

BUSINESS ENVIRONMENT & CONCEPTS

CPA2904US3-38

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ABOUT UPDATING SUPPLEMENT VERSION 38.3

Information that is only six months old is eligible to be tested on the CPA exam. Candidates with the 38th edition and corresponding software (version 12) will find the information in the version 38.3 updating supplement more than adequate for the January-February 2010 exam window and later exam windows.

When new information first becomes available, the examiners tend to test new or changed portions of concepts lightly. Coverage of information after that point may increase, if it is in a heavily tested area. Do not fall into the trap of attaching undue significance to new information merely because it is new.

Remember, with the information and techniques in our material, passing the exam is an attainable goal. ***Adhere to a reasonable study plan—and pass the first time!***

STUDY OPTIONS AVAILABLE TO CANDIDATES

As every candidate's needs are different, Bisk Education offers a variety of CPA Review formats and packages that are guaranteed* to help you pass the CPA exam on your next sitting. Options include: our Online CPA Review with structured Internet classes and our self-study CPA Review utilizing multimedia CD-ROM software, video programs, audio lectures, and books.

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OTHER SOURCES OF INFORMATION FOR CANDIDATES

Candidates choosing to use previous editions of our books must accept responsibility for adequately updating their materials. Candidates should consider the strain that this will add to the already time-consuming process of studying for the exam. Candidates with the 37th edition and corresponding software also will want Updating Supplement Version 37.3. Material in the earlier updating supplements is incorporated within the 38th edition, and the corresponding version 12 software, as appropriate. Material in version 38.2 updating supplement is incorporated within version 38.3.

Candidates with editions earlier than the 37th are strongly encouraged to purchase new materials. At a minimum, these candidates should read the supplements pertaining to the edition that they have. Each supplement has information on the appropriate supplements for the edition previous to the one it updates. Candidates choosing to use previous editions of our books must accept responsibility for adequately updating their materials. Candidates should consider the strain that this will add to the already time-consuming process of studying for the exam. Material in the related updating supplements may be reviewed to determine the nature and quantity of information that has changed from one edition to another.

SIMULATIONS: UNCHANGED

There will be no simulations in the BEC section in the 2010 exam windows. Bisk Education expects simulations to be in the BEC exam section starting no earlier than 2011.

The AICPA examiners have not made an official announcement on when they will add simulations to the BEC exam. Our best estimate currently is that if the AICPA examiners add simulations to BEC, it will be when the content specification outline (CSO) is changed. The AICPA plans to implement the new CSO in late 2010 and will include written communications. The examiners generally announce changes at least six months in advance of the exam window that the changes affect.

ERRATA

The following error is in the 38th edition book. If you find other items that you believe are ambiguous or in error, please contact the Bisk Education editors (help@cpaexam.com) with details.

Chapter 51

Page 51-45, Exhibit 21: The fourth sentence in paragraph three should be replaced with: "Faith pays a total of \$26/share for a stock valued at \$40/share, $(\$40 - \$25) = \$15$ /share gain on her \$1/share warrant investment. The \$15/share gain represents a 3000% annualized return for a 6 month period."

Chapter 52, page 36, Question #89 should be replaced with:

89. What amount should Augusta budget for cash payments to material suppliers during the period?

- a. \$189,000
- b. \$229,000
- c. \$210,000
- d. \$214,000

(11/96, AR, #4-1, 6329)

Chapter 52, page 46, Answer #89 should be replaced with:

89. (b) \$70,000 represents the entire payments for the entire period of ten weeks. Payments for nine, not ten, weeks of the period must be made. The beginning accounts payable balance also must be paid.

Beginning accounts payable	\$ 40,000
$(\$3 \times 70,000 \text{ units per week} \times 9 / 10)$	<u>189,000</u>
Total payments during the 10 weeks	\$ 229,000

RECENTLY RELEASED AICPA QUESTIONS

In September 2008, and April 2009, the AICPA released several questions labeled as “Year 2008 Disclosed Questions,” and “Year 2009 Disclosed Questions.” Respectively the BEC questions and the related unofficial solutions are reproduced here, along with the exclusive Bisk Education explanations. The AICPA did not state whether these questions were used on an exam. These questions are intended only as a study aid and should not be used to predict the content of future exams. It is extremely unlikely that released questions will appear on future examinations.

Unlike some other exam sections, the AICPA made no reference to a difficulty rating for these questions.

Problem 1

1. Which of the following statement(s) is(are) true regarding the relationship between absorption costing net income and variable costing income?

- I. When production exceeds sales, variable costing income exceeds absorption costing net income.
- II. When sales exceeds production, absorption costing income exceeds variable costing net income.

- a. I only
- b. II only
- c. Both I and II
- d. Neither I nor II (R/08, BEC, 0140M, #1, 8698)

2. Which of the following statements is(are) correct regarding corporate debt and equity securities?

- I. Both debt and equity security holders have an ownership interest in the corporation.
- II. Both debt and equity securities have an obligation to pay income.

- a. I only
- b. II only
- c. Both I and II
- d. Neither I nor II (R/08, BEC, 0150L, #2, 8699)

3. Selected information concerning the operations of a company for the year ended December 31 is as follows:

Units produced	20,000
Units sold	18,000
Direct materials used	\$80,000
Direct labor incurred	\$40,000
Fixed factory overhead	\$50,000
Variable factory overhead	\$24,000
Fixed selling and administrative expenses	\$60,000
Variable selling and administrative expenses	\$ 9,000

Work-in-process inventories at the beginning and end of the year were zero. What was the company’s finished goods inventory cost at December 31 under the variable (direct) costing method?

- a. \$23,900
- b. \$19,400
- c. \$17,000
- d. \$14,400 (R/08, BEC, 0233MR1, #3, 8700)

4. Which of the following circumstances may permit the piercing of the corporate veil of a closely held corporation and thus may cause its shareholders to be held personally liable?

- I. The corporation is thinly capitalized.
- II. The corporation borrows money from a shareholder without giving the shareholder a security interest in corporate assets.

- a. I only
- b. II only
- c. Both I and II
- d. Neither I nor II (R/08, BEC, 0301L, #4, 8701)

5. The principle that protects corporate directors from personal liability for acts performed in good faith on behalf of the corporation is known as

- a. The clean hands doctrine
- b. The full disclosure rule
- c. The responsible person doctrine
- d. The business judgment rule (R/08, BEC, 0999L, #5, 8702)

6. What type of business organization may generally be formed without filing an organizational document or certificate with a state government agency or office?

- a. A corporation
- b. A limited liability company
- c. A general partnership
- d. A limited partnership (R/08, BEC, 1077L, #6, 8703)

7. Which of the following is usually a benefit of using electronic funds transfer for international cash transactions?

- Creation of multilingual disaster recovery plans
- Reduction in the frequency of data entry errors
- Off-site storage of foreign source documents
- Improvement in the audit trail for cash transactions (R/08, BEC, 1433A, #7, 8704)

8. Which of the following acts is most likely to cause a court to pierce the corporate veil?

- Failure to designate a registered agent in the articles of incorporation (Charter)
- Retention of excess capital
- Failure to conduct a significant portion of business in the chartering state
- Using corporate assets for the owner's personal purposes (R/08, BEC, 5134L, #8, 8705)

9. What business entity can be voluntarily dissolved and terminated without filing a dissolution document with the state of organization?

- A corporation
- A general partnership
- A limited liability limited partnership
- A limited partnership (R/08, BEC, 5206L, #9, 8706)

10. JackKue Co. plans to produce 200,000 pairs of roller skates during January of next year. Planned production for February is 250,000 pairs. Sales are forecasted at 180,000 pairs for January and 240,000 pairs for February. Each pair of roller skates has eight wheels. JackKue's policy is to maintain 10% of the next month's production in inventory at the end of a month. How many wheels should JackKue purchase during January?

- 195,000
- 205,000
- 1,560,000
- 1,640,000 (R/08, BEC, A0380B, #10, 8707)

11. The following information is available on Crain Co.'s two product lines:

	<u>Chairs</u>	<u>Tables</u>
Sales	\$180,000	\$ 48,000
Variable costs	<u>(96,000)</u>	<u>(30,000)</u>
Contribution margin	84,000	18,000
Fixed costs:		
Avoidable	(36,000)	(12,000)
Unavoidable	<u>(18,000)</u>	<u>(10,800)</u>
Operating income (loss)	<u>\$ 30,000</u>	<u>\$ (4,800)</u>

Assuming the tables line is discontinued, and the factory space previously used to make tables is rented for \$24,000 per year, operating income will increase by what amount?

- \$13,200
- \$18,000
- \$24,000
- \$28,800 (R/08, BEC, A0504B, #11, 8708)

12. Which of the following decision-making models equates the initial investment with the present value of the future cash inflows?

- Accounting rate of return
- Payback period
- Internal rate of return
- Cost-benefit ratio (R/08, BEC, A0627B, #12, 8709)

13. Hughes and Brody start a business as a closely-held corporation. Hughes owns 51 of the 100 shares of stock issued by the firm and Brody owns 49. One year later, the corporation decides to sell another 200 shares. Which of the following types of rights would give Hughes and Brody a preference over other purchasers to buy shares to maintain control of the firm?

- Shareholder derivative rights
- Pre-emptive rights
- Cumulative voting rights
- Inspection rights (R/08, BEC, A0718B, #13, 8710)

14. Which of the following listings correctly describes the order in which the four types of budgets must be prepared?

- Production, direct materials purchases, sales, cash disbursements
- Sales, production, direct materials purchases, cash disbursements
- Cash disbursements, direct materials purchases, production, sales
- Sales, direct materials purchases, production, cash disbursements (R/08, BEC, A0909B, #14, 8711)

15. Which of the following statements is correct regarding financial decision making?

- Opportunity cost is recorded as a normal business expense.
- The accounting rate of return considers the time value of money.
- A strength of the payback method is that it is based on profitability.
- Capital budgeting is based on predictions of an uncertain future.

