

***Managerial Accounting: Making Decisions and Motivating Performance (Datar/Rajan)***  
**Chapter 2 An Introduction to Cost Terms and Purposes**

Learning Objective 2-1

1) The cost incurred is:

- A) actual costs.
- B) budgeted costs.
- C) cost object.
- D) cost accumulation.
- E) cost allocation.

Answer: A

Diff: 1 Page Ref: 31

LO: 2-1

EOC: E2-1; E2-6

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) A \_\_\_\_\_ is usually measured as the amount of money that must be paid to acquire goods and services.

- A) time
- B) cost
- C) goal
- D) product
- E) prediction

Answer: B

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-10; E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

3) Which of the following explains why managers compare the budgeted costs to actual costs?

- A) Managers only focus on the budgeted costs.
- B) Managers only learn how to make better decisions in the future.
- C) Managers know how well they did to control costs only.
- D) Managers evaluate how well they did to control costs and learn how to do better in the future.
- E) Managers never compare these costs.

Answer: D

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-10; E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

4) The cost object is:

- A) the cost incurred.
- B) a collection of cost data in some organized way by means of a cost object.
- C) a predicted, or forecasted, cost.
- D) anything for which a measurement of costs is desired.
- E) used to describe the assignment of indirect costs to a particular cost object.

Answer: C

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-1

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

5) Budgeted costs include:

- A) the costs incurred this year.
- B) the costs incurred last year.
- C) the planned or forecasted costs.
- D) the cost of a competitor.
- E) the costs incurred two years ago.

Answer: C

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-6

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

6) Cost accumulation:

- A) is the cost incurred.
- B) is a collection of cost data in an organized way by means of a cost object.
- C) predicts, or forecasts, costs.
- D) measures the desired costs.
- E) describes the assignment of indirect costs to a particular cost object.

Answer: B

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-1

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

7) The two main ways managers use cost information are when they \_\_\_\_\_ decisions; and, \_\_\_\_\_ decisions.

- A) make; implement
- B) create; brainstorm
- C) control; create
- D) brainstorm; control
- E) control; accumulate

Answer: A

Diff: 2 Page Ref: 30

LO: 2-1

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

8) A/an \_\_\_\_\_ cost is the cost incurred; and they are distinguished from a \_\_\_\_\_ cost; which is a predicted, forecasted, or future cost.

- A) budget; object
- B) actual; budgeted
- C) accumulated; actual
- D) budgeted; actual
- E) cost object; actual

Answer: B

Diff: 3 Page Ref: 30

LO: 2-1

EOC: E2-10

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

9) The predicted, or forecasted costs, are:

- A) actual costs.
- B) budgeted costs.
- C) cost object.
- D) cost accumulation.
- E) cost allocation.

Answer: B

Diff: 1 Page Ref: 31

LO: 2-1

EOC: E2-1

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

10) Evans Manufacturing has three cost objects that it uses to accumulate costs for its manufacturing plant in Virginia. They include:

Cost Object #1: The real estate dwelling(s) (physical buildings and equipment)

Cost Object #2: The use of buildings and equipment

Cost Object #3: The use and availability of manufacturing labor

The following manufacturing overhead cost categories are found in the accounting records:

- a. Depreciation on buildings and equipment
- b. Machine lubricants
- c. Insurance for property
- d. Supervisors salaries
- e. Fringe benefits
- f. Property taxes
- g. Utilities

Required:

Assign each of the above costs to the most appropriate cost object.

Answer:

Cost Object #1 includes categories a, c and f

Cost Object #2 includes categories b and g

Cost Object #3 includes categories d and e

Diff: 2 Page Ref: 30

LO: 2-1

EOC: E2-14

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

11) A BMW X6 sports activity coupe is an example of the \_\_\_\_\_ cost object at BMW.

- A) product
- B) service
- C) project
- D) customer
- E) activity

Answer: A

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-1

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

12) Accountants measure the cost of direct materials or advertising at manufacturing plants by using the monetary amount paid to acquire them.

Answer: TRUE

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-10

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

13) Budgeted costs are also known as predicted or forecasted costs (future costs).

