufacturing overhead	22,000
Variable selling expense	199,000

Assume that direct labor is a variable cost and that there were no beginning or ending inventories. What was the company's total contribution margin for the quarter?

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3. An analysis of past janitorial costs indicates that janitorial cost is an average of \$0.80 per machine-hour at an activity level of 80,000 machine-hours and \$1.00 per machine-hour at an activity level of 64,000 machine-hours. Assuming that this activity is within the relevant range, what is the total expected janitorial cost if the activity level is 74,000 machine-hours?
4. The Burlington Company has recorded the following costs for factory utilities at various volumes of production:

Production Volume	Total Factory Utilities Costs
600,000	\$700,000
400,000	500,000
200,000	300,000

Using a scattergraph plot, estimate the cost function for utilities costs.

5. Shipping expense is \$20,000 for 2,000 pounds shipped and \$27,500 for 3,000 pounds shipped. Assuming that this activity is within the relevant range, if the company ships 2,500 pounds, what is its expected shipping expense?

GNB 12e Practice Exam Solutions – Chapter 5

1. Solution (Learning Objective 4):

The company's contribution margin for the quarter would be determined as follows:

Sales		\$1,400,000
Variable expenses:		
Variable selling expense	\$140,000	
Cost of goods sold	640,000	
Variable administrative expenses	<u>60,000</u>	
Total variable expenses		<u>840,000</u>
Contribution margin		<u>\$560,000</u>

2. Solution (Learning Objective 4):

The company's total contribution margin for the quarter would be determined as follows:

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Sales		\$1,200,000
Variable expenses:		
Direct labor	\$ 290,000	
Direct materials	206,000	
Variable administrative expenses	192,000	
Variable manufacturing overhead	164,000	
Variable selling expense	<u>199,000</u>	
Total variable expenses		<u>1,051,000</u>
Contribution margin		<u>\$ 149,000</u>

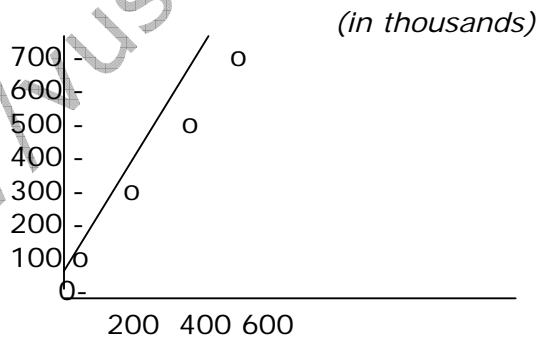
3. Solution (Learning Objective 1):

Janitorial costs are fixed (rather than variable or mixed) in nature; that is, they total \$64,000 at both 80,000 and 64,000 machine hours (MHs) as shown below.

MHs	Average Cost per MH	Total Cost
80,000	\$0.80	\$64,000
64,000	\$1.00	\$64,000

Accordingly, janitorial costs would be expected to be \$64,000 at 74,000 machine hours (or at any other level of machine hours within the relevant range).

4. Solution (Learning Objective 2):



Based on the scattergraph above, the fixed cost portion of utilities cost is equal to the intercept, \$100,000. The variable cost portion appears to be \$1 per unit (that is, for every 200,000 units costs increase \$200,000, so variable costs appear to be \$1 per unit).

5. Solution (Learning Objective 3):

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Using the high-low method, the company's variable cost per unit for shipping costs can be calculated as follows:

Variable cost per unit = Change in costs ÷ Change in units

Variable cost per unit = (\$27,500 – \$20,000) ÷ (3,000 – 2,000)

Variable cost per unit = \$7,500 ÷ 1,000 = \$7.50 per pound shipped.

Then, the company's fixed shipping cost can be calculated as follows:

Total cost = Total variable cost + Total fixed cost or

Total fixed cost = Total cost – Total variable cost

Total fixed cost = \$20,000 – (2,000 pounds x \$7.50 per pound)

Total fixed cost = \$20,000 – \$15,000 = \$5,000

Finally, if the company ships 2,500 pounds, its total shipping cost can be estimated as follows:

Total cost = Total variable cost + Total fixed cost

Total cost = (2,500 pounds x \$7.50 per pound) + \$5,000

Total cost = \$18,750 + \$5,000 = \$23,750

GNB 12e Practice Exam – Chapter 6

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. The following is Shearer Corporation's contribution format income statement for last month:

Sales	\$4,000,000
Less variable expenses	<u>2,800,000</u>
Contribution margin	1,200,000
Less fixed expenses	<u>720,000</u>
Net income	<u>\$ 480,000</u>

A total of 80,000 units were produced and sold last month. The company has no beginning or ending inventories.

Part (a) What is the company's breakeven in sales dollars?

Part (b) How many units would the company have to sell to attain target profits of \$600,000?

Part (c) What is the company's margin of safety?

Part (d) What is the company's degree of operating leverage?

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2. Morris Company sells a single product. The product has a selling price of \$100 per unit and variable expenses of 80% of sales. If the company's fixed expenses total \$150,000 per year, what is its break-even point? (Give answer in dollars and in units.)

3. Garrett Company sells hand-crafted furniture. One item it sells is a small table that sells for \$30 per unit. The variable costs related to the table, including product and shipping costs, are \$18 per unit. Total fixed costs for the company are \$60,000. Assume the tables are the only product the company sells this year and draw a CVP graph to represent the company's sales and expenses. From this graph, compute the approximate breakeven point in dollars and units.

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GNB 12e Practice Exam Solutions – Chapter 6

1. Part (a) Solution (Learning Objectives 1 and 5):

Determine the contribution margin (CM) per unit as follows:

Total contribution margin \div Number of units sold = CM per unit

$\$1,200,000 \div 80,000 \text{ units} = \15 per unit

So, breakeven in sales dollars are the fixed expenses (\$720,000) divided by the 30% contribution margin percentage (\$1,200,000 divided by \$4,000,000, which equals 30%), or a breakeven of \$2,400,000.

Part (b) Solution (Learning Objective 6):

Calculate the unit sales required to achieve the targeted profit as follows:

(Fixed expenses + Targeted profit) \div CM per unit = Required units

$(\$720,000 + \$600,000) \div \$15 \text{ per unit} = \$1,320,000 \div \$15 = 88,000 \text{ units}$

Part (c) Solution (Learning Objective 7):

Note that breakeven sales are \$2,400,000 (see part (a) above).