(R/08, BEC, A1054B, #15, 8712)

16. A company purchases an item for \$43,000. The salvage value of the item is \$3,000. The cost of capital is 8%. Pertinent information related to this purchase is as follows:

	<u>Net cash flows</u>	<u>Present value factor at 8%</u>
Year 1	\$10,000	0.926
Year 2	15,000	0.857
Year 3	20,000	0.794
Year 4	27,000	0.735

What is the discounted payback period in years?

- 3.10
- 3.25
- 2.90
- 3.14

(R/08, BEC, A1173B, #16, 8713)

17. What is an internal rate of return?

- A net present value
- An accounting rate of return
- A payback period expected from an investment
- A time-adjusted rate of return from an investment

(R/08, BEC, A1330B, #17, 8714)

18. For the current period production levels, Woodwork Co. budgeted 11,000 board feet of production and purchased 15,000 board feet. The material cost was budgeted at \$7 per foot. The actual cost for the period was \$8.50 per foot. What was Woodwork's material price variance for the period?

- \$ 6,000 unfavorable
- \$16,500 unfavorable
- \$19,500 unfavorable
- \$22,500 unfavorable

(R/08, BEC, A1351B, #18, 8715)

19. Snyder Co. manufactures fans with direct material costs of \$10 per unit and direct labor of \$7 per unit. A local carrier charges Snyder \$5 per unit to make deliveries. Sales commissions are paid at 10% of the selling price. Fans are sold for \$100 each. Indirect factory costs and administrative costs are \$6,800 and \$37,200 per month, respectively. How many fans must Snyder produce to break even?

- 1,375
- 648
- 564
- 530

(R/08, BEC, A1356B, #19, 8716)

20. The difference between standard hours at standard wage rates and actual hours at standard wage rates is referred to as which of the following types of variances?

- Labor rate
- Labor usage
- Direct labor spending
- Indirect labor spending

(R/08, BEC, A1597B, #20, 8717)

21. Which of the following events would decrease the internal rate of return of a proposed asset purchase?

- Decrease tax credits on the asset
- Decrease related working capital requirements
- Shorten the payback period
- Use accelerated, instead of straight-line depreciation

(R/08, BEC, A1669B, #21, 8718)

22. Which of the following changes would result in the highest present value?

- A \$100 decrease in taxes each year for four years
- A \$100 decrease in the cash outflow each year for three years
- A \$100 increase in disposal value at the end of four years
- A \$100 increase in cash inflow each year for three years

(R/08, BEC, A1694B, #22, 8719)

23. Which of the following internal control procedures would prevent an employee from being paid an inappropriate hourly wage?

- Having the supervisor of the data entry clerk verify that each employee's hours worked are correctly entered into the system
- Using real-time posting of payroll so there can be **no** after-the-fact data manipulation of the payroll register
- Giving payroll data entry clerks the ability to change any suspicious hourly pay rates to a reasonable rate
- Limiting access to employee master files to authorized employees in the personnel department (R/08, BEC, A1722B, #23, 8720)

24. ABC, Inc. assessed overall risks of MIS systems projects on two standard criteria: technology used and design structure. The following systems projects have been assessed on these risk criteria. Which of the following projects holds the highest risk to ABC?

	<u>Technology</u>	<u>Structure</u>
a.	Current	Sketchy
b.	New	Sketchy
c.	Current	Well defined
d.	New	Well defined

(R/08, BEC, A1833B, #24, 8721)

25. A lender and a borrower signed a contract for a \$1,000 loan for one year. The lender asked the borrower to pay 3% interest. Inflation occurred and prices rose by 2% over the next year. The borrower repaid \$1,030. What is the amount worth in real terms, after inflation?

- \$1,060.90
- \$1,050.60
- \$1,019.80
- \$1,009.80 (R/08, BEC, A1932B, #25, 8722)

26. Which of the following is an advantage of net present value modeling?

- It is measured in time, **not** dollars.
- It uses accrual basis, **not** cash basis accounting for a project.
- It uses the accounting rate of return.
- It accounts for compounding of returns. (R/08, BEC, A1978B, #26, 8723)

27. Which of the following individuals would be most hurt by an unanticipated increase in inflation?

- A retiree living on a fixed income
- A borrower whose debt has a fixed interest rate
- A union worker whose contract includes a provision for regular cost-of-living adjustments
- A saver whose savings was placed in a variable rate savings account

(R/08, BEC, A1983B, #27, 8724)

28. An accounts payable clerk is accused of making unauthorized changes to previous payments to a vendor. Proof could be uncovered in which of the following places?

- Transaction logs
- Error reports
- Error files
- Validated data file

(R/08, BEC, A2003B, #28, 8725)

29. A client wants to know how many years it will take before the accumulated cash flows from an investment exceed the initial investment, without taking the time value of money into account. Which of the following financial models should be used?

- Payback period
- Discounted payback period
- Internal rate of return
- Net present value

(R/08, BEC, A2057B, #29, 8726)

30. If the dollar price of the euro rises, which of the following will occur?

- The dollar depreciates against the euro.
- The euro depreciates against the dollar.
- The euro will buy fewer European goods.
- The euro will buy fewer U.S. goods.

(R/08, BEC, A2088B, #30, 8727)

31. The calculation of depreciation is used in the determination of the net present value of an investment for which of the following reasons?

- The decline in the value of the investment should be reflected in the determination of net present value.
- Depreciation adjusts the book value of the investment.
- Depreciation represents cash outflow that must be added back to net income.
- Depreciation increases cash flow by reducing income taxes. (R/08, BEC, A2473B, #31, 8728)

32. Which of the following is a characteristic of a flexible budget?

- Provides budgeted numbers for various activity levels
- Allows for modification during the budgeted period
- Isolates the impact of variable costs on the overall budget
- Can be utilized by several product divisions
(R/08, BEC, A2495B, #32, 8729)

33. Wilson and Thomas are partners. Wilson contributed \$150,000 to the partnership, and Thomas contributed \$50,000. Wilson does 40% of the work, and Thomas does 60%. They do not have a partnership agreement that addresses the sharing of profits and losses. By the end of the year, the partnership has earned a profit of \$200,000. What is Wilson's share of the profit under the Revised Uniform Partnership Act?

- \$ 80,000
- \$100,000
- \$115,000
- \$150,000 (R/08, BEC, A2540B, #33, 8730)

34. A fast-growing service company is developing its information technology internally. What is the first step in the company's systems development life cycle?

- Analysis
- Implementation
- Testing
- Design (R/08, BEC, A2642B, #34, 8731)

35. Which of the following best describes a hot site?

- Location within the company that is most vulnerable to a disaster
- Location where a company can install data processing equipment on short notice
- Location that is equipped with a redundant hardware and software configuration
- Location that is considered too close to a potential disaster area
(R/08, BEC, A2733B, #35, 8732)

36. Which of the following attributes of a management report has the greatest impact on management's ability to make effective decisions?

- Summarization
- Exception orientation
- Relevance
- Conciseness (R/08, BEC, A3097B, #36, 8733)

37. A company's controller is adjusting next year's budget to reflect the impact of an expected 5% inflation rate. Listed below are selected items from next year's budget before the adjustment:

Total salaries expense	\$250,000
Health costs	100,000
Depreciation expense	65,000
Interest expense on 10-year fixed-rate notes	37,750

After adjusting for the 5% inflation rate, what is the company's total budget for the selected items before taxes for next year?

- \$470,250
- \$472,138
- \$473,500
- \$475,388 (R/08, BEC, A3267B, #37, 8734)

38. Compared to online real-time processing, batch processing has which of the following disadvantages?

- A greater level of control is necessary.
- Additional computing resources are required.
- Additional personnel are required.
- Stored data are current only after the update process. (R/08, BEC, A3405B, #38, 8735)

39. An economy is at the peak of the business cycle. Which of the following policy packages is the most effective way to dampen the economy and prevent inflation?

- Increase government spending, reduce taxes, increase money supply, and reduce interest rates
- Reduce government spending, increase taxes, increase money supply, and increase interest rates
- Reduce government spending, increase taxes, reduce money supply, and increase interest rates
- Reduce government spending, reduce taxes, reduce money supply, and reduce interest rates
(R/08, BEC, A3493B, #39, 8736)

40. Which of the following strategies would the Federal Reserve most likely pursue under an expansionary policy?

- Purchase federal securities and lower the discount rate.
- Reduce the reserve requirement while raising the discount rate.
- Raise the reserve requirement and lower the discount rate.
- Raise the reserve requirement and raise the discount rate. (R/08, BEC, A3583B, #40, 8737)

41. Which of the following represents the procedure managers use to identify whether the company has information that unauthorized individuals want, how these individuals could obtain the information, the value of the information, and the probability of unauthorized access occurring?

- a. Disaster recovery plan assessment
- b. Systems assessment
- c. Risk assessment
- d. Test of controls

(R/08, BEC, A3800B, #41, 8738)

42. A value-added network (VAN) is a privately owned network that performs which of the following functions?

- a. Route data transactions between trading partners
- b. Route data within a company's multiple networks
- c. Provide additional accuracy for data transmissions
- d. Provide services to send marketing data to customers

(R/08, BEC, A3885B, #42, 8739)

43. The Business Judgment Rule is a rule that immunizes corporate

- a. Management from liability for actions that result in corporate losses or damages if the actions are undertaken in good faith but are **not** within the power of the corporation or the authority of management to make
- b. Management from liability for actions that result in corporate losses or damages if the actions are undertaken in good faith and are within both the power of the corporation and the authority of management to make
- c. Shareholders from liability for actions that result in corporate losses or damages if the actions are undertaken in good faith and are within both the power of the corporation and the authority of shareholders to make
- d. Shareholders from liability for actions that result in corporate losses or damages if the actions are undertaken in good faith but are not within the power of the corporation or the authority of shareholders to make

(R/08, BEC, C00406B, #43, 8740)

44. A company uses a standard costing system. At the end of the current year, the company provides the following overhead information:

Actual overhead incurred	
Variable	\$90,000
Fixed	\$62,000
Budgeted fixed overhead	\$65,000
Variable overhead rate	
(per direct labor hour)	\$ 8
Standard hours allowed for actual production	12,000
Actual labor hours used	11,000

What amount is the variable overhead efficiency variance?