Answer: TRUE

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-11; E2-12; E2-13

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

14) Managers use their knowledge about costs to help guide their decisions about product innovation, quality, and customer service.

Answer: TRUE

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-18

AACSB: Reflective Thinking Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

15) The managers at BMW utilize their knowledge about costs to make decisions about product innovation, quality, and customer service.

Answer: TRUE

Diff: 1 Page Ref: 30

LO: 2-1

EOC: E2-1

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

16) Recall that managers use a cost system to determine the costs of various cost objects. List and discuss how managers use the two basic stages in this process to determine the cost.

Answer: The two stages that managers use are accumulation and assignment. In the first stage, managers accumulate costs. For example, they collect, or accumulate, the cost data that they use in an accounting system. In the second stage, assignment, managers assign the accumulated costs in various categories.

Diff: 2 Page Ref: 30

LO: 2-1

EOC: E2-1

AACSB: Reflective Thinking Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

## Learning Objective 2-2

1) The general term used to identify the tracing and allocation of accumulated costs to a cost object is:

- A) cost accumulation.
- B) cost assignment.
- C) cost tracing.
- D) conversion costing.
- E) convertible costing.

Answer: B

Diff: 2 Page Ref: 31

LO: 2-2

EOC: E2-1

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) Cost tracing:

- A) describes the assignment of direct costs to a particular cost object.
- B) is the cost incurred which is a predicted or forecasted cost.
- C) is the collection of data in some organized way.
- D) is used to describe the assignment of indirect costs to a particular cost object.
- E) encompasses both cost tracing and allocating indirect costs to a cost object.

Answer: A

Diff: 3 Page Ref: 31

LO: 2-2

EOC: E2-12; E2-13; E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

3) Which of the following is correct about indirect costs of a cost object?

- A) Cost allocation is not used to describe the assignment of these costs to a particular cost object.
- B) Cost tracing is used to describe its assignment of these costs to a particular cost object.
- C) Can be traced to a cost object in an economically feasible way.
- D) Cannot be traced to a cost object in an economically feasible way.
- E) Cost assignment is not used in indirect costing methods.

Answer: C

Diff: 3 Page Ref: 31

LO: 2-2

EOC: E2-12; E2-13; E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

4) The broader definition of a cost object is:

- A) the higher proportion of costs that are direct costs and the managers are more confident in the accuracy of the cost amounts.
- B) the lower proportion of costs that are direct costs and the managers are more confident in the accuracy of the cost amounts.
- C) the higher proportion of costs that are indirect costs and the managers are less confident in the accuracy of cost amounts.
- D) the lower proportion of costs that are indirect costs and the managers are less confident in the accuracy of cost amounts.
- E) the managers are never confident in the accuracy of cost amounts.

Answer: A

Diff: 3 Page Ref: 32

LO: 2-2

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

5) Which of the following is **not** a challenge to managers that allocate costs?

- A) Assign inaccurate product costs.
- B) Inaccurate product costs mislead managers about the profitability of products.
- C) Managers will promote unprofitable products.
- D) Managers deemphasize profitable products.
- E) Assign accurate product costs.

Answer: E

Diff: 3 Page Ref: 31

LO: 2-2

EOC: E2-12; E2-13; E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

6) Which of the following statements about the direct or indirect cost classification is **not** true?

- A) Indirect costs are always traced.
- B) Indirect costs are always allocated.
- C) The design of operations affects the direct or indirect cost classification.
- D) The direct/indirect classification depends on the choice of the cost object.
- E) All of these statements are true.

Answer: A

Diff: 2 Page Ref: 31

LO: 2-2

EOC: E2-11

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

7) We define cost tracing as:

- A) the assignment of direct costs to a chosen cost object.
- B) a function of cost allocation.
- C) the process of tracking both direct and indirect costs associated with a cost object.
- D) the process of determining the actual cost of the cost object.
- E) the process of tracking only the direct and indirect costs.

Answer: A

Diff: 1 Page Ref: 31

LO: 2-2

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

8) We define cost allocation as:

- A) the process of tracking both direct and indirect costs associated with a cost object.
- B) the process of determining the actual cost of the cost object.
- C) the assignment of indirect costs to the chosen cost object.
- D) a function of cost tracing.
- E) not a function of cost assignment.