Margin of safety = Total sales – Breakeven sales

Margin of safety = \$4,000,000 - \$2,400,000 = \$1,600,000

Part (d) Solution (Learning Objective 8):

Degree of operating leverage = Contribution margin \div Net income

Degree of operating leverage = $\$1,200,000 \div \$480,000 = 2.5$

2. Solution (Learning Objectives 1 and 5):

The contribution margin (CM) percentage may be calculated as:

Sales percentage (100%) – Variable expenses percentage equals CM percentage

$100\% - 80\% = 20\%$

Then, the break-even point may be calculated as:

Fixed costs divided by CM percentage equals break-even point (in sales dollars)

$\$150,000 \div 20\% = \$750,000$.

In units, divide contribution margin per unit (\$20) into fixed costs (\$150,000) for breakeven in units of 7,500.

This also could be computed as breakeven in dollars (\$750,000) divided by sales price of \$100, which equals 7,500 units.

3. Solution (Learning Objective 1):

On a CVP graph, the vertical axis is typically dollars, and the horizontal axis shows

number of units. One line is drawn to represent fixed expenses (a flat line since fixed

costs do not increase as volume increases.) Another line is drawn to represent the

revenues (number of units times the selling price per unit) and another line is drawn to

represent expenses (number of units times the variable expenses per unit, plus total

fixed expenses). The amount of fixed expenses will be shown as the intercept on the

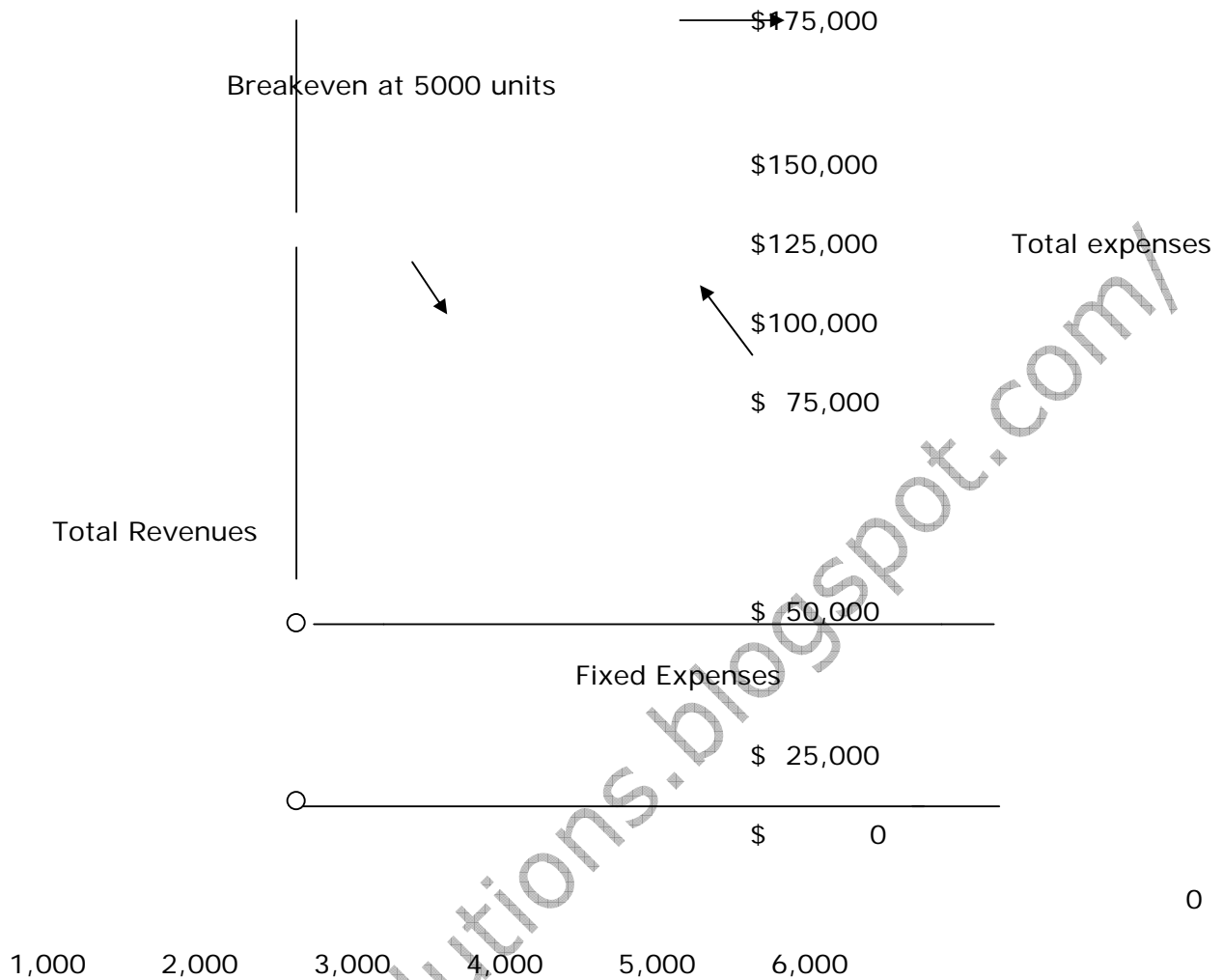
vertical axis. Thus, with a sales price of \$30/unit, variable costs of \$18/unit, and fixed

costs of \$60,000, the CVP graph would appear as follows:



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GNB 12e Practice Exam – Chapter 7

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. Piscopo Company produces mint chocolate candies. The chocolates sell for \$12 per box. During its first year of operations, the company produced 10,000 boxes of chocolates and sold 9,000 boxes of the candies. The company's cost information includes the following:

Direct materials	\$ 2.00 per unit
Direct labor	\$ 3.00 per unit
Fixed manufacturing overhead	\$20,000
Fixed selling and administrative expenses	\$ 5,000
Variable manufacturing overhead	\$ 1.00 pr unit
Variable selling and administrative expenses	\$ 3.00 per unit

Part (a) Compute the unit product cost under absorption costing.

Part (b) Compute the unit product cost under variable costing.

Part (c) Prepare an income statement using absorption costing.

Part (d) Prepare an income statement using variable costing.

Part (e) Explain the difference of \$2,000 in the net operating income determined under the absorption and variable costing methods.

2. Describe the major advantages of the absorption costing method.
3. Describe the major advantages of the variable costing method.