- a. \$8,000 favorable
- b. \$8,000 unfavorable
- c. \$6,000 favorable
- d. \$2,000 unfavorable

(R/08, BEC, C01897B, #44, 8741)

45. DJ Co. has a job-order cost system. The following debits (credits) appeared in the Work in Process account for the month of March:

March 1, balance	\$ 12,000
March 31, direct materials	40,000
March 31, direct labor	30,000
March 31, manufacturing overhead applied	27,000
March 31, to finished goods	(100,000)

DJ Co. applies overhead at a predetermined rate of 90% of direct labor cost. Job No. 101, the only job still in process at the end of March, has been charged with manufacturing overhead of \$2,250. What was the amount of direct materials charged to Job No. 101?

- a. \$2,250
- b. \$2,500
- c. \$4,250
- d. \$4,725

(R/08, BEC, C01902B, #45, 8742)

46. The owners of a limited liability company are known as which of the following?

- a. Partners
- b. Members
- c. Stockholders
- d. Shareholders

(R/08, BEC, C03398B, #46, 8743)

47. ABC Co. had debt with a market value of \$1 million and an after-tax cost of financing of 8%. ABC also had equity with a market value of \$2 million and a cost of equity capital of 9%. ABC's weighted-average cost of capital would be

- 8.0%
- 8.5%
- 8.7%
- 9.0%

(R/08, BEC, C03731B, #47, 8744)

48. Which of the following is a key difference in controls when changing from a manual system to a computer system?

- Internal control principles change
- Internal control objectives differ
- Control objectives are more difficult to achieve
- Methodologies for implementing controls change

(R/08, BEC, C03806B, #48, 8745)

49. Relevant information for material A follows:

Quantity purchased	6,500 lbs.
Standard quantity allowed	6,000 lbs.
Actual price	\$3.80
Standard price	\$4.00

What was the direct material price variance for material A?

- \$1,300 favorable
- \$1,200 favorable
- \$1,200 unfavorable
- \$1,300 unfavorable

(R/08, BEC, C05097B, #49, 8746)

50. Relevant information for product A follows:

Actual variable overhead cost per hour	\$8.00
Standard variable overhead cost per hour	\$7.50
Actual hours	4,500
Standard hours	5,000

What was the variable overhead spending variance for product A?

- \$2,250 favorable
- \$4,000 favorable
- \$2,250 unfavorable
- \$4,000 unfavorable

(R/08, BEC, C05101B, #50, 8747)

Problem 2

1. A company's target gross margin is 40% of the selling price of a product that costs \$89 per unit. The product's selling price should be

- \$124.60
- \$142.40
- \$148.33
- \$222.50

(R/09, BEC, 0077M, #1, 8891)

2. Wren Co. manufactures and sells two products with selling prices and variable costs as follows:

	A	B
Selling price	\$18.00	\$22.00
Variable costs	12.00	14.00

Wren's total annual fixed costs are \$38,400. Wren sells four units of A for every unit of B. If operating income last year was \$28,800, what was the number of units Wren sold?

- 5,486
- 6,000
- 9,600
- 10,500

(R/09, BEC, 0164M, #2, 8892)

3. Which form of business entity has the following attributes?

- Limited liability for all its owners
- Can permit all its owners to participate in management and control of the entity
- Absent an agreement to the contrary, is dissolved on the death, withdrawal, or bankruptcy of an owner

- A limited partnership
- A limited liability company
- A general partnership
- A corporation

(R/09, BEC, 1072L, #3, 8893)

4. Joint ventures are most similar to which of the following types of business organizations?

- Limited partnerships
- General partnerships
- Business trusts
- Subchapter S corporations

(R/09, BEC, 5030L, #4, 8894)

5. Which of the following statements best states the purpose of cumulative voting?

- a. To assure the continuance of incumbent directors
- b. To allow minority shareholders to gain representation on the board of directors
- c. To allow for the election of one-third of the board of directors each year
- d. To assure that a majority of shares voted elects the entire board of directors

(R/09, BEC, 5140L, #5, 8895)

6. Which of the following forms of business generally provides all owners with limited liability while avoiding federal taxation of income at the entity level?

- a. Subchapter C corporation
- b. Subchapter S corporation
- c. Partnership
- d. Limited partnership

(R/09, BEC, 5193L, #6, 8896)

7. Under the Revised Model Business Corporation Act, which of the following dividends is not defined as a distribution?

- a. Cash dividends
- b. Property dividends
- c. Liquidating dividends
- d. Stock dividends

(R/09, BEC, 5335L, #7, 8897)

8. Which of the following rates is most commonly compared to the internal rate of return to evaluate whether to make an investment?

- a. Short-term rate on U.S. Treasury bonds
- b. Prime rate of interest
- c. Weighted-average cost of capital
- d. Long-term rate on U.S. Treasury bonds

(R/09, BEC, A0069B, #8, 8898)

9. What is the most likely effect if a court pierces the corporate veil?

- a. The corporation's shareholders, officers, and directors can be assigned liability.
- b. The corporation can be held liable for acts of the directors.
- c. The corporation can lose its tax exempt status.
- d. The corporation can be held liable for acts of nonofficer employees of the corporation.

(R/09, BEC, A0084B, #9, 8899)

10. Eaton is the sole owner of a construction company. Eaton is concerned about personal liability. Which of the following entities will best allow Eaton to limit personal liability?

- a. Sole proprietorship
- b. C corporation
- c. General partnership
- d. Limited partnership

(R/09, BEC, A0470B, #10, 8900)

11. Which of the following costs would decrease if production levels were increased within the relevant range?

- a. Total fixed costs
- b. Variable costs per unit
- c. Total variable costs
- d. Fixed costs per unit

(R/09, BEC, A0591B, #11, 8901)

12. Which of the following assumptions is associated with the economic order quantity formula?

- a. The carrying cost per unit will vary with quantity ordered.
- b. The cost of placing an order will vary with quantity ordered.
- c. Periodic demand is known.
- d. The purchase cost per unit will vary based on quantity discounts.

(R/09, BEC, A0603B, #12, 8902)

13. Which of the following statements about investment decision models is true?

- a. The discounted payback rate takes into account cash flows for all periods.
- b. The payback rule ignores all cash flows after the end of the payback period.
- c. The net present value model says to accept investment opportunities when their rates of return exceed the company's incremental borrowing rate.
- d. The internal rate of return rule is to accept the investment if the opportunity cost of capital is greater than the internal rate of return.

(R/09, BEC, A0772B, #13, 8903)

14. Which of the following Federal Reserve policies would increase money supply?

- a. Change the multiplier effect
- b. Increase reserve requirements
- c. Reduce the discount rate
- d. Sell more U.S. Treasury bonds

(R/09, BEC, A0934B, #14, 8904)

15. Which of the following tasks would be included in a document flowchart for processing cash receipts?

- Compare control and remittance totals
 - Record returns and allowances
 - Authorize and generate an invoice
 - Authorize and generate a voucher
- (R/09, BEC, A0975B, #15, 8905)

16. The performance audit report of an information technology department indicated that the department lacked a disaster recovery plan. Which of the following steps should management take first to correct this condition?

- Bulletproof the information security architecture
 - Designate a hot site
 - Designate a cold site
 - Prepare a statement of responsibilities for tasks included in a disaster recovery plan
- (R/09, BEC, A0995B, #16, 8906)

17. The regression analysis results for ABC Co. is shown as $y = 90x + 45$. The standard error (S_b) is 30 and coefficient of determination (r^2) is 0.81. The budget calls for production of 100 units. What is ABC's estimate of total costs?

- \$3,090
 - \$4,590
 - \$9,030
 - \$9,045
- (R/09, BEC, A1069B, #17, 8907)

18. An information technology director collected the names and locations of key vendors, current hardware configuration, names of team members, and an alternative processing location. What is the director most likely preparing?

- Data restoration plan
 - Disaster recovery plan
 - System security policy
 - System hardware policy
- (R/09, BEC, A1166B, #18, 8908)

19. A company currently has 1,000 shares of common stock outstanding with zero debt. It has the choice of raising an additional \$100,000 by issuing 9% long-term debt, or issuing 500 shares of common stock. The company has a 40% tax rate. What level of earnings before interest and taxes (EBIT) would result in the same earnings per share (EPS) for the two financing options?

- An EBIT of \$27,000 would result in EPS of \$10.80 for both.
 - An EBIT of \$27,000 would result in EPS of \$7.20 for both.
 - An EBIT of -\$18,000 would result in EPS of (\$7.20) for both.
 - An EBIT of -\$10,800 would result in EPS of (\$7.92) for both.
- (R/09, BEC, A1260B, #19, 8909)

20. What does the consumer price index measure?

- Cost of capital
 - Average household income
 - Rate of inflation
 - Prime rate of interest
- (R/09, BEC, A1561B, #20, 8910)

21. Platinum Co. has a receivable due in 30 days for 30,000 euros. The treasurer is concerned that the value of the euro relative to the dollar will drop before the payment is received. What should Platinum do to reduce this risk?

- Buy 30,000 euros now
 - Enter into an interest rate swap contract for 30 days
 - Enter into a forward contract to sell 30,000 euros in 30 days
 - Platinum **cannot** effectively reduce this risk
- (R/09, BEC, A1658B, #21, 8911)

22. Which of the following best defines electronic data interchange (EDI) transactions?

- Electronic business information is exchanged between two or more businesses.
 - Customers' funds-related transactions are electronically transmitted and processed.
 - Entered sales data are electronically transmitted via a centralized network to a central processor.
 - Products sold on central web servers can be accessed by users any time.
- (R/09, BEC, A1871B, #22, 8912)

23. Which of the following entities does **not** require the approval of the state in which the entity is formed?

- A general partnership
- A limited liability partnership
- A limited liability company
- A corporation

(R/09, BEC, A1882B, #23, 8913)

24. Freely fluctuating exchange rates perform which of the following functions?

- They automatically correct a lack of equilibrium in the balance of payments.
- They make imports cheaper and exports more expensive.
- They impose constraints on the domestic economy.
- They eliminate the need for foreign currency hedging.