Answer: C

Diff: 2 Page Ref: 31

LO: 2-2

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

9) Indirect costs of a cost object can be traced to a specific cost object and direct costs of a cost object cannot be traced to a specific cost object.

Answer: FALSE

Explanation: Indirect costs of a cost object are related to the particular cost object but cannot be traced to it in an economically feasible way. Direct costs of a cost object are related to the particular cost object and can be traced to it in an economically feasible way.

Diff: 1 Page Ref: 31

LO: 2-2

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

10) Cost tracing is used to describe the assignment of indirect costs to a particular cost object.

Answer: FALSE

Explanation: The term cost tracing is used to describe the assignment of direct costs to a particular cost object.

Diff: 2 Page Ref: 31

LO: 2-2

EOC: E2-18; E2-19

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.



11) One highlight of indirect costs of a cost object is that it can be traced in an economically feasible way.

Answer: FALSE

Explanation: Indirect costs of a cost object are related to the particular cost object but cannot be traced to it in an economically feasible way.

Diff: 2 Page Ref: 31

LO: 2-2

EOC: E2-18; E2-19

AACSB: Reflective Thinking Skills

Learning Outcome: MA-2: Describe the components of and prepare the four basic financial statements.

12) The cost of steel and tires to an automobile manufacturer is an example of a direct cost.

Answer: TRUE

Diff: 1 Page Ref: 31

LO: 2-2

EOC: E2-19

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

13) Ford Motor Company is an example of a plant that manufactures automobiles. The cost of the lease where it manufactures automobiles can be categorized as an indirect cost.

Answer: TRUE

Diff: 2 Page Ref: 31

LO: 2-2

EOC: E2-11

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

14) In general, a manager is more confident about the accuracy of direct costs of cost objects.

Answer: TRUE

Diff: 2 Page Ref: 31

LO: 2-2

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

15) The plant administrative costs at a manufacturing company are indirect costs.

Answer: TRUE

Diff: 1 Page Ref: 31

LO: 2-2

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

16) Write a short essay and explain why a manager at a manufacturing company considers the direct costs to be more accurate than indirect costs.

Answer: Managers at manufacturing companies consider the direct costs to be more accurate than indirect costs because they can be traced to a specific or particular cost object. Indirect costs, for example, the salaries of administrative personnel at a manufacturing company, can't be traced to a specific cost object.

Diff: 3 Page Ref: 31

LO: 2-2

EOC: E2-11; E2-14

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

17) Write a short essay and explain how technological advances have improved the accounting or finance manager's ability to track costs. Be specific.

Answer: Managers enjoy the advances in information-gathering technology because it enhances their ability to trace direct costs. The development of bar codes now permit managers to classify low-cost products, for example, clips and screws that were previously classified as indirect costs.

Diff: 2 Page Ref: 32

LO: 2-2

EOC: E2-11

AACSB: Use of Information Technology

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

18) Write a short essay and explain why it is important for managers to assign costs accurately to cost objects. What are some of the challenges that managers face when they allocate costs to cost objects?

Answer: It is important for managers to assign costs accurately to cost objects because the data reported and assigned to the product will not be accurate. Inaccurate product costs results in the inaccurate profitability of different products. As a result, the manager may select to promote the unprofitable product instead of the profitable product. If costs are consistently inaccurate it could affect the long-term profit forecast of the product.

One challenge to a manager is the allocation of indirect administrative costs. Managers must decide whether the administrative costs are calculated by the number or products produced or by the number of administrative workers that produce the product.

Diff: 3 Page Ref: 31-32

LO: 2-2

EOC: E2-10

AACSB: Analytic Skills

Learning Outcome: MA-2: Describe the components of and prepare the four basic financial statements.

19) Write a short essay and discuss some of the factors that affect the classification of direct and indirect costs.

Answer: Some of the factors that affect the classification of direct and indirect costs include the materiality of the cost in question, the available technology used to gather information, and the design of the operations. In addition, managers must learn to make logical decisions based on the cost object depending on the purpose of the cost because in certain cases, a cost could be classified as a direct cost or an indirect cost.