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GNB 12e Practice Exam Solutions – Chapter 7

1. Part (a) Solution (Learning Objective 1):

Direct materials	\$2.00
Direct labor	3.00
Variable manufacturing overhead	1.00
Fixed manufacturing overhead (\$20,000 divided by 10,000 units)	<u>2.00</u>
Product cost using absorption costing	<u>\$8.00</u>

Part (b) Solution (Learning Objective 1):

Direct materials	\$2.00
Direct labor	\$3.00
Variable manufacturing overhead	\$1.00
Product cost using variable costing	<u>\$6.00</u>

Part (c) Solution (Learning Objective 2):

Sales (9,000 units @ \$12)		\$108,000
Cost of goods sold:		
Beginning inventory	\$ 0	
Cost of goods manufactured (10,000 @ \$8 per unit)	80,000	
Less: ending inventory (1,000 @ \$8 per unit)	<u>(8,000)</u>	<u>72,000</u>
Gross margin		36,000
Less fixed manufacturing overhead		
Less selling & administrative expenses (variable of 9,000 @ \$3 per unit + fixed of \$5,000)		<u>32,000</u>
Net operating income		<u>\$ 4,000</u>

Part (d) Solution (Learning Objective 2):

Sales (9,000 units @ \$12)		\$108,000
Variable cost of goods sold (9,000 @ \$6 per unit)		54,000
Less variable selling & administrative expenses (9,000 @ \$3 per unit)		<u>27,000</u>

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Contribution margin		27,000
Fixed manufacturing overhead	20,000	
Fixed selling & administrative expenses	<u>5,000</u>	<u>25,000</u>
Net operating income		<u>\$ 2,000</u>

Part (e) Solution (Learning Objective 2):

Note that there was no beginning inventory. As such, the difference in net operating income of \$2,000 can be explained by looking at the amount of ending inventory reported using the two methods. The difference is due to the fixed manufacturing overhead costs (1,000 units in ending inventory @ \$2 of fixed manufacturing overhead cost per unit = \$2,000) is included in inventory (rather than expensed) when absorption costing is used, but is expensed immediately (rather than being included in inventory) when variable costing is used.

2. Solution (Learning Objective 4):

Advantages of absorption costing include:

- Method is required by GAAP and tax authorities, and
- Method reflects the full costs of manufacturing a product.

3. Solution (Learning Objective 4):

Advantages of variable costing include:

- Method is compatible with CVP and TOC analysis,
- Method does not cause fluctuations in profit due to changing production and inventory levels, unlike the absorption method,
- Method show only variable product costs so it avoids the problem under absorption method where managers mistakenly think fixed manufacturing costs are variable product costs,
- Variable costing allows total fixed manufacturing overhead costs to be visible on the income statement, rather than being "buried" in the cost of goods sold and inventory figures,
- Variable costing avoids some of the problems with overhead costs allocations, and
- Variable costs are more easily used with standard costing and flexible budgeting.

GNB 12e Practice Exam – Chapter 8

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. Sargent Company uses activity-based costing to determine the costs of its two products: A and B. The estimated total cost and expected activity for each of the company's three activity cost pools are as follows:

Activity Cost Pool	Estimated Cost	Expected Activity		
		Product A	Product B	Total
Activity 1	\$32,000	2,200	1,800	4,000

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Activity 2	\$28,000	400	300	700
Activity 3	\$37,600	800	300	1,100

Part (a) What is the activity rate under the activity-based costing system for Activity 2?

Part (b) How much total cost will be assigned to Products A and B for Activity 2?

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2. Fey Company has two products: A and B. The annual production and sales level of Product A is 18,188 units. The annual production and sales level of Product B is 31,652. The company uses activity-based costing and has prepared the following analysis showing the estimated total cost and expected activity for each of its three activity cost pools:

Activity Cost Pool	Estimated Cost	Expected Activity		
		Product A	Product B	Total
Activity 1	\$ 58,400	1,000	500	1,500
Activity 2	\$ 80,000	200	800	1,000
Activity 3	\$360,000	600	5,400	6,000

Part (a) What is the total overhead cost allocated to Product B under activity-based costing?

Part (b) What is the overhead cost per unit of Product B under activity-based costing?

3. Fey Company has two products: A and B. The annual production and sales level of Product A is 18,188 units. The annual production and sales level of Product B is 31,652. The company uses activity-based costing and has prepared the following analysis showing the estimated total cost and expected activity for each of its three activity cost pools:

Activity Cost Pool	Estimated Cost	Expected Activity		
		Product A	Product B	Total
Activity 1	\$ 58,400	1,000	500	1,500
Activity 2	\$ 80,000	200	800	1,000
Activity 3	\$360,000	600	5,400	6,000

(Note that this is the same information as provided for the previous question.) The following information is also available:

Sales price per unit	\$100.00
Direct material per unit	20.00
Direct labor per unit	10.00

Prepare a profit margin report for Product B from an activity view.

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GNB 12e Practice Exam Solutions – Chapter 8

1. Part (a) Solution (Learning Objective 3):

The activity rate for Activity 2 would be determined as follows:

$$\$28,000 \div 700 = \$40.00$$

Part (b) Solution (Learning Objective 4):

The product cost allocations for Activity 2 would be determined as follows:

Product A cost allocation for Activity 2: $400 \times \$40 = \$16,000$

Product B cost allocation for Activity 2: $300 \times \$40 = \$12,000$

2. Part (a) Solution (Learning Objective 2):

The total overhead cost allocations for Product #2 would be determined as follows:

Activity 1	$(\$58,400 \div 1,500) \times 500$	\$ 19,466.67
Activity 2	$(\$80,000 \div 1,000) \times 800$ 64,000.00	64,000.00
Activity 3	$(\$360,000 \div 6,000) \times 5,400$	<u>324,000.00</u>
Total overhead cost per unit for Product B		<u>\$407,466.67</u>

2. Part (b) Solution (Learning Objective 2):

The overhead cost per unit allocations for Product B would be determined as follows:

Total overhead cost per unit for Product B	\$407,466.67
Divided by number of units produced	\div <u>31,652</u>
Overhead cost per unit of Product B	<u>\$ 12.87</u>

3. Solution (Learning Objective 3):

The profit margin report for Product B from an activity view would be as follows:

Sales Revenues ($\$100 \times 31,652$ units)		\$3,165,200
Direct Materials ($\$20 \times 31,652$ units)	\$ 633,040	
Direct Labor ($\$10 \times 31,652$ units)	316,520	
Activity 1 Overhead costs	19,467	
Activity 2 Overhead costs	64,000	
Activity 3 Overhead costs	<u>324,000</u>	<u>1,357,027</u>
Product margin		<u>\$1,808,173</u>

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GNB 12e Practice Exam – Chapter 9

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. Frame-It Company produces and sells picture frames. To guard against out of stock situations, the company requires that 20% of the next month's sales be on hand at the end of each month. Budgeted sales of picture frames over the next three months are:

	January	February	March
Budgeted sales in units	320,000	480,000	400,000

What would budgeted production for February be?