(R/09, BEC, A1960B, #24, 8914)

25. Which of the following characteristics would indicate that an item sold would have a high price elasticity of demand?

- The item has many similar substitutes.
- The cost of the item is low compared to the total budget of the purchasers.
- The item is considered a necessity.
- Changes in the price of the item are regulated by governmental agency.

(R/09, BEC, A1985B, #25, 8915)

26. A company has an outstanding one-year bank loan of \$500,000 at a stated interest rate of 8%. The company is required to maintain a 20% compensating balance in its checking account. The company would maintain a zero balance in this account if the requirement did not exist. What is the effective interest rate of the loan?

- 8%
- 10%
- 20%
- 28%

(R/09, BEC, A2410B, #26, 8916)

27. Which of the following is a primary function of a database management system?

- Report customization
- Capability to create and modify the database
- Financial transactions input
- Database access authorizations

(R/09, BEC, A2434B, #27, 8917)

28. Which of the following types of bonds is most likely to maintain a constant market value?

- Zero-coupon
- Floating-rate
- Callable
- Convertible

(R/09, BEC, A2682B, #28, 8918)

29. To maintain effective segregation of duties within the information technology function, an application programmer should have which of the following responsibilities?

- Modify and adapt operating system software
- Correct detected data entry errors for the cash disbursement system
- Code approved changes to a payroll program
- Maintain custody of the billing program code and its documentation

(R/09, BEC, A2704B, #29, 8919)

30. Which of the following limitations is common to the calculations of payback period, discounted cash flow, internal rate of return, and net present value?

- They do not consider the time value of money.
- They require multiple trial and error calculations.
- They require knowledge of a company's cost of capital.
- They rely on the forecasting of future data.

(R/09, BEC, A2919B, #30, 8920)

31. A company with a combined federal and state tax rate of 30% has the following capital structure:

<u>Weight</u>	<u>Instrument</u>	<u>Cost of capital</u>
40%	Bonds	10%
50%	Common stock	10%
10%	Preferred stock	20%

What is the weighted-average after-tax cost of capital for this company?

- 3.3%
- 7.7%
- 8.2%
- 9.8%

(R/09, BEC, A2927B, #21, 8921)

32. Which of the following terms best describes a payroll system?

- Data base management system (DBMS)
- Transaction processing system (TPS)
- Decision support system (DSS)
- Enterprise resource planning (ERP) system

(R/09, BEC, A3143B, #32, 8922)

33. To measure inventory management performance, a company monitors its inventory turnover ratio. Listed below are selected data from the company's accounting records:

	<u>Current year</u>	<u>Prior year</u>
Annual sales	\$2,525,000	\$2,125,000
Gross profit percent	40%	35%

Beginning finished goods inventory for the current year was 15% of the prior-year's annual sales, and ending finished goods inventory was 22% of the current-year's annual sales. What was the company's inventory turnover at the end of the current period?

- a. 1.82
 - b. 2.31
 - c. 2.73
 - d. 3.47
- (R/09, BEC, A3301B, #33, 8923)

34. In a large multinational organization, which of the following job responsibilities should be assigned to the network administrator?

- a. Managing remote access
 - b. Developing application programs
 - c. Reviewing security policy
 - d. Installing operating system upgrades
- (R/09, BEC, A3654B, #34, 8924)

35. An employee mistakenly enters April 31 in the date field. Which of the following programmed edit checks offers the best solution for detecting this error?

- a. Online prompting
 - b. Mathematical accuracy
 - c. Preformatted screen
 - d. Reasonableness
- (R/09, BEC, A3816B, #35, 8925)

36. A ceramics manufacturer sold cups last year for \$7.50 each. Variable costs of manufacturing were \$2.25 per unit. The company needed to sell 20,000 cups to break even. Net income was \$5,040. This year, the company expects the price per cup to be \$9.00; variable manufacturing costs to increase 33.3%; and fixed costs to increase 10%. How many cups (rounded) does the company need to sell this year to break even?

- a. 17,111
 - b. 17,500
 - c. 19,250
 - d. 25,667
- (R/09, BEC, A4022B, #36, 8926)

37. A company has the following financial information:

<u>Source of capital</u>	<u>Proportion of capital structure</u>	<u>Cost of capital</u>
Long-term debt	60%	7.1%
Preferred stock	20%	10.5%
Common stock	20%	14.2%

To maximize shareholder wealth, the company should accept projects with returns greater than what percent?

- a. 7.1%
 - b. 9.2%
 - c. 10.6%
 - d. 14.2%
- (R/09, BEC, A4203B, #37, 8927)

38. Two individuals are planning to form a business with equal ownership. The individuals would like to limit their personal liability, avoid double taxation, and be active in the business. Which of the following organizational structures would meet their requirements?

- a. C corporation
 - b. Limited liability company
 - c. Limited partnership
 - d. General partnership
- (R/09, BEC, C00385B, #38, 8928)

39. A company has the following information in its financial records:

	<u>Beginning balance</u>	<u>Ending balance</u>
Cash	\$ 3,900	\$ 3,000
Marketable securities	3,800	4,400
Accounts receivable	14,600	12,900
Total current assets	\$ 22,300	\$20,300
Net sales	\$103,200	
Expenses	20,430	
Net income	\$ 82,770	

What is the company's receivable turnover ratio?

- a. 6.0
 - b. 7.1
 - c. 7.5
 - d. 8.0
- (R/09, BEC, C00501B, #39, 8929)

40. A controller is developing a disaster recovery plan for a corporation's computer systems. In the event of a disaster that makes the company's facilities unusable, the controller has arranged for the use of an alternate location and the delivery of duplicate computer hardware to this alternate location. Which of the following recovery plans would best describe this arrangement?

- Hot site
 - Cold site
 - Back-up site procedures
 - Hot spare site agreement
- (R/09, BEC, C00517B, #40, 8930)

41. Controls in the information technology area are classified into the preventive, detective, and corrective categories. Which of the following is a preventive control?

- Contingency planning
 - Hash total
 - Echo check
 - Access control software
- (R/09, BEC, C01047B, #41, 8931)

42. Which of the following topics is the focus of managerial accounting?

- Financial statements and other financial reports
 - Historical cost principles
 - The needs of creditors
 - The needs of the organization's internal parties
- (R/09, BEC, C01109B, #42, 8932)

43. Which of the following statements is true regarding opportunity cost?

- Opportunity cost is recorded in the accounts of an organization that has a full costing system.
 - The potential benefit is not sacrificed when selecting an alternative.
 - Idle space that has no alternative use has an opportunity cost of zero.
 - Opportunity cost is representative of actual dollar outlay.
- (R/09, BEC, C01506B, #43, 8933)

44. Merry Co. has two major categories of factory overhead: material handling and quality control. The costs expected for these categories for the coming year are as follows:

Material handling	\$120,000
Quality inspection	200,000

The plant currently applies overhead based on direct labor hours. The estimated direct labor hours are 80,000 per year. The plant manager is asked to submit a bid and assembles the following data on a proposed job:

Direct materials	\$4,000
Direct labor (2,000 hours)	6,000

What amount is the estimated product cost on the proposed job?

- \$ 8,000
 - \$10,000
 - \$14,000
 - \$18,000
- (R/09, BEC, C02810B, #44, 8934)

45. Under the Revised Uniform Limited Partnership Act, which of the following statements is correct regarding limited partnerships?

- Limited partners may lose limited liability if they participate in management activities.
 - Limited partnerships may legally exist without filing a certificate of limited partnership.
 - Limited partners have the same rights, responsibilities, and authority as general partners.
 - Limited partners may contribute cash only and may not contribute services as their capital contributions.
- (R/09, BEC, C03405B, #45, 8935)

46. Which of the following is not a basic approach to allocating costs for costing inventory in joint-cost situations?

- Sales value at split-off
 - Flexible budget amounts
 - Physical measures such as weights or volume
 - Constant gross margin percentage net realizable value method
- (R/09, BEC, C03487B, #46, 8936)

47. A company has two divisions. Division A has operating income of \$500 and total assets of \$1,000. Division B has operating income of \$400 and total assets of \$1,600. The required rate of return for the company is 10%. Division B's residual income would be which of the following amounts?

- \$ 40
 - \$240
 - \$400
 - \$640
- (R/09, BEC, C03863B, #47, 8937)

48. The management of a company would do which of the following to compare and contrast its financial information to published information reflecting optimal amounts?

- a. Budget
- b. Forecast
- c. Benchmark
- d. Utilize best practices

(R/09, BEC, C03869B, #48, 8938)

49. Weighted average and first in, first out (FIFO) equivalent units would be the same in a period when which of the following occurs?

- a. No beginning inventory exists.
- b. No ending inventory exists.
- c. Beginning inventory units equal ending inventory units.
- d. Both a beginning and an ending inventory exist but are not necessarily equal.

(R/09, BEC, C03881B, #49, 8939)

50. Bacchus, Inc. is a large multinational corporation with various business units around the world. After a fire destroyed the corporate headquarters and largest manufacturing site, plans for which of the following would help Bacchus ensure a timely recovery?