Diff: 2 Page Ref: 32

LO: 2-2

EOC: E2-11

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

20) Write a brief summary and discuss why cost allocation is important to a manager. Discuss some of the challenges that managers face when they allocate costs and discuss those factors that affect the direct/indirect cost classification. Be specific.

Answer: Cost allocation is important to a manager because they must assign costs accurately to a cost object. Managers are challenged to ensure costs are appropriately allocated to a product. For example, if the product costs are not accurate, the true profitability to products is distorted. As a result, a manager could sell a product that should not be sold because it is not profitable to the company.

Some of the factors that affect cost classification include the materiality of the cost in question, the amount of available information-gathering technology, and the product design.

Diff: 3 Page Ref: 31

LO: 2-2

EOC: E2-10; E2-11

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

## Learning Objective 2-3

1) The costing systems that managers use to identify the cost of each activity such as testing, design, or set-up are called:

- A) product-based costing systems.
- B) action-based costing systems.
- C) managerial-based costing systems.
- D) activity-based costing systems.
- E) resource-based costing systems.

Answer: D

Diff: 3 Page Ref: 35

LO: 2-3

EOC: E2-12; E2-13; E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) Financial accountants realize that a mixed cost is:

- A) a fixed cost.
- B) a cost with fixed and variable elements.
- C) a variable cost.
- D) always an indirect cost.
- E) only an indirect cost.

Answer: B

Diff: 1 Page Ref: 35

LO: 2-3

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

3) An example of a mixed cost is:

- A) monthly rent payments.
- B) manager's salary.
- C) monthly electric bill.
- D) direct materials.
- E) none of these are mixed costs.

Answer: C

Diff: 2 Page Ref: 35

LO: 2-3

EOC: E2-3

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

4) Fixed and variable costs:

- A) always change in the same proportion.
- B) are defined as variable or fixed for a specific activity for a given time period.
- C) are only defined for a specific activity and never for a given period of time.
- D) are only defined for a given period of time and not for a specific activity.
- E) are never useful to managers when they make cost decisions.

Answer: B

Diff: 3 Page Ref: 35

LO: 2-3

EOC: E2-15; E2-16; E2-17

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

5) Which of the following is **not** a true statement about variable costs?

- A) A total cost that can change in proportion to changes in the number of product produced.
- B) An important cost to identify so managers can make important management decisions.
- C) Total cost never changes in proportion to any changes in related levels of volume or activity.
- D) When considering total cost behavior, focus on total costs.
- E) Total cost is known to change in proportion to any changes in related level of volume or activity.

Answer: C

Diff: 3 Page Ref: 32

LO: 2-3

EOC: E2-15; E2-16; E2-17

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

6) A band of normal activity or volume in which specific cost-volume relationships are maintained is referred to as the:

- A) average range.
- B) cost-allocation range.
- C) cost drive range.
- D) relevant range.
- E) driving range.

Answer: D

Diff: 1 Page Ref: 35

LO: 2-3

EOC: E2-17

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

7) If each motorcycle requires a fan belt that costs \$20 and 2,000 motorcycles are produced in the month, the total cost for the fan belts is:

- A) considered to be a fixed cost.
- B) considered to be a direct variable cost.
- C) considered to be an indirect fixed cost.
- D) considered to be an indirect variable cost.
- E) none of these are true.

Answer: B

Diff: 3 Page Ref: 33

LO: 2-3

EOC: E2-20

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

8) Answer the question using the information provided below:

Number of Custom Carburetors Produced	Variable Cost Per Custom Carburetors	Total Fixed Cost Per Custom Carburetor
(1)	(2)	(3)
1	\$50	\$50
500	50	
1000	50	

The manager at the Carburetor Factory buys a custom carburetor at \$50.00 each for each of its custom vehicles. Compute the total fixed cost per custom carburetor if 1, 500, and 1,000 custom carburetors are produced.