2. Santypal Company has budgeted production for next year as follows:

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Production in units	80,000	96,000	128,000	112,000

Ten pounds of raw materials are required for each unit produced. Raw materials on hand at the beginning of the year total 20,000 lbs. The raw materials inventory at the end of each quarter should equal 10% of the next quarter's production needs. What would budgeted purchases of raw materials in the second quarter be?

3. Daley Company plans to sell 96,000 units during the month of August. If the company has 20,000 units on hand at the start of the month, and plans to have 16,000 units on hand at the end of the month, how many units must be produced during the month?
4. Fifty percent of Java Company's sales are for cash; the rest are on credit. Seventy percent of the credit sales are collected in the month of sale, twenty percent in the month following sale, and five percent in the second month following sale. The remainder is expected to be uncollectible. The following are budgeted sales data:

	October	November	December
Total sales	\$280,000	\$240,000	\$320,000

- Part (a) How much of the December sales are expected to be collected during December?
Part (b) What is the budgeted amount of total cash receipts in December?

GNB 12e Practice Exam Solutions – Chapter 9

- 1 **Solution (Learning Objective 3):**

Budgeted production for February would be determined as follows:

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Sales	480,000
Plus planned ending inventory (400,000 x .20)	80,000
Less beginning inventory (480,000 x .20)	<u>(96,000)</u>
Units to be produced	<u>464,000</u>

2. Solution (Learning Objective 4):

Budgeted purchases of raw materials in the second quarter would be determined as follows:

Required for:	
Second quarter production (96,000 x 10 lbs.)	960,000
Planned ending inventory (128,000 x .10 x 10 lbs.)	128,000
Less planned beginning inventory (96,000 x .10 x 10 lbs.)	<u>(96,000)</u>
Budgeted purchases of pounds of raw materials	<u>992,000</u>

3. Solution (Learning Objective 3):

The number of units that must be produced during the month would be determined as follows:

Sales	96,000
Plus planned ending inventory	16,000
Less beginning inventory	<u>(20,000)</u>
Units to be produced	<u>92,000</u>

4. Part (a) Solution (Learning Objective 2):

The amount of December sales expected to be collected during December would be budgeted as follows:

Month of	Collected during December	Calculations

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Sale		
December:		
Credit	\$112,000	$(\$320,000 \times .50 \times .70)$
Cash	<u>160,000</u>	$(\$320,000 \times .50)$
Total	<u>\$272,000</u>	

Part (b) Solution (Learning Objective 2):

Total cash receipts in December would be budgeted as follows:

Month of Sale	Collected during December	Calculations
December	\$272,000	From part (a)
November	24,000	$(\$240,000 \times .50 \times .20)$
October	<u>7,000</u>	$(\$280,000 \times .50 \times .05)$
Total	<u>\$303,000</u>	

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GNB 12e Practice Exam – Chapter 10

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. Prescott Company employs a standard cost system in which direct materials inventory is carried at standard cost. The company has established the following standards for the prime costs of one unit of product:

	Standard Quantity	Standard Price	Standard Cost
Direct labor	2.6 hours	\$44.00/hour	\$114.40
Direct materials	12.0 pounds	\$14.00/pound	168.00

During April, the company purchased 330,000 pounds of direct material at a total cost of \$4,686,000. The total factory wages for June were \$3,200,000, of which 90% was for direct labor. The company manufactured 25,000 units of product during April using 302,000 pounds of direct material and 64,000 direct labor hours.

Part (a) What is the price variance for the direct material acquired by the company during April?

Part (b) What is the direct material quantity variance for April?

Part (c) What is the direct labor rate variance for April?

Part (d) What is the direct labor efficiency variance for April?

2. Phoenix Company maintains warehouses that stock items carried by its e-retailer clients. When one of Phoenix' clients receives an order from an online customer, the order is forwarded to Phoenix. Phoenix then pulls the item from the warehouse, packs it and ships it to the customer. Phoenix uses a predetermined variable overhead rate based on direct labor-hours. According to the company's records, 0.04 direct labor-hours are required to fulfill an order for one item and the variable overhead rate is \$3.25 per direct-labor hour. During December, Phoenix shipped 120,000 orders using 4,600 direct labor-hours. The company incurred a total of \$14,720 in variable overhead costs.

Part (a) What is the variable overhead spending variance during December?

Part (b) What is the variable overhead efficiency variance during December?

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GNB 12e Practice Exam Solutions – Chapter 10

1. Part (a) Solution (Learning Objective 2):

First, calculate the actual price per unit of materials as follows.

Total cost of \$4,686,000 ÷ 330,000 lbs. = \$14.20 per pound

Then calculate the materials price variance as follows.

Materials price variance = AQ x (AP – SP) = 330,000 x (\$14.20 – \$14.00) = \$66,000 (U)

Part (b) Solution (Learning Objective 2):

First, calculate the standard quantity as follows.

25,000 units x 12.0 pounds per unit = 300,000 pounds

Then calculate the material quantity variance as follows.

Materials quantity variance = SP x (AQ – SQ) = \$14.00 x (302,000 – 300,000) = \$28,000(U)

Part (c) Solution (Learning Objective 3):

First, calculate the actual rate per hour of direct labor as follows:

(\$3,200,000 x .90) ÷ 64,000 hours = \$45.00 per hour

Then calculate the labor rate price variance as follows:

Labor rate variance = AH x (AR – SR)

Labor rate variance = 64,000 x (\$45.00 – \$44.00) = \$64,000 (U)

Part (d) Solution (Learning Objective 3):

First, calculate the standard hours as follows:

25,000 units x 2.6 hours per unit = 65,000 hours

Then calculate the direct labor efficiency variance as follows:

Direct labor efficiency variance = SR x (AH – SH) = \$44.00 x (64,000 – 65,000) = \$44,000 (F)

2. Part (a) Solution (Learning Objective 4):

The variable overhead spending variance during December is determined as follows:

Actual Hours of Input, at the Actual Rate (AH×AR)	Actual Hours of Input, at the Standard Rate (AH×SR)
4,600 hours (given) × \$3.20 per hour (or \$14,720 ÷ 4,600 hours)	4,600 hours (given) × \$3.25 per hour (given)
= \$14,720 (given)	= \$14,950
Variable overhead spending variance, \$230 F	

Alternatively, the variable overhead spending variance is determined as follows:

AH x (AR – SR) = 4,600 hours (\$3.20 per hour – \$3.25 per hour) = \$230 F

Part (b) Solution (Learning Objective 4):