- a. Daily backup
- b. Network security
- c. Business continuity
- d. Backup power

(R/09, BEC, C05054BR1 # 50, 8940)

Solution 1

1. (d) When production exceeds sales, inventories increase. In absorption costing, fixed manufacturing costs are charged to inventory. When inventories increase, absorption costing defers the fixed manufacturing costs charged to inventory to future periods. Variable costing expenses all fixed costs; resulting in lower net income than under absorption costing when inventories increase. When inventories decrease, absorption costing expenses all the current period's fixed costs plus the fixed costs included in inventory, while variable costing expenses only current-period fixed costs. (Chapter 52-4-3, CBT Skill: Judgment, CSO: 5.2.1)

2. (d) Shareholders are a corporation's owners. Debt security holders are the corporation's creditors. Corporations have an obligation to pay interest to bondholders. Shareholders have a right to share in dividends, if and when declared by the board of directors. The board of directors declares dividends at its discretion. It is not obligated to declare dividends. (Chapter 49-4-1, also see Chapter 51-3-1, CBT Skill: Analysis, CSO: 1.3.0)

3. (d) Under variable costing, only variable product costs are inventoried. The variable product costs are direct materials, direct labor, and variable overhead ($\$80,000 + \$40,000 + \$24,000 = \$144,000$). Cost per unit = $\$144,000 / 20,000$ units produced = $\$7.20$ per unit. Finished goods (FG) ending inventory is FG beginning inventory plus goods finished less sales (0 units + $20,000$ units - $18,000$ units) \times cost per unit ($\$7.20$) = $\$14,400$. Fixed overhead is expensed as a period cost along with selling and administrative expenses. (Chapter 52-4-2, CBT Skill: Analysis, CSO: 5.3.2)

4. (a) A thinly capitalized corporation has capital inadequate to meet the foreseeable needs of the corporation. Shareholders of an undercapitalized corporation may be held personally liable upon the corporation's insolvency. Corporations commonly borrow money without pledging collateral. Shareholders also may be corporate debtors. (Chapter 49-1-5, CBT Skill: Understanding, CSO: 1.4.0)

5. (d) The business judgment rule holds that a director who acts in good faith will not be held liable for mere errors of judgment or want of prudence, short of clear and gross negligence. The clean hands doctrine originated in equity and bars a plaintiff from seeking judicial relief regarding a matter in which s/he is not free of guilt. Compliance with the Sarbanes Oxley Act requires full disclosure. The responsible person doctrine is not a commonly used

term in this context. (Chapter 49-1-4, CBT Skill: Understanding, CSO: 1.4.0)

6. (c) A general partnership may be formed by oral agreement. No document is required unless the nature of the partnership falls under the 'Statute of Frauds.' A corporation, a limited liability company, and a limited partnership are all required to file an organizational document with a state government agency or office. (Chapter 48-2-1, CBT Skill: Understanding, CSO: 1.1.1)

7. (b) With electronic funds transfers (EFT), data is entered only once. Further processing is done electronically. Disaster recovery plans are contingency plans in the event of an unplanned shutdown. Document storage is an archiving function. EFT audit trails can be difficult to follow without adequate controls, documentation, and reporting. (Chapter 55-3-1, CBT Skill: Understanding, CSO: 4.5.0)

8. (d) Courts most likely will pierce the corporate veil when corporate assets are used for the owner's personal purposes. Failure to designate a registered agent in the articles of incorporation, retention of excess capital, and failure to conduct a significant portion of business in the chartering state are not indications of fraudulent acts or undercapitalization. (Chapter 49-1-7, CBT Skill: Analysis, CSO: 1.2.0)

9. (b) A general partnership does not necessarily require a dissolution document. When the partnership agreement specifies that the partnership will terminate on a certain date or when a particular project is completed, then the expiration of the term or completion of the project will dissolve the partnership. A corporation, a limited liability limited partnership and a limited partnership are required to execute a dissolution certificate. (Chapter 48-5-1, CBT Skill: Understanding, CSO: 1.2.0)

10. (d) JackKue Co. needs to order enough wheels to produce the 200,000 pairs in January ($200,000$ minus the December ending inventory of $20,000$ pairs = $180,000$), and another $25,000$ (10% of Feb production) pairs. $180,000 + 25,000 = 205,000$ pairs of skates \times 8 wheels per skate = $1,640,000$ wheels. Answers (a) & (b) reflect numbers of pairs of skates, not numbers of wheels. (Chapter 54-3-2, CBT Skill: Analysis, CSO: 3.1.1)

11. (b) The $\$18,000$ increase in operating income equals the difference between the new operating income of $\$43,200$ ($\$24,000$ rent + $\$30,000$ Chair income less the $\$10,800$ of unavoidable table

fixed costs) – the current operating income of \$25,200 (\$30,000 Chair income – \$4,800 Table loss). (Chapter 52-2-2, CBT Skill: Analysis, CSO: 5.1.1)

12. (c) By definition; the internal rate of return equates the initial investment with the present value of the future cash inflows. The accounting rate of return, the payback period, and the cost-benefit ratio do not take into account the time value of money. (Chapter 51-5-2, CBT Skill: Understanding, CSO: 3.1.1)

13. (b) Pre-emptive rights give shareholders the first right of refusal to subscribe to any new issues of stock in proportion to their existing holdings so as to maintain their percentage ownership and level of control. Derivative rights are shareholder rights to sue for the benefit of the corporation. Cumulative voting rights give minority shareholders a greater say on the board of directors. Inspection rights allow shareholders to inspect records of the corporation for proper purposes. Chapter 49-4-1, CBT Skill: Analysis, CSO: 1.4.0)

14. (b) The order in preparing a budget is to (1) estimates sales, (2) estimate needed production to support those sales, (3) estimate what direct materials are needed for that production level, and (4) determine what the direct materials will cost. (Chapter 54-1-2, CBT Skill: Understanding, CSO: 5.1.3)

15. (d) Capital budgeting's primary purpose is to estimate future expenditures based upon predictions of an uncertain future. Opportunity cost is an economic cost and not recorded as a business expense. The accounting rate of return does not consider the time value of money. The payback method is based on cash investment and nominal future cash flows. (Chapter 54-1-2, CBT Skill: Judgment, CSO: 5.1.2)

16. (b) Discounting year 1 ($\$10,000 \times 0.926 = \$9,260$), year 2 ($\$15,000 \times 0.857 = \$12,855$), and year 3 ($\$20,000 \times 0.794 = \$15,880$) cash flows yields \$37,995. Year 4 discounted cash flows are $\$27,000 \times 0.735 = \$19,845$. $\$43,000 - \$37,995 = \$5,005$. $\$5,005 / \$19,845 = 0.25$ (rounded). 3 years plus 0.25 years equals 3.25 years. The salvage value presumably is received beyond the payback period and so is irrelevant. (Chapter 51-5-2, CBT Skill: Analysis, CSO 3.1.2)

17. (d) The internal rate of return is the time-adjusted rate of return that would equate the present value of the future cash inflows to the initial cost of the investment. The accounting rate of return is calculated by dividing the annual average income by

the annual average investment. The payback period is that length of time that it takes to recover the initial investment. The time-adjusted rate of return is not a commonly used method. (Chapter 51-5-2, CBT Skill: Understanding, CSO 3.1.1)

18. (d) Material Price Variance (MPV) is $(\text{Actual Price} - \text{Standard Price}) \times \text{Actual Quantity}$. $(\$8.50 - \$7.00) \times 15,000 = \$1.50 \times 15,000 = \$22,500$ The MPV is unfavorable (actual price is greater than budgeted price). (Chapter 53-6-6, CBT Skill: Analysis, CSO: 5.3.1)

19. (b) By definition, the break-even point is where there is no profit or loss; thus, total fixed costs equal the total contribution margin. The break-even units equal total fixed costs divided by the contribution margin per unit. Total fixed costs = $\$6,800 + \$37,200 = \$44,000$. Contribution margin = Sales price minus variable costs = $\$100 - (\$10 + \$7 + \$5 + (10\% \text{ of } \$100)) = \68 . Break-even units = $\$44,000 / \$68 = 648$ fans. Contribution margin equals sales less all variable costs, not only variable production costs. Sales commissions are variable. (Chapter 52-2-4, CBT Skill: Analysis, CSO: 5.1.2)

20. (b) Labor usage variance is $(\text{Actual hours} - \text{Standard hours}) \times \text{Standard rate}$. This equation also can be written as $(\text{Actual hours} \times \text{Standard rate}) - (\text{Standard hours} \times \text{Standard rate})$. The labor rate variance is the difference between the actual and standard labor rates times the total hours worked. The direct labor spending and indirect labor spending variances are not used commonly. (Chapter 53-6-6, CBT Skill: Understanding, CSO: 5.1.3)

21. (a) Decreasing tax credits on the asset has the effect of increasing the initial cost of the investment. If there is no change in the discounted future cash flows, then the internal rate of return would decrease. Working capital items are not part of the IRR equation. The payback period does not consider the discounted rate of return. Accelerated depreciation would increase the internal rate of return due to the increased cash flow due to the reduced income taxes. (Chapter 51-5-2, CBT Skill: Analysis, CSO: 3.1.2)

22. (a) The present value is maximized by the smallest initial cash outflow or the largest increase in future cash inflows for the longest period of time. Three annual \$100 decreases in cash outflow and three annual \$100 increases in cash inflow have a present value equivalent to each other, but lower than four annual \$100 decreases in cash outflow. The one-time \$100 increase in disposal value at the end of four years has the lowest present value of the

given options. (Chapter 51-5-2, CBT Skill: Analysis, CSO: 3.1.2)

23. (d) An employee's hourly wage is recorded on the employee master file. Access to the employee master files should be limited to authorized employees in the personnel department only. This is an effective separation of duties. Having the data-entry clerk's supervisor verify hours worked doesn't prevent manipulation of wage rates. Early timing of the payroll posting doesn't prevent data manipulation. Giving data-entry clerks authorization to set wage rates as well as enter hours worked (recording) is a violation of the separation of duties. (Chapter 55-5-1, CBT Skill: Understanding, CSO: 4.1.4)

24. (b) As a general rule, well-defined structures are preferable to sketchy ones. A sketchy structure introduces uncertainties and, hence, risk. Presumably, current technology already has gone through a stage where hidden design defects and unexpected features have been discovered and resolved. New technology is more prone to hidden design defects and unexpected features. (Chapter 55-5-2, CBT Skill: Judgment, CSO: 4.1.4)

25. (d) The borrower pays \$1,030 in dollars that are worth 2% less than they were when lent [$\$1,030 / (100\% + 2\%) = \$1,009.80$]. An alternative solution is to multiply the \$1,000 lent by the nominal interest factor (1.03) divided by the inflation factor (1.02) and use it to determine a repayment valued in real terms, after inflation. [$\$1,000 \times (1.03 / 1.02) = \$1,009.80$]. (Chapter 50-2-7, also see Chapter 51-1-5, CBT Skill: Analysis, CSO: 3.1.2)