- A) \$25,000; \$50,000
- B) \$30,000; \$60,000
- C) \$35,000; \$70,000
- D) \$40,000; \$45,000
- E) \$45,000; \$90,000

Answer: A

Explanation: A) Total cost changes in proportion to the changes of the number of units produced

Number of Custom Carburetors Produced	Variable Cost Per Custom Carburetors	Total Fixed Cost Per Custom Carburetor
(1)	(2)	(3) = 1 × 2
1	\$50	\$50
500	50	\$25,000
1000	50	\$50,000

Diff: 2 Page Ref: 33

LO: 2-3

EOC: E2-3

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

9) Answer the question below using the following information:

Annual Total Fixed Supervision Costs for Carburetor Assembly Line (1)	Number of Carburetors Produced (2)	Fixed Supervision Cost Per Custom Carburetor (3)
\$2,500,000	5,000	
\$2,500,000	10,000	
\$2,500,000	15,000	

Required:

Compute the fixed supervision cost per custom carburetor for 5,000, 10,000, and 15,000 carburetors produced.

- A) \$250; \$300
- B) \$250; \$166.66
- C) \$150; \$100
- D) \$200; \$300
- E) \$50; \$25

Answer: B

Explanation: B) Fixed costs become smaller and smaller on a per-unit basis as the number of vehicles assembled increase.

Annual Total Fixed Supervision Costs for Carburetor Assembly Line (1)	Number of Carburetors Produced (2)	Fixed Supervision Cost Per Custom Carburetor (3) = (1) ÷ (2)
\$2,500,000	5,000	\$500
\$2,500,000	10,000	\$250
\$2,500,000	15,000	\$166.66

Diff: 3 Page Ref: 33

LO: 2-3

EOC: E2-3

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

10) The managerial accountant at Sahara Organizations matches business functions to cost drivers. The list below provides representative cost drivers in the right column are randomized with respect to the list of functions in the left column [Note: These are not matched to the respective cost driver].

	Business Function			Representative Cost Driver
1	Billing		A	Number of shipments
2	Purchasing		B	Number of employees
3	Shipping		C	Number of customers
4	Computer Support		D	Number of invoices
5	Personnel		E	Number of desktop computers
6	Customer Service		F	Number of purchase orders

Numbers 1-6 represent the Business Functions and the letters A-F represent the cost drivers at the company.

Required:

Insert the letter of the appropriate cost driver (A through F) and match each business function with its appropriate cost driver.

	FUNCTION	Insert letter of appropriate cost driver (Letters A-F)
1	Billing	
2	Purchasing	
3	Shipping	
4	Computer Support	
5	Personnel	
6	Customer Services	

Answer: D, F, A, E, B, C

Explanation:

	FUNCTION	Insert letter of appropriate cost driver (Letters A-F)
1	Billing	D
2	Purchasing	F
3	Shipping	A
4	Computer Support	E
5	Personnel	B
6	Customer Services	C

Diff: 2 Page Ref: 35

LO: 2-3

EOC: E2-4

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.



11) A manager at an airline must purchase individual annual licenses and pay registration costs for each airplane in the fleet of airplanes they operate at the airport. What type of cost is/are the registration and license costs for the miles flown each year for each individual airplane?

- A) Fixed and variable cost for the miles flown by each individual plane.
- B) Mixed cost for the miles flown by all planes each year.
- C) Fixed cost for the miles flown by each individual plane.
- D) Variable cost for the miles flown by each individual plane.
- E) Licenses and registrations are not considered costs to the airline.

Answer: C

Diff: 3 Page Ref: 39

LO: 2-3

EOC: E2-16; E2-21

AACSB: Analytic Skills

Learning Outcome: MA-2: Describe the components of and prepare the four basic financial statements.

12) Costs are defined as variable or fixed for a specific activity and for a given time period.

Answer: TRUE

Diff: 1 Page Ref: 32

LO: 2-3

EOC: E2-11; E2-12; E2-13; E2-14; E2-15; E2-16

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

13) Fixed costs can be changed quickly to match the amount of resources that are needed or used in the organization.

Answer: FALSE

Explanation: Unlike variable costs, fixed costs of resources cannot be quickly and easily changed to match the resources needed or used.

Diff: 2 Page Ref: 34

LO: 2-3

EOC: E2-11

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

14) Costs that have both fixed and variable elements are called mixed costs or semivariable costs.