The variable overhead spending variance during December is determined as follows:

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Actual Hours of Input, at the Standard Rate . (AH×SR)	Standard Hours Allowed for Output, at the Standard Rate . (SH×SR)
4,600 hours (given) × \$3.25 per hour (given)	4,800 hours (or 120,000 × 0.04 DLH) × \$3.25 per hour (given)
= \$14,950	= \$15,600
Variable overhead efficiency variance, \$650 F	

Alternatively, the variable overhead efficiency variance is determined as follows:
 $SR \times (AH - SH) = \$3.25 \text{ per hour } (4,600 \text{ hours} - 4,800 \text{ hours}) = \650 F

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GNB 12e Practice Exam – Chapter 11

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. The Duvall Company applies manufacturing overhead costs to products on the basis of direct labor-hours. The standard cost card shows that 6 direct labor-hours are required per unit of product. The company estimated that it would work 180,000 direct labor-hours and incur the following manufacturing overhead costs for the month of March:

Total fixed overhead costs	\$237,600
Total variable overhead costs	\$198,000

During March, the company completed 28,000 units of product, worked 172,000 direct labor-hours, and incurred the following total manufacturing overhead costs:

Total fixed overhead costs	\$230,600
Total variable overhead costs	\$197,800

The denominator activity used to calculate its predetermined overhead rate was 180,000 direct labor-hours.

Part (a) What is the variable overhead (VOH) spending variance for March?

Part (b) What is the variable overhead (VOH) efficiency variance for March?

Part (c) What is the fixed overhead budget variance for March?

Part (d) What is the fixed overhead volume variance for March?

2. What are the major weaknesses of static budgets?

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GNB 12e Practice Exam Solutions – Chapter 11

1. Part (a) Solution (Learning Objective 3):

First, compute the variable overhead (VOH) rate as follows:

VOH rate = Budgeted variable overhead costs ÷ budgeted direct labor hours

VOH rate = \$198,000 ÷ 180,000 direct labor hours = \$1.10 per direct labor hour

Then, compute the variable overhead (VOH) spending variance as follows:

VOH spending variance = Actual VOH incurred – (Actual direct labor hours x VOH rate per direct labor hour) = \$197,800 – (172,000 hours x \$1.10 per hour) = \$8,600 U

The variance is unfavorable because the actual overhead costs were more than the benchmark (that is, how much should have been spent in total on variable overhead items during the period).

Part (b) Solution (Learning Objective 4):

First, compute the variable overhead (VOH) rate as follows:

VOH rate = Budgeted variable overhead costs ÷ budgeted direct labor hours

VOH rate = \$198,000 ÷ 180,000 direct labor hours = \$1.10 per direct labor hour

Then, compute the efficiency variance as follows:

VOH efficiency variance = (AH hours x VOH rate) - (SH hours x VOH rate) = (172,000 hours x \$1.10/DL hour) – ((28,000 units x 6 DL hours/unit) x \$1.10/hour) = \$4,400 U

More direct labor hours (172,000) were worked than were allowed at standard (168,000); as such, the overhead efficiency variance is unfavorable.

Part (c) Solution (Learning Objective 6):

The fixed overhead (FOH) budget variance is determined as follows:

FOH budget variance = Actual fixed overhead – Budgeted fixed overhead = \$230,600 – \$237,600 = \$7,000 F

Since actual fixed overhead was less than the amount budgeted for the period, the budget variance is favorable.

Part (d) Solution (Learning Objective 6):

First, compute the fixed overhead (FOH) rate as follows:

FOH rate = Budgeted fixed overhead costs ÷ budgeted direct labor hours = \$237,600 ÷ 180,000 direct labor hours = \$1.32 per direct labor hour

Then, the FOH volume variance is determined as follows:

FOH Volume variance = Budgeted fixed overhead – (Standard hours allowed x FOH rate) = \$237,600 – (((28,000 units x 6 DL hrs./unit) x \$1.32 per DL hour) = \$15,840 U

Since budgeted fixed overhead was more than the amount applied to work in process during the period, the volume variance is unfavorable.

2. Solution (Learning Objective 1):

The major weaknesses of static budgets include the following:

- Static budgets are geared only to a single level of activity.
- Static budgets cannot be used to assess whether variable costs are under control.
- Static budgets force the manager to compare actual costs at one level of activity to budgeted costs at a different level of activity.

GNB 12e Practice Exam – Chapter 12

Print these pages. Answer each of the following questions, explaining your answers or

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showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. The following data are available for the Southwestern Division of Evans, Inc. and the single product it makes.

Annual fixed costs	\$560,000
Average operating assets	\$3,000,000
Unit selling price	\$40
Variable cost per unit	\$24

How many units must the division sell each year to have an ROI of 16%?

2. The Northeastern Division of Brillstein Inc. recorded operating data as follows for the past year.

Average operating assets	200,000
Net operating income	50,000
Residual income	26,000
Sales	\$400,000
Stockholders' equity	160,000

Part (a) What was the division's return on investment?

Part (b) What was the division's margin?

Part (c) What was the division's turnover?

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3. Cameron Company has recorded the following information about the results of its operations for the first quarter:

	Total Company	Southern Division	Northern Division
Sales revenues	\$200,000	\$ 80,000	\$120,000
Variable cost of sales	\$ 60,000	30,000	30,000
Fixed costs:			
Common	\$100,000	25,000	75,000
Traceable	\$ 50,000	20,000	30,000

Based on this information, prepare a segmented income statement for the quarter and comment on the results.

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GNB 12e Practice Exam Solutions – Chapter 12

1. Solution (Learning Objective 2):

First, calculate, the division's required operating income as follows:

Net operating income = Average operating assets x ROI = \$3,000,000 x .16 = \$480,000

Then, calculate the number of units that must be sold to generate that operating income as follows: Net operating income = Sales – Variable expenses – Fixed expenses

Let X represent the number of units

$\$480,000 = \$40X - \$24X - \$560,000$; $\$1,040,000 = \$16X$; $X = 65,000$

2. Part (a) Solution (Learning Objective 2):

The return on investment for the past year is determined as follows:

$\text{ROI} = \text{Net operating income} \div \text{Average operating assets} = \$50,000 \div \$200,000 = 25\%$

Part (b) Solution (Learning Objective 2):

The margin for the past year is determined as follows:

$\text{Margin} = \text{Net operating income} \div \text{Sales} = \$50,000 \div \$400,000 = 12.5\%$

Part (c) Solution (Learning Objective 2):