26. (d) Net present value (NPV) modeling recognizes the compounding effect of interest. NPV is measured in dollars or other units of money. NPV is calculated using cash flows, not accrual income amounts. Unlike the accounting rate of return, NPV uses the time value of money. (Chapter 51-2-2, CBT Skill: Understanding, CSO: 3.1.1)

27. (a) The retiree living on a fixed income suffers a reduction in purchasing power each year due to inflation increases. Presumably, a union worker and a saver with a variable rate savings account would have their earnings adjusted upward over time with inflation, mitigating—if not eliminating—its effects. The borrower whose debt has a fixed interest rate will benefit by inflation, as the debt is repaid with devalued money. (Chapter 50-2-7, CBT Skill: Analysis, CSO: 2.2.0)

28. (a) Transaction logs can be effectively reviewed and analyzed for inaccuracies and discrepancies to the data entered by the clerk. Error reports,

error files, and validated data files are effective controls for ensuring the system has correctly processed the initial data entry and all output meets the system specifications per the submitted user requirements. These controls all assume that the data entered into the system is correct. (Chapter 55-6-1, CBT Skill: Analysis, CSO: 4.3.2)

29. (a) By definition, the payback period is the length of time required to recover the initial cash outflow from the incremental future cash flows. All cash flows are measured in nominal dollars, that is, there is no attempt to account for the time value of money. The discounted payback period is the length of time required to recover the initial cash outflow from the future cash flows, discounted for the time value of money. The internal rate of return is the rate of return that results in a net present value (NPV) of zero. The NPV is the sum of all cash inflows and outflows discounted to present value. (Chapter 51-5-2, CBT Skill: Understanding, CSO: 3.1.2)

30. (a) A rise in the dollar price of the euro means that it takes more dollars to purchase euros. Therefore, the value of the dollar has depreciated against the euro. This will have no effect on how many European goods can be purchased with a euro since the dollar is not involved in such transactions. Because the euro has increased in value relative to the dollar, it is able to buy more U.S. goods than previously. (Chapter 50-3-3, CBT Skill: Understanding, CSO: 2.4.0)

31. (d) Depreciation has an indirect impact on cash flow in that it shelters income from income taxes. The decrease in cash paid for income taxes is equivalent to an increase in cash inflows in net present value calculations. While depreciation adjusts the book value of the related investment, this value is not used to determine the net present value of an investment. The recording of depreciation is a non-cash event. (Chapter 51-5-1, CBT Skill: Analysis, CSO: 3.1.2)

32. (a) A flexible budget reflects total fixed costs and variable costs based on a per unit basis times production levels. Thus, a flexible budget provides budgeted numbers for various activity levels within a relevant range. Because of its built-in flexibility, the budget does not need modification during the budget period. A flexible budget may or may not isolate the impact of variable costs or be used by several divisions, but neither of these attributes is the defining characteristic. (Chapter 54-1-3, CBT Skill: Understanding, CSO: 5.1.3)

33. (b) In a partnership, profits and losses are shared equally unless the agreement specifies

otherwise, even if the amount of contributed labor or capital is unequal. Since the partnership agreement does not address the sharing of profits and losses, profits are shared equally. Wilson is credited with 50% of the \$200,000 profit, or \$100,000. (Chapter 48-1-6, CBT Skill: Analysis, CSO: 1.3.0)

34. (a) A systems development life cycle follows the following phases: (1) Systems Analysis (Feasibility Study), (2) Systems Design, (3) Programming and Testing, (4) Implementation, and (5) Monitoring. (Chapter 55-1-5, CBT Skill: Understanding, CSO: 4.1.4)

35. (c) By definition, a hot site is a location where a functioning system is planned for use with minimal preparation in the event of a sudden shutdown at the primary work location. A cold site is a location where resources are available, but not ready for use without considerable effort. The situations described in the other answer options don't have a commonly used term. (Chapter 55-4-2, CBT Skill: Understanding, CSO: 4.4.0)

36. (c) Irrelevant information is useless for decision makers, regardless of summarization level, conciseness, or orientation. Only relevant information will assist management to make appropriate decisions. Summarized and concise information promotes timely analysis. Exception orientation helps focuses attention on possible problem areas. (Chapter 52-3-1, CBT Skill: Judgment, CSO: 4.1.3)

37. (a) Depreciation is based on previously made expenditures and, thus, is not subject to the effects of subsequent inflation. Interest expense related to fixed-rate notes likewise will remain the same for the notes' duration. Based upon current conditions, salary expense and health costs are subject to inflation's effects. Therefore, the budgeted costs for next year inflate salary expense and health costs $[(\$250,000 + \$100,000) \times 1.05 = \$367,500]$ by 5%, but not depreciation and interest expense $(\$367,500 + \$65,000 + \$37,750 = \$470,250)$. (Chapter 52-3-1, CBT Skill: Analysis, CSO: 5.1.3)

38. (d) One disadvantage of batch processing compared to online real-time processing is that the stored master data is current only immediately after the update process. As soon as the next transaction occurs, the master data file is obsolete. Batch processing often requires less complex controls, fewer computing resources, and fewer processing personnel. (Chapter 55-1-6, CBT Skill: Judgment, CSO: 4.3.2)

39. (c) Reducing government spending, increasing taxes, reducing the money supply, and

increasing interest rates are all ways to dampen the economy and prevent inflation. Reducing government spending reduces demand. Increasing taxes makes fewer resources available to the private sector and decreased motivation to generate more income; it results in reduced demand. Reducing increasing interest rates decreases the money supply, consequently decreasing demand. (Chapter 50-2-2, CBT Skill: Judgment, CSO: 2.1.0)

40. (a) Federal Reserve purchasing federal securities (debt) increases the money supply available to the private sector with a corresponding increase in demand. The reserve requirement is the percentage of deposits banks must have on hand related to loans. Reducing it in isolation eases lending constraints. The discount rate is the rate at which federal debt is discounted. Lowering the discount rate in isolation eases lending constraints. Easing lending constraints tends to increase borrowing for capital investments, which generally are held to spur economic growth. Both reducing the reserve requirement while raising the discount rate and raising the reserve requirement while lowering the discount rate tend to have offsetting effects on economic growth. Raising the reserve requirement and raising the discount rate most likely would dampen economic growth. (Chapter 50-2-4, CBT Skill: Judgment, CSO: 2.2.0)

41. (c) Risk assessment is concerned with impairments to operations from uncertain events, including unauthorized access to information and natural disasters. A disaster recovery plan assessment evaluates contingent plans to maintain computer functionality after an unplanned shutdown. Systems assessment involves the evaluation of a system, generally during system development. Tests of controls evaluate whether safeguards are effective. (Chapter 55-4-1, CBT Skill: Understanding, CSO: 4.1.4)

42. (a) A value-added network (VAN) provides additional services beyond mere connections to the Internet, particularly services enabling EDI (Electronic Data Interchange) to route communications and data transactions between entities such as trading partners. A router is a switch that transfers incoming messages to outgoing links via the most efficient route possible—for example, over the Internet. Transmission protocols provide additional accuracy for data transmissions. An extranet likely would be used to send marketing data to customers. Note: The editors do not expect similar questions on future exams. (Chapter 55-1-3, CBT Skill: Understanding, CSO: 4.5.0)

43. (b) The Business Judgment Rule protects management from liability for actions that result in losses or damages if undertaken in good faith, within the corporation's power, and within management's authority. The liability of a shareholder generally is limited to her/his capital investment. There is no doctrine providing additional protection to shareholders. (Chapter 49-1-4, CBT Skill: Understanding, CSO: 1.4.0)

44. (a) The variable overhead efficiency variance is the difference in actual and standard quantities times the standard price $[(11,000 \text{ actual hours} - 12,000 \text{ standard hours}) \times \$8/\text{hour} = (\$8,000)]$. Since actual hours are less than standard hours, the variance is favorable. (Chapter 53-6-7, CBT Skill: Analysis, CSO: 5.3.1)

45. (c) Goods available to finish of $(\$12,000 + \$40,000 + \$30,000 + \$27,000)$ are $\$109,000$. Since $\$100,000$ was transferred to finished goods, ending work in process (WIP) must be $\$9,000$. As ending WIP includes $\$2,250$ of overhead, direct labor must be $\$2,250 / 0.90 = \$2,500$. The remaining cost $(\$9,000 - \$2,250 - \$2,500 = \$4,250)$ in ending WIP is due to direct materials. (Chapter 53-1-2, CBT Skill: Understanding, CSO: 5.3.2)

46. (b) Owners of a limited liability company commonly are called members. Partnership owners are partners. Owners of a corporation are called either stockholders or shareholders. (Chapter 48-7-1, CBT Skill: Understanding, CSO: 1.1.2)

47. (c) The weighted-average cost of capital is the average cost of debt and equity weighted by their market values. The cost of debt is determined using an after-tax rate. The cost of debt is $\$1 \text{ million} \times 8\% = \$80,000$. The cost of equity capital is $\$2 \text{ million} \times 9\% = \$180,000$. The cost of capital is divided by total capital to determine the weighted average. $(\$80,000 + \$180,000) / (\$1 \text{ million} + \$2 \text{ million}) = 8.7\%$. (Chapter 51-5-3, CBT Skill: Analysis, CSO: 3.2.0)

48. (d) The key difference in controls when changing from a manual system to a computer system is the methodologies used for implementing the control changes. There is no difference in the control principles or control objectives when changing from one system to another. Furthermore, control objectives are not necessarily more difficult to achieve with a computer system. (Chapter 55-5-1, CBT Skill: Understanding, CSO: 4.1.4)

49. (a) The direct material price variance is $(\text{Actual Price} - \text{Standard Price}) \times \text{Actual Quantity}$. $(\$3.80/\text{unit} - \$4.00/\text{unit}) \times 6,500 \text{ units} = -\$0.20/\text{unit} \times 6,500 \text{ units} = -\$1,300$. The variance is favorable since actual price is less than standard price. (Chapter 53-6-6, CBT Skill: Analysis, CSO: 5.1.3)

50. (c) The variable overhead spending variance is $(\text{Actual price} - \text{Standard price}) \times \text{Actual quantity}$. $(\$8.00/\text{unit} - \$7.50/\text{unit}) \times 4,500 \text{ units} = \$0.50/\text{unit} \times 4,500 \text{ units} = \$2,250$. The variance is unfavorable since actual price is greater than standard price. Chapter 53-6-6, CBT Skill: Analysis, CSO: 5.1.3)

Solution 2

1. (c) A product's selling price is comprised of two components; cost of the product plus gross margin. Since the gross margin is stated to be 40%, then the product cost of $\$89$ per unit equals 60% of the selling price. Selling price is $\$89 / .60 = \148.33 (Chapter 52-3-7, CBT Skill: Analysis, CSO: 5.1.2)

2. (d) The total number of units needed to be sold = $(\text{fixed costs} + \text{operating income}) / \text{weighted composite contribution margin per unit}$.