Answer: TRUE

Diff: 1 Page Ref: 35

LO: 2-3

EOC: E2-15; E2-16; E2-17

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

15) Outside the relevant range, variable costs, such as direct materials, may **not** change proportionately with changes in production volume.

Answer: TRUE

Diff: 2 Page Ref: 36

LO: 2-3

EOC: E2-5; E2-16; E2-17

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

16) Write a short essay and explain how managers differentiate between fixed costs and variable costs.

Answer: Managers understand that total fixed costs do not change in the time-period observed despite the changes in the level of activity or volume. However, the variable costs do change in proportion to changes in the total level of activity or volume.

Diff: 2 Page Ref: 32

LO: 2-3

EOC: E2-11; E2-15; E2-16; E2-17

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

17) Write a short essay and discuss whether or not managers should assume that individual cost items are inherently fixed or variable? Why are some costs fixed and other costs variable costs?

Answer: No, managers should never assume that individual cost items are inherently fixed or variable. For example, a labor cost can be a variable cost for the units produced when those workers are paid on a piece-rate, or piece-unit, basis. Forecasted labor costs at a plant could be considered a fixed cost in the next fiscal accounting period.

Diff: 2 Page Ref: 34

LO: 2-3

EOC: E2-20

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

18) Write a brief summary and explain how the impact of a financial crisis impacts how managers at global companies account for fixed costs. Be specific.

Answer: Managers that work at global companies are reluctant to lock in fixed costs. Certain policies could increase the risk of losses during economic downturns. In addition, if there is a decrease in revenues that result from an economic crisis, the fixed costs remain unchanged. If there is a decrease in the revenues, it will prevent problems in the organization.

Diff: 3 Page Ref: 34

LO: 2-3

EOC: E2-11

AACSB: Dynamics of the Global Economy

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

19) Write an essay and define relevant range. Discuss what the relevant range is and explain why it is important to managers?

Answer: The relevant range is known as the band or range of normal activity level or volume in which there is a specific relationship between the level of activity or volume and the cost in question. Managers are concerned about the relevant range because it is known as the region of activity where a particular relationship holds between a driver and a cost. Managers also observe variable costs because they many not change in proportion to changes in volume.

Diff: 2 Page Ref: 35

LO: 2-3

EOC: E2-17; E2-18

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

## Learning Objective 2-4

1) Which of the following is **not** true about unit costs?

- A) Decision makers think in terms of total costs rather than unit costs.
- B) Decision makers think in terms of unit costs rather than total costs.
- C) Calculating unit cost is essential.
- D) Unit costs are also known as average costs.
- E) Managers can express costs in various ways.

Answer: B

Diff: 2 Page Ref: 37

LO: 2-4

EOC: E2-20; E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) Managers compute the unit cost by:

- A) multiplying total cost by the number of units.
- B) dividing total cost by the number of units.
- C) dividing variable cost by the number of units.
- D) adding variable cost to fixed cost.
- E) adding variable, direct, and indirect costs.

Answer: B

Diff: 2 Page Ref: 37

LO: 2-4

EOC: E2-20; E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

- 3) Unit costs are found in:
- A) only the production department.
  - B) only the sales department.
  - C) all areas of the value chain.
  - D) only in the marketing department.
  - E) only in the human resource department.

Answer: C

Diff: 2 Page Ref: 37

LO: 2-4

EOC: E2-6

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

- 4) When 40,000 units are produced, fixed costs are \$16 per unit. Therefore, when 80,000 units are produced, fixed costs will:
- A) increase to \$32 per unit.
  - B) remain at \$16 per unit.
  - C) decrease to \$8 per unit.
  - D) total \$640,000.
  - E) total \$540,000.

Answer: C

Diff: 3 Page Ref: 37-38

LO: 2-4

EOC: E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

- 5) When 5,000 units are produced, variable costs are \$6 per unit. Therefore, when 20,000 units are produced:
- A) variable costs will total \$120,000.
  - B) variable costs will total \$60,000.
  - C) variable unit costs will increase to \$12 per unit.
  - D) variable unit costs will decrease to \$3 per unit.
  - E) variable costs will decrease to \$2 per unit.