The turnover for the past year is determined as follows:

$\text{Turnover} = \text{Sales} \div \text{Average operating assets} = \$400,000 \div \$200,000 = 2$

3. Solution (Learning Objective 1):

	Total Company	Southern Division	Northern Division
Sales revenues	\$200,000	\$ 80,000	\$120,000
Variable cost of sales	<u>60,000</u>	<u>30,000</u>	<u>30,000</u>
Contribution margin	140,000	50,000	90,000
Less traceable fixed costs	<u>50,000</u>	<u>20,000</u>	<u>30,000</u>
Segment margin	90,000	<u>\$ 30,000</u>	<u>\$ 60,000</u>
Less common fixed costs	<u>100,000</u>		
Net operating loss	<u>(\$10,000)</u>		

Since common fixed costs are not traceable to the divisions, they should not be included in segment margins. As can be seen from the data, the company's divisions have performed with positive segment margins, but as a whole the company has a net operating loss for the quarter due to the significant amount of common fixed costs. If possible, the company needs to increase its revenues and/or decrease its costs (particularly fixed costs) to generate operating income instead of loss.

GNB 12e Practice Exam – Chapter 13

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1. Bazar Company is a small family business that produces wooden plaques and trophies:

	Plaques	Trophies
Selling price per unit	\$18	\$15
Variable cost per unit	<u>12</u>	<u>8</u>
Contribution margin per unit	<u>\$ 6</u>	<u>\$ 7</u>
Contribution margin ratio	<u>33%</u>	<u>47%</u>

In producing the items, the primary "bottleneck" is due to the fact the company only has one machine, a sander, to sand the wood that is used for the plaques or the trophies. Generally, the wood required for each plaque takes 0.25 hour to sand, while the wood required for each trophy takes 0.50 hour to sand. Based on the constraint related to the machine time, which product should be emphasized if only limited machine time is available?

2. A study has been conducted to determine if one of the departments of Sparrow Company should be discontinued. The contribution margin in the department is \$150,000 per year. Fixed expenses charged to the department are \$130,000 per year. It is estimated that \$120,000 of these fixed expenses could be eliminated if the department is discontinued.

Part (a) If the department is discontinued, what will be the impact on the company's overall net operating income?

Part (b) Which costs are irrelevant to this decision?

3. Lavender Company produces 2,000 parts per year, which are used in the assembly of one of its products. The unit product cost of these parts is:

Variable manufacturing cost	\$64
Fixed manufacturing cost	<u>36</u>
Unit product cost	<u>\$100</u>

The part can be purchased from an outside supplier at \$80 per unit. If the part is purchased from the outside supplier, two-thirds of the fixed manufacturing costs can be eliminated.

Part (a) What costs are irrelevant to this decision?

Part (b) What would the annual impact on the company's net operating income be as a result of buying the part from the outside supplier?

4. The following are Carly Company's unit costs of making and selling an item at a volume of 20,000 units per month (which represents the company's capacity):

Manufacturing:	
----------------	--

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Direct materials	\$2.00
Direct labor	4.00
Variable overhead	1.00
Fixed overhead	1.80
Selling and administrative:	
Variable	3.00
Fixed	1.200

Assume the company has 100 units left over from last year which have small defects and which will have to be sold at a reduced price as scrap. This would have no effect on the company's other sales. The variable selling and administrative costs would have to be incurred to sell the defective units. What cost is relevant as a guide for setting a minimum price on these defective units?

5. Golden Company sells its product for \$42 per unit. The company's unit product cost based on the full capacity of 400,000 units is as follows:

Direct materials	\$ 8
Direct labor	10
Manufacturing overhead	<u>12</u>
Unit product cost	<u>\$30</u>

A special order offering to buy 40,000 units has been received from a foreign distributor. The only selling costs that would be incurred on this order would be \$6 per unit for shipping. The company has sufficient idle capacity to manufacture the additional units. Two-thirds of the manufacturing overhead is fixed and would not be affected by this order. Assume that direct labor is an avoidable cost in this decision. In negotiating a price for the special order, what is the minimum acceptable selling price per unit?

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GNB 12e Practice Exam Solutions – Chapter 13

1. Solution (Learning Objective 5):

To evaluate a situation where there is a constrained resource ("bottleneck"), the contribution margin per unit of constrained resource should be calculated. While at first it appears the trophies should be emphasized based on the data given above, when the contribution margin per machine hour is computed, it appears the plaques should be emphasized, as follows:

	Plaques	Trophies
Contribution margin (CM) per unit	\$ 6	\$ 7
Machine hours per unit (MH)	.25	.50
CM per machine hour (CM ÷ MH)	\$ 24	\$ 14

In other words, for each hour of machine time, the wood for four plaques can be sanded with a CM of \$6 per plaque, for a total of \$24 CM per machine hour. Alternatively, for each hour of machine time, the wood for two trophies can be sanded with a CM of \$7 per trophy, for a total of \$14 CM per hour of machine time. So with limited machine time, the plaques should be emphasized since more CM per machine hour will be realized.

2. Part (a) Solution (Learning Objective 2):

CM that would be lost if department is discontinued	\$(150,000)
Less fixed costs that can be avoided if department is discontinued	120,000
Increase (decrease) in net operating income	\$ (30,000)

Part (b) Solution (Learning Objective 1):

Based on this information alone, because the company's net operating income would decrease by \$30,000 per year, they should not discontinue this department. The common fixed costs of \$10,000 (or \$130,000 - \$120,000) are irrelevant to this decision.

3. Part (a) Solution (Learning Objective 3):

The product costs related to making the parts that can be eliminated are the variable manufacturing costs (\$48 per unit) and two-thirds of the fixed manufacturing costs ($2/3 \times \$36 = \24) for a total of \$72 (or \$48 + \$24) per unit. Those are the costs that are relevant to the "make" decision. The cost that is relevant to the "buy" decision is the purchase price of \$80 per unit.

Since one-third of the fixed manufacturing costs cannot be eliminated, they are irrelevant to this decision.

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Part (b) Solution (Learning Objective 3):

The annual impact on the company's net operating income as a result of buying the part from the outside supplier is determined as follows:

	Production "Cost" per Unit	Per Unit Differential Costs		Total Differential Costs—2,000 Units	
		Make	Buy	Make	Buy
Variable manufacturing costs	\$ 64	\$64		\$128,000	
Fixed manufacturing costs	<u>36</u>				
Outside purchase price			\$80		\$160,000
Fixed manufacturing costs eliminated			<u>(24)</u>		<u>(48,000)</u>
Total cost	<u>\$100</u>	<u>\$64</u>	<u>\$56</u>	<u>\$128,000</u>	<u>\$112,000</u>
Difference in favor of purchasing			<u>\$8</u>		<u>\$16,000</u>

4. Solution (Learning Objective 3):

A relevant cost is a cost that differs between alternatives in a decision-making situation. Since the variable selling and administrative expenses of \$3.00 per unit would need to be incurred to sell the defective units, they are relevant to the decision and should be used as a guide for setting the minimum price on these defective units.