Product	A	B	Composite
Selling price	\$18	\$22	
Variable cost	\$12	\$14	
Contribution margin	\$ 6	\$ 8	
Sales mix ratio	4	1	5
Weighted CM	\$24	\$ 8	\$32.00
Weighted CM/unit ($\$32.00/5$)			\$ 6.40

Total units to be sold = $(\text{fixed costs} + \text{operating income}) / \text{weighted contribution margin per unit}$.
Total units to be sold = $(\$38,400 + \$28,800) / \$6.40 = 10,500 \text{ units}$. (Chapter 52-2-4, CBT Skill: Analysis, CSO: 5.3.1)

3. (b) A limited liability company is an entity that provides limited liability for all its owners, allows all owners to participate in management and control, and absent an agreement to the contrary, is dissolved on the death, withdrawal, or bankruptcy of an owner. A limited partnership must have at least one general partner who bears unlimited personal liability. In a general partnership, all partners bear unlimited personal liability. The shareholders of a corporation are the owners with limited liability but do not all participate in the management and control of the corporation. (Chapter 48.7.1, CBT Skill: Judgment, CSO: 1.1.2)

4. (b) All partners in a joint venture have the right to share in the management and profits and have unlimited personal liability, similar to general partnerships. Limited partnerships, subchapter S corporations, and business trusts provide limited personal liability for at least some owners. (Chapter 48-1-2, CBT Skill: Understanding, CSO: 1.1.2)

5. (b) Cumulative voting is designed to allow minority shareholders to gain representation on the board of directors. Each shareholder receives votes equal to the number of her/his shares times the number of directors, and can then vote all of their votes for a particular director. The continuance of incumbent directors is not assured by voting design, nor does voting design assure that a majority of shares voted elects the entire board of directors. The election of one-third of the board of directors each year is accomplished by staggered terms. (Chapter 49-4-1, CBT Skill: Analysis, CSO: 1.4.0)

6. (b) A subchapter S corporation is specifically designed as a business entity which provides all owners with limited personal liability and avoids federal taxation of income at the entity level. All income is passed through to the owners where it is taxed on each owner's personal income tax form. C corporations are subject to federal tax. All partners in a general partnership and the general partner(s) in a limited partnership bear unlimited personal liability. (Chapter 49-6-2, CBT Skill: Judgment, CSO: 1.1.3)

7. (d) Stock dividends are additional shares issued to shareholders in proportion to their existing holdings. They reduce neither total assets nor stockholder's equity. The effect of a stock dividend is to reduce retained earnings and increase legal capital. Generally, cash dividends, property dividends and liquidating dividends are considered distributions. (Chapter 49-6-1, CBT Skill: Understanding, CSO: 1.3.0)

8. (c) An entity's weighted average cost of capital is equal to the weighted average of the cost of debt, preferred and common stock, and retained earnings, with their market values as weights. Since this is the composite rate of return on the company's current overall capital, it provides a hurdle rate which is compared to the projected internal rate of return on investments being evaluated. The short-term rate on U.S. Treasury bonds, the long-term rate on U.S. Treasury bonds and the prime rate of interest generally are less relevant than the weighted average cost of capital. (Chapter 51-5-2, CBT Skill: Analysis, CSO: 3.1.1)

9. (a) By definition, the act of disregarding the shareholders' general shield from liability for corporate debts is called piercing the corporate veil. This occurs when the court finds corporate fraud and desires to hold shareholders liable along with officers and directors. Piercing the corporate veil does not determine whether a corporation is liable for acts of the directors, and does not, in itself, cause a corporation to lose its tax-exempt status. A corporation is already liable for acts of employees of the corporation. (Chapter 49-1-7, CBT Skill: Judgment, CSO: 1.4.0)

10. (b) An attractive attribute of a C corporation is limited liability for owners. Risk of loss extends only to the shareholder's actual investment in the corporation. A sole proprietor and general partner bear full personal liability. A limited partnership must have at least one general partner bearing full personal liability. (Chapter 49-1-2, CBT Skill: Analysis, CSO: 1.4.0)

11. (d) By definition, fixed costs are costs that remain constant over the relevant range of activity. If production levels were increased, then fixed costs would be applied to a larger number of units and thus fixed costs per unit would decrease. Variable costs per unit remain the same. Total variable costs vary directly with production and would increase if production levels were increased. (Chapter 52.1.3, CBT Skill: Judgment, CSO: 5.3.2)

12. (c) The formula for the economic order quantity assumes that periodic demand for the good is known. The carrying cost per unit and the cost of placing an order are assumed to be fixed costs. The purchase cost per unit is not a part of the formula. (Chapter 51-4-3, CBT Skill: Analysis, CSO: 3.1.1)

13. (b) By definition, the payback period is the length of time required to recover the initial cash outflow from the incremental cash benefits after tax and only accounts for cash flows up to the point of recovering the initial investment. It ignores any further cash flows. The net present value model compares the rate of return with the company's cost of capital, not the company's borrowing rate. The internal rate of return method would reject investments if the opportunity cost of capital is greater than the internal rate of return. (Chapter 51-5-2, CBT Skill: Understanding, CSO: 3.1.2)

14. (c) Lowering the discount rate encourages borrowing and increases the money supply. The multiplier effect recognizes that money is spent and spent again as it changes hands among buyers and sellers. A higher multiplier effect increases income within the economy but does not change the total

money supply. Increasing reserve requirements or selling more U.S. Treasury bonds would decrease money supply. (Chapter 50-2-6, CBT Skill: Analysis, CSO: 2.2.0)

15. (a) Comparing control and remittance totals would be included in a document flowchart for processing cash receipts. An example would be comparing a batch total to the calculated amount that accounts receivable has decreased when processing cash receipts. Recording returns and allowances, authorizing and generating an invoice, and authorizing and generating a voucher are not part of processing cash receipts and would not be shown on this document flowchart. (Chapter 55-6-1, CBT Skill: Analysis, CSO: 4.2.1)

16. (d) Preparing a statement of responsibilities for tasks included in a disaster recovery plan is the first step that management should take. Only after an overall framework has been documented can management proceed with decisions defining the detailed tasks to be performed should a disaster occur. "Bulletproofing the information security architecture" is not a widely used term. (Chapter 55-4-2, CBT Skill: Understanding, CSO 4.4.0)

17. (d) The dependent variable (total costs) is $y = \$90x + \45 . The independent variable (the total number of units to be produced) is x , and $\$45$ represents fixed costs. $Y = (\$90 \times 100) + \$45 = \$9,045$. The standard error and the coefficient of determination are measures of reliability and accuracy, but are not used in the formula itself. (Chapter 54-2-2, CBT Skill: Judgment, CSO 5.1.2)

18. (b) A disaster recovery plan generally includes the names and locations of key vendors, the current hardware configuration, the names of team members, and an alternative processing location. A data restoration plan, a system security policy, and a system hardware policy do not need this information. (Chapter 55-6-1, CBT Skill: Understanding, CSO: 4.4.0)

19. (a) An EBIT of \$27,000 results in EPS of \$10.80 for both financing options. Taxable income is EBIT less interest expense. Net Income is taxable income times (100% less the tax rate). EPS is net income divided by outstanding shares.

Option 1—issue 9% debt

Taxable income $[(\$27,000) - (\$100,000 \times 9\% = \$9,000)] = \$18,000$

Net income $[\$18,000 \times (100\% - 40\%)] = \$10,800.$

EPS $=(\$10,800 / 1,000) = \$10.80/\text{share}$

Option 2—issue 500 shares of common stock

Taxable income $=(\$27,000 - \$0) = \$27,000$

Net income $=[\$27,000 \times (100\% - 40\%)] = \$16,200$

EPS $=(\$16,200 / 1,500) = \$10.80/\text{share}$

(Chapter 51-6-5, CBT Skill: Understanding, CSO: 3.2.0)

20. (c) The consumer price index is a comparison of the prices of a large market basket of items to a base value. It yields a rate of price changes over time and is commonly used as a measure of the rate of inflation. A firm's cost of capital is a weighted average of the costs of debt and equity funds. The prime rate is an interest rate that banks charge their most favored customers. Average household income is a measure of the standard of living. (Chapter 50-2-7, CBT Skill: Understanding, CSO: 2.2.0)

21. (c) Platinum Co. should enter into a forward contract to sell 30,000 euros in 30 days. Foreign-exchange forward contracts obligate one party to buy, and a counterparty to sell, a fixed amount of currency at an agreed-upon future date. By entering into a foreign-exchange forward contract, entities can effectively reduce the risk of large movements in foreign-exchange rates. Buying euros now or entering into an interest rate swap contract would not mitigate the risk of movements in future foreign-exchange rates. (Chapter 50-3-3, CBT Skill: Analysis, CSO: 2.4.0)

22. (a) By definition, EDI (electronic data interchange) is electronic communication among entities such as two or more companies. Electronically transmitting funds-related transactions and sales data to a central processor are internal to a single company. Access by users to products sold on central web servers does not involve exchanging business information. (Chapter 55-3-1, CBT Skill: Understanding, CSO: 4.5.0)

23. (a) An oral agreement or acts of the parties alone may establish a general partnership. A written agreement is needed only when the general partnership would otherwise be in violation of the Statute of Frauds. A limited liability partnership, a limited liability company, and a corporation all must file with the state. (Chapter 48-2-1, CBT Skill: Understanding, CSO: 1.1.1)