Answer: A

Diff: 3 Page Ref: 38

LO: 2-4

EOC: E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

- 6) Accounting systems report:
- A) only the total cost amounts.
  - B) only the average-cost per unit amounts.
  - C) both total-cost amounts and average-cost per unit amounts.
  - D) only average costs.
  - E) no cost amount data.

Answer: C

Diff: 2 Page Ref: 37

LO: 2-4

EOC: E2-18

AACSB: Use of Information Technology

Learning Outcome: MA-2: Describe the components of and prepare the four basic financial statements.

7) As a general rule, managers first calculate total costs, and then compute which of the following costs when they need to make decisions?

- A) A direct cost.
- B) A unit cost.
- C) A variable cost.
- D) An indirect cost.
- E) A cost driver.

Answer: B

Diff: 3 Page Ref: 38

LO: 2-4

EOC: E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

8) Acme Candle Company reported the following information:

Manufacturing costs	\$1,500,000
Units Manufactured	300,000
Units sold (60,000 units sold at \$25 per unit)	\$1,500,000
Beginning inventory	0 units

Required:

Compute the average manufacturing cost per unit.

- A) \$1.00
- B) \$1.75
- C) \$2.95
- D) \$4.50
- E) \$5.00

Answer: E

Explanation: E)  $(\$1,500,000 / 300,000) = \$5$  per unit

Diff: 2 Page Ref: 37-38

LO: 2-4

EOC: E2-33

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

9) Jim's Manufacturing currently produces 1,250 brakes per month. The following per unit data apply for sales to regular customers:

Direct materials	\$225
Direct manufacturing labor	28
Variable manufacturing overhead	50
Fixed manufacturing overhead	35
Total manufacturing costs	<u>\$338</u>

The plant has capacity for 2,000 brakes.

**Required:**

- What is the total cost of producing 1,000 brakes?
- What is the total cost of producing 1,500 brakes?
- What is the per-unit cost when producing 1,500 brakes?

Answer:

- $[(\$225 + \$28 + \$50) \times 1,000 \text{ units}] + (\$35 \times 1,250 \text{ units}) = \$346,750$
- $[(\$225 + \$28 + \$50) \times 1,500 \text{ units}] + \$43,750 = \$498,250$
- $(\$498,250 \div 1,500) = \$332.16 \text{ per unit}$

Diff: 2 Page Ref: 38

LO: 2-4

EOC: E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

10) During 2011, Maryland Corporation incurred manufacturing expenses of \$15,000,000 to produce 300,000 finished units. At year-end, it was determined that 250,000 units were sold while 25,000 units remained in ending inventory.

**Required:**

- Compute the cost to produce one unit.
- Compute the amount that will be reported on the income statement for cost of goods sold.
- Compute the amount that will be reported on the balance sheet for ending inventory.

Answer:

- $\$15,000,000 \div 300,000 = \$50.00$
- $250,000 \text{ units} \times \$50 = \$12,500,000$
- $25,000 \text{ units} \times \$50 = \$1,250,000$

Diff: 2 Page Ref: 37-38

LO: 2-4

EOC: E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

11) Managers should think in terms of unit costs rather than terms of total costs for many decisions.

Answer: FALSE

Explanation: Managers should think in terms of total costs rather than terms of total costs for many decisions.

Diff: 2 Page Ref: 38

LO: 2-4

EOC: E2-20; E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

12) The unit cost, or average cost, is the ratio of total costs to the number of units produced.

Answer: TRUE

Diff: 1 Page Ref: 38

LO: 2-4

EOC: E2-20

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

13) Write a short essay and discuss how unit costs are calculated. Discuss how unit costs are related to the value chain.

Answer: Unit costs are also known as the average cost. Unit costs can be calculated by dividing total cost by the related number of units. Unit costs are directly related to the value chain because they can be summed in all areas of the value chain. Managers can sum unit costs of different products and services and determine whether or not the product or service is profitable. This information is useful to managers because they use the information to determine which products that they will invest more resources in and the prices that they can charge for the products and services.