Note that none of the other per unit costs would be relevant as a guide for setting the minimum price on the defective units. The four types manufacturing costs listed above are sunk costs (i.e., a cost that has already been incurred and that cannot be changed by any decision made now or in the future) and, as such, are not relevant to this decision. The fixed selling and administrative expenses is a common fixed cost (i.e., a cost that supports the operations of more than one segment of an organization and is not avoidable in whole or in part by eliminating any one segment) and, as such, are not relevant to this decision.)

5. Solution (Learning Objective 4):

The minimum acceptable selling price per unit is determined as follows:

Direct materials	\$ 8
Direct labor	10
Variable manufacturing overhead (\$12 x 1/3)	4
Variable selling costs (shipping)	<u>6</u>
Minimum selling price	<u>\$28</u>

GNB 12e Practice Exam – Chapter 14

Print these pages. Answer each of the following questions, explaining your answers or

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showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. The following data pertain to an investment that is being considered by the management of Newton Company:

Cost of the investment	\$56,865
Estimated salvage value	\$ 3,000
Annual cost savings	\$ 15,000
Life of the project	5 years
Discount rate	10%

Part (a) What is the net present value of the proposed investment?

Part (b) Should the project be accepted?

2. Touro Company has gathered the following data on a proposed investment project:

Cost of the investment	\$1,200,000
Estimated salvage value	\$0
Annual cost inflows	\$240,000
Life of the project	10 years
Discount rate	10%

Part (a) What is the payback period for the investment?

Part (b) What is the simple rate of return on the investment?

3. Touro Company has gathered the following data on a proposed investment project:

Cost of the investment	\$1,200,000
Estimated salvage value	\$0
Annual cost inflows	\$ 240,000
Life of the project	10 years
Discount rate	10%

Part (a) What is the net present value of this investment?

Part (b) Should the proposal be accepted? Why or why not?

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GNB 12e Practice Exam Solutions – Chapter 14

1. Parts (a) and (b) Solution (Learning Objective 1):

Since the NPV is positive, the project would be acceptable, as follows:

	<u>Years</u>	<u>Cash Flows</u>	<u>10% Factor</u>	<u>Present Value</u>
Investment in equipment	Now	\$(56,865)	1.000	\$(56,865)
Annual net cash inflows	1-5	15,000	3.791	56,865
Salvage value of equipment	5	3,000	0.621	<u>1,863</u>
Net present value				<u>\$ 1,863</u>

2. Part (a) Solution (Learning Objective 5):

The payback period for the investment would be determined as follows:

Payback period = Required investment ÷ Annual cash inflows = \$1,200,000 ÷ \$240,000 = 5 years

Part (b) Solution (Learning Objective 5):

The simple rate of return on the investment would be determined as follows:

Incremental net operating income ÷ Investment required = Simple rate of return

\$240,000 ÷ \$1,200,000 = 20%

3. Parts (a) and (b) Solution (Learning Objective 1):

Since the NPV of the project is positive, the project would be acceptable, as follows:

	<u>Years</u>	<u>Cash Flows</u>	<u>10% Factor</u>	<u>Present Value</u>
Investment in equipment	Now	\$(1,200,000)	1.000	\$(1,200,000)
Annual net cash inflows	1-10	240,000	6.145	<u>1,474,800</u>
Net present value				<u>\$ 274,800</u>

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GNB 12e Practice Exam – Chapter 15

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. Charles Company recorded the following events for the year just ended:

Collection of a loan	\$165,000
Dividends paid to shareholders	270,000
Interest paid on notes payable	105,000
Payment of taxes	135,000
Retirement of preferred stock	150,000
Sale of bonds issued by other companies	225,000

Part (a) What was the net cash resulting from financing activities for the year?

Part (b) What was the net in cash resulting from investing activities for the year?

2. Tyler Company recorded the following activity for the year just ended:

Common stock issued	\$ 600,000
Dividends paid to stockholders	60,000
Dividends received from investments	90,000
Notes issued for long-term borrowings	240,000
Proceeds from sale of plant equipment	1,200,000
Purchase of plant equipment	360,000

Part (a) What was the net cash provided by financing activities for the year?

Part (b) What was the net cash provided by investing activities for the year?

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3. The Eagle Rock Company has the following information about its activities for the current year:

Beginning cash balance	\$40,000
Cash collections from customers	50,000
Net income	120,000
Depreciation expense	8,000
Cash paid to suppliers	10,000
Increase in accounts receivable	60,000
Decrease in accounts payable	28,000
Purchase of property, plant and equipment	15,000
Issuance of common stock	4,000

Part (a) Prepare a cash flows statement using the indirect method (Hint: You will not use all of the information provided above.)

Part (b) (Complete this part of the problem only if you are responsible for Appendix 15A)
Prepare a cash flows statement using the direct method (Hint: You will not use all of the information provided above.)

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GNB 12e Practice Exam Solutions – Chapter 15

1. Part (a) Solution (Learning Objective 1):

	Inflow (Outflow)
Retirement of preferred stock	\$ (150,000)
Dividends paid to shareholders	<u>(270,000)</u>
Net cash used by financing activities	<u>\$(420,000)</u>

Part (b) Solution (Learning Objective 2):

	Inflow (Outflow)
Sale of bonds issued by other companies	\$225,000
Collection of a loan	<u>165,000</u>
Net cash provided by investing activities	<u>\$390,000</u>

2. Solution (Learning Objective 3):

	Inflow (Outflow)
Common stock issued	\$600,000
Notes issued for long-term borrowings	240,000
Dividends paid to stockholders	<u>(60,000)</u>
Net cash provided by financing activities	<u>\$780,000</u>

Part (b) Solution (Learning Objective 3):

	Inflow (Outflow)
Proceeds from sale of plant equipment	\$1,200,000
Purchase of plant equipment	<u>(360,000)</u>
Net cash provided by investing activities	<u>\$ 840,000</u>

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3. Part (a) Solution (Learning Objective 3):

Statement of Cash Flows (Indirect Method):