24. (a) Freely fluctuating exchange rates automatically correct a lack of equilibrium in the balance of payments. They neither impose nor remove constraints on the domestic economy. They do not eliminate the need for foreign currency hedging. Depending on the direction of the fluctuating exchange rates, they could make imports more expensive and

exports cheaper. (Chapter 50-3-5, CBT Skill: Understanding, CSO: 2.4.0)

25. (a) Price elasticity of demand measures responsiveness of demand to changes in price. If an item has many similar substitutes, then a price increase would cause customers to readily buy a substitute good. If the cost of the item is low, then a price increase provides little incentive to switch to a substitute good. Necessities, by definition, have low price elasticity. Government regulation of prices could occur with either high or low price elasticity. (Chapter 50-1-4, CBT Skill: Analysis, CSO: 2.3.0)

26. (b) Since the company is required to keep \$100,000 in the checking account as a compensating balance, then it is incurring a $\$100,000 \times 8\% = \$40,000$ interest cost on \$400,000 of accessible money. Therefore, the effective interest rate is the interest cost (\$40,000) divided by the principal (\$400,000) = 10%. (Chapter 51-4-1, CBT Skill: Analysis, CSO: 3.2.0)

27. (b) By definition, a database management system (DBMS) is a set of programs (software) that manages (i.e., creates, accesses, modifies) a database. Report customization can utilize the data in a DBMS, but is not the primary purpose of the DBMS. Financial transactions input is one use, but hardly a primary function of a DBMS. Access authorizations are control features, not primary functions. (Chapter 55-1-2, CBT Skill: Analysis, CSO: 4.3.1)

28. (b) A floating-rate bond has a variable interest rate. The interest rate is reset to equal the current market interest rate. Therefore, the market value of the bond itself will remain constant since that set price always will yield the current market rate. The market values of a zero-coupon bond, a callable bond, and a convertible bond will change as market interest rates fluctuate. (Chapter 51-3-1, CBT Skill: Judgment, CSO: 3.2.0)

29. (c) Segregation of functions among IT department personnel is a general internal control. An application programmer would code approved changes to a payroll program (application, not operating, software). System programmers modify operating systems. The user or computer operators correct data entry errors. A librarian maintains custody of programs and documentation. (Chapter 55-5-1, CBT Skill: Analysis, CSO: 4.2.2)

30. (d) All investment evaluation methods rely on the forecasting of future data. Except for the payback period, all consider the time value of money. Only the internal rate of return requires multiple trial and error calculations. The payback period does not

utilize a company's cost of capital. (Chapter 51-5-2, CBT Skill: Judgment, CSO: 3.1.3)

31. (d) The after-tax cost of bonds is $40\% \times 10\% = 4\%$. The after-tax cost of common stock is 10%. The after-tax cost of preferred stock is 20%. The company's weighted-average after-tax cost of capital is $(70\% \times 4\%) + (50\% \times 10\%) + (10\% \times 20\%) = 9.8\%$ (Chapter 51-5-3, CBT Skill: Analysis, CSO: 3.2.0)

32. (b) The payroll system is an application that processes transactions. (A transaction processing system). A DBMS and a DSS do not process transactions. An enterprise resource planning (ERP) system integrates multiple application programs as well as databases; it is not limited to just payroll functions. (Chapter 55-1-2, CBT Skill: Analysis, CSO: 4.1.2)

33. (d) Inventory turnover ratio = cost of goods sold / average inventory. Cost of goods sold (CGS) = annual sales $\$2,525,000 \times (100\% - 40\%) = \$1,515,000$. Beginning inventory (BI) = $15\% \times \$2,125,000 = \$318,750$. Ending inventory (EI) = $22\% \times \$2,525,000 = \$555,500$. Average inventory = $(BI \$318,750 + EI \$555,500) / 2 = \$437,125$. The company's inventory turnover at the end of the current period = $CGS \$1,515,000 / \text{average inventory } \$437,125 = 3.47$ (Chapter 54-3-2, see also Appendix D Financial Ratios, CBT Skill: Analysis, CSO: 5.2.1)

34. (a) The network administrator is responsible for maintaining the efficiency and effectiveness of the internal network including managing remote access. Application programmers develop application programs. The control group reviews security policy. System programmers install operating system upgrades. (Chapter 55-1-7, CBT Skill: Judgment, CSO: 4.2.1)

35. (d) A reasonableness check would be used to detect errors such as non-existent dates. The accuracy of mathematical calculations within programs generally is tested during development and implementation. Online prompting and preformatted screens are input controls, not edit checks. (Chapter 55-4-1, CBT Skill: Analysis, CSO: 4.2.1)

36. (c) Let Q = the number of cups needed to sell this year to break even.

$Q = \text{Fixed costs} / \text{contribution margin per cup}$

$\text{Fixed costs} = \$20,000 \times (\$7.50 - \$2.25) \times 110\% = \$115,500$

Contribution margin per cup = \$9.00 – (\$2.25 × 133.3%) = \$6.00

$Q = \$115,500 / \$6.00 = 19,250$ cups (Chapter 52-3-1, CBT Skill: Analysis, CSO: 5.2.1)

37. (b) A company generally should accept projects with returns greater than its weighted cost of capital.

Source	% of cap	cost of cap	weighted avg
LTD	60%	7.1%	4.26%
P/S	20%	10.5%	2.10%
C/S	20%	14.2%	2.84%
Composite			9.20%

(Chapter 51-5-3, CBT Skill: Analysis, CSO: 3.2.0)

38. (b) A limited liability company limits members' personal liability, allows all members to actively participate in the business, and passes all earnings through to the members proportionately, avoiding double taxation. C corporation profits are subject to double taxation. A limited partnership requires at least one general partner bearing unlimited personal liability. All partners in a general partnership bear unlimited personal liability. (Chapter 48-7-1, CBT Skill: Understanding, CSO: 1.1.2)

39. (c) The accounts receivable turnover ratio is calculated as net credit sales (\$103,200) / average net receivables [(\$14,600 + \$12,900) / 2 = \$13,750] = 7.5. Note: In the absence of further information, candidates must assume that all sales are credit sales. (Chapter 51-4-2, also see Appendix D Financial Ratios, CBT Skill: Understanding, CSO: 3.3.1)

40. (b) By definition, a cold site is a location where equipment and power is available in the event of disaster at the primary location, but requires considerable effort to become functional. A hot site is similar to a cold site, except it has constant operational system functionality. Back-up site procedures and a hot spare site agreement are not commonly used terms. (Chapter 55-4-2, CBT Skill: Understanding, CSO: 4.4.0)

41. (d) Preventive controls are distinguished by the fact that they prevent errors from occurring. Access control software ensures that only authorized personnel have access to the system programs and documentation. Contingency planning generally is not considered a control. An echo check is a detective control. A hash total is a detective control. (Chapter 55-5-4, CBT Skill: Judgment, CSO: 4.3.2)

42. (d) Managerial accounting is designed to meet the needs of the organization's internal parties.

Financial accounting is used for purposes external to the business. Financial accounting must adhere to GAAP and therefore utilizes defined historical cost principles. (Chapter 52-1-1, CBT Skill: Understanding, CSO: 5.2.1)

43. (c) Opportunity costs are the costs of not engaging in an alternative activity. Therefore, idle space that has no alternative use has an opportunity cost of zero. Opportunity costs are not actual dollar outlays and are not recorded in the accounts of an organization. Any potential benefit of the alternative activity is sacrificed. (Chapter 51-5-2, CBT Skill: Understanding, CSO: 3.1.2)

44. (d) To answer this question, the candidate must assume material handling and quality inspection costs are fixed. Fixed costs per hour = (\$120,000 + \$200,000) / 80,000 = \$4.00 per hour.

Estimated product cost of the proposed job is

Direct materials	\$ 4,000
Direct labor	6,000
Fixed costs (\$4.00 × 2,000 hrs)	<u>8,000</u>
Total estimated costs	\$18,000

(Chapter 53-5-2, CBT Skill: Analysis, CSO: 5.3.2)

45. (a) Limited partners lose their limited liability if they actively participate in management activities. A limited partnership must file a certificate with the state. Limited partners, unlike general partners, cannot actively participate in the management and control of the company and retain their liability protection. Consequently, limited partnerships typically have different rights and responsibilities for the different partner types. Limited partners may contribute services as their capital contributions. (Chapter 48-1-2, CBT Skill: Understanding, CSO: 1.1.1)

46. (b) Flexible budget amounts are typically not used when allocating costs for costing inventory in joint-cost situations. The relative market value method allocates costs based on their relative sales value at split-off. The net realizable value is defined as the difference between sales value and estimated costs to complete and sell. Allocating costs based on joint costs occasionally are allocated based on physical measures, but this approach generally is not preferred. (Chapter 53-4-2, CBT Skill: Understanding, CSO: 5.3.1)

47. (b) Residual income = operating income (\$400) – (required rate of return 10% × average capital \$1,600) = \$240. (The editors recognize that the explanation is coded as organizational performance measures. However, residual income is defined and discussed at length in the financial management

chapter.) (Chapter 51-5-5, CBT Skill: Analysis, CSO: 5.2.1)

48. (c) Benchmarking typically involves comparing a process being considered for improvement to an exemplary similar process at a different entity. Utilizing best practices, forecasts, and budgets are developed with internal information. (Chapter 54-3-4, CBT Skill: Understanding, CSO: 5.2.2)

49. (a) Under weighted average, computing the average current period costs will combine the beginning inventory costs with current period costs. Under FIFO, costs in the beginning inventory are not combined with the current period costs, but are transferred out as a separate batch of goods at a

different unit cost than units started and completed during the period. The weighted average and FIFO methods would result in equal unit costs if no beginning inventory exists. (Chapter 53-2-2, CBT Skill: Judgment, CSO: 5.3.2)

50. (c) Business continuity planning is the creation of a practiced logistical plan for recovering and restoring partially or completely interrupted critical operations within a predetermined time after a disaster or extended disruption. A business continuity plan typically would address issues such as network security, backup power, and daily backup of files. (Chapter 55-4-1, CBT Skill: Understanding, CSO: 4.4.0)