Diff: 3 Page Ref: 37

LO: 2-4

EOC: E2-18; E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

## Learning Objective 2-5

1) Which of the following is **not** a characteristic of the type of inventory used in manufacturing-type sector companies?

- A) Direct materials inventory.
- B) Work-in process inventory.
- C) Finished goods inventory.
- D) Materials in stock and waiting to use.
- E) Products already manufactured and sold.

Answer: E

Diff: 2 Page Ref: 38

LO: 2-5

EOC: E2-13

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) Which of the following is **not** a commonly used classification or characteristic of manufacturing costs?

- A) Direct material costs.
- B) Direct manufacturing labor costs.
- C) Indirect manufacturing costs.
- D) Freight-in charges.
- E) Cost of goods sold.

Answer: E

Diff: 2 Page Ref: 39

LO: 2-5

EOC: E2-13

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

3) All costs of a product that are considered as assets in the balance sheet when they are incurred and that become cost of goods sold only when the product is sold are:

Answer: inventoriable costs.

Diff: 2 Page Ref: 39

LO: 2-5

EOC: E2-22

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

4) Which of the following is normally included in direct materials inventory?

- A) Direct materials in stock and awaiting use in the manufacturing process.
- B) Goods partially worked on but not yet fully completed.
- C) Goods fully completed but not yet sold.
- D) Products in their original form intended to be sold without changing their basic form.
- E) Goods and products that have been completed and sold.

Answer: A

Diff: 1 Page Ref: 39

LO: 2-5

EOC: E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.



5) In finished goods inventory:

- A) direct materials are in stock and awaiting use in the manufacturing process.
- B) goods are partially worked on but not yet fully completed.
- C) goods are fully completed but not yet sold.
- D) products are in their original form intended to be sold but the basic form is changed basic form.
- E) goods are partially completed and sold as is.

Answer: C

Diff: 1 Page Ref: 39

LO: 2-5

EOC: E2-13

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

6) Manufacturing-sector companies purchase materials and components and convert them into various finished goods.

Answer: TRUE

Diff: 1 Page Ref: 38

LO: 2-5

EOC: E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

7) Merchandising-sector companies purchase and then sell tangible products without changing their basic form.

Answer: TRUE

Diff: 1 Page Ref: 38

LO: 2-5

EOC: E2-13

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

8) Service-sector companies are known as companies that provide products to its customers.

Answer: FALSE

Explanation: Service-sector companies provide services to its customers.

Diff: 1 Page Ref: 39

LO: 2-5

EOC: E2-12

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

9) Service-sector companies only provide services or intangible products and so do **not** hold inventories of tangible products.

Answer: TRUE

Diff: 2 Page Ref: 39

LO: 2-5

EOC: E2-12

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

10) Write a brief summary and explain why managers account for inventoriable and period costs. Explain the differences between inventoriable and period costs.

Answer: The inventoriable costs are all costs of a product that a firm regards as an asset in the accounting period when they incurred. They become a cost of the goods sold in the accounting period when the product is sold.

Managers expense period costs in the accounting period that they are incurred. All of the costs in an income statement with the exception of cost of goods sold.

Diff: 2 Page Ref: 39

LO: 2-5

EOC: E2-22

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

11) Write a brief essay and discuss how manufacturing-sector companies inventory their products.

Answer: Manufacturing-sector companies purchase materials and components and convert them into finished goods. Typically, manufacturing-sector companies have three types of inventory. (1) Direct materials inventory is used to account for direct materials that managers keep in stock when they are waiting to use them in the manufacturing process, (2) Work-in process inventory, also known as work-in process inventory, is used to account for goods that are worked on but not completed, and, (3) Finished goods inventory is used to account for goods that are completed but not sold.

Diff: 3 Page Ref: 39

LO: 2-5

EOC: E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

12) Write a short essay and explain how managers classify manufacturing costs.

Answer: There are three ways that managers classify manufacturing costs. They are (1) Direct material cost is the acquisition costs of all materials that become part of the cost object. They include freight-in charges, sales taxes, and customs duties (2) Direct manufacturing labor costs include the compensation of manufacturing labor that managers trace to the cost object