Operating Activities:	
Net income	\$120,000
Add back noncash expense—depreciation	8,000
Less: Increase in accounts receivable	(60,000)
Decrease in accounts payable	(28,000)
Net cash provided by operating activities	<u>40,000</u>
Investing Activities:	
Purchase of property, plant and equipment	<u>(15,000)</u>
Financing Activities:	
Issuance of common stock	<u>4,000</u>
Net increase in cash over quarter	29,000
Beginning cash balance	<u>40,000</u>
Ending cash balance	<u>\$69,000</u>

Part (b) Solution (Learning Objective 4; Appendix 15A):

Statement of Cash Flows (Direct Method)

Operating Activities:	
Cash collected from customers	\$ 50,000
Cash paid to suppliers	<u>(10,000)</u>
Net cash provided by operating activities	<u>40,000</u>
Investing Activities:	
Purchase of property, plant and equipment	<u>(15,000)</u>
Financing Activities:	
Issuance of common stock	<u>4,000</u>
Net increase in cash over quarter	29,000
Beginning cash balance	<u>40,000</u>
Ending cash balance	<u>\$69,000</u>

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GNB 12e Practice Exam – Chapter 16

Print these pages. Answer each of the following questions, explaining your answers or showing your work, as appropriate, and then compare your solutions to those provided at the end of the practice exam.

1. The following information pertains to the Pointe Company:

	2009	2008
Revenues	\$100,000	\$80,000
Cost of sales	50,000	40,000
Selling and administrative expense	20,000	10,000
Interest expense	<u>5,000</u>	<u>3,000</u>
Net income	<u>\$ 25,000</u>	<u>\$27,000</u>

Based on this information, perform comparative and common-size analyses of the company's performance for the two years presented.

2. Robin Company had \$540,000 in sales on account last year. The accounts receivable balance increased from \$30,000 at the beginning of the year to \$54,000 at the end of the year. What was the company's average collection period (age of receivables)?
3. During the year, Gardenia Company paid dividends of \$30,000 on its preferred stock. The company's net income for the year was \$360,000. Other selected financial data for the company includes the following:

Account Balances	Beginning of Year	End of Year
Common stock	\$900,000	\$1,200,000
Preferred stock	375,000	375,000
Retained earnings	225,000	555,000

What is the company's return on common stockholders' equity for the year?

4. The total assets of Barrington Company were \$1,950,000 at the beginning of the year and \$1,830,000 at the end of the year. The company reported net income of \$225,000 and interest expense of \$30,000. The company's income tax rate was 30%. What was the company's return on total assets for the year?

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5. Simmons Company had no prepaid expenses and inventories remained unchanged during the year. Other selected year-end data for the company includes the following:

Current liabilities	\$1,800,000
Cost of goods sold	\$1,500,000
Acid-test ratio	2.5 to 1
Current ratio	3.0 to 1

What was the company's inventory turnover ratio for the year?

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GNB 12e Practice Exam Solutions – Chapter 16

1. Solution (Learning Objective 1):

Comparative (horizontal analysis) looks at how performance has been over time (e.g. year-to-year), while common size (vertical) analysis looks at the relative percentages of the items within a financial statement.

Pointe Company Comparative and Common-Size Analysis 2009 and 2008

	2009	%	2008	%	\$ Change	% Change
Revenues	\$100,000	100	\$80,000	100	\$20,000	+ 25%
Cost of sales	<u>50,000</u>	<u>50</u>	<u>40,000</u>	<u>50</u>	<u>10,000</u>	+ 25%
Gross margin	<u>50,000</u>	<u>50</u>	<u>40,000</u>	<u>50</u>	<u>10,000</u>	+ 25%
Selling & admin. expense	20,000	20	10,000	12	10,000	+100%
Interest expense	<u>5,000</u>	<u>5</u>	<u>3,000</u>	<u>4</u>	<u>2,000</u>	+ 67%
Net income	<u>\$ 25,000</u>	<u>25</u>	<u>\$27,000</u>	<u>(34)</u>	<u>\$(2,000)</u>	– 7%

Based on the analysis above, it appears that while the company's sales have increased significantly from 2008 to 2009 (25% increase, or \$20,000), the net income actually decreased slightly (7%) due to increased selling and administrative expenses (which increased 100% over the year) as well as higher interest expense. It would be wise for the management and employees to look for ways to reduce selling and administrative expenses so that future sales revenues will not be consumed by increased expenses.

2. Solution (Learning Objective 4):

The company's average collection period would be determined as follows:

First, calculate the accounts receivable turnover as follows:

$$\text{Accounts receivable turnover} = \text{Sales} \div \text{Average accounts receivable} = \$540,000 \div [(\$30,000 + \$54,000) \div 2] = 12.857$$

Then, calculate the average collection period as follows:

$$\text{Average collection period} = 365 \text{ days} \div \text{Accounts receivable turnover} = 365 \div 12.857 = 28.389 \text{ (or 28.4 days)}$$

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3. Solution (Learning Objective 2):

The company's return on common stockholders' equity would be determined as follows:

Return on common stockholders' equity = $(\text{Net income} - \text{Preferred dividends}) \div \text{Average common stockholders' equity}$

Return on common stockholders' equity = $(\$360,000 - \$30,000) \div [((\$1,200,000 + \$555,000) + (\$900,000 + \$225,000)) \div 2] = 22.92\%$

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4. Solution (Learning Objective 2):

The company's return on total assets would be determined as follows:

Return on total assets = $[\text{Net income} + (\text{Interest expense} \times (1 - \text{Tax rate}))] \div \text{Average total assets}$
 $= [\$225,000 + (\$30,000 \times (1 - .30))] \div [(\$1,950,000 + \$1,830,000) \div 2] = 13.0\%$

5. Solution (Learning Objective 3):

The company's inventory turnover ratio would be determined as follows:

First, determine the amount of current assets using the current ratio as follows:

Current ratio of 3.0 = Current assets \div Current liabilities of \$1,800,000; Current assets = \$5,400,000

Next, determine the amount of quick assets using the acid-test (or quick) ratio as follows:

Acid-test ratio of 2.5 = Quick assets \div Current liabilities of \$1,800,000; Quick assets = \$4,500,000

Since there are no prepaid expenses in this situation, estimated inventories would be the difference between current assets and quick assets as follows:

Inventory = Current assets of \$5,400,000 – Quick assets of \$4,500,000 = \$900,000

Finally, compute the inventory turnover ratio as follows:

Inventory turnover ratio = Cost of goods sold \div Average inventories = $\$1,500,000 \div [(\$900,000 + \$900,000) \div 2] = 1.67 \text{ times}$

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virtual.uni.help@gmail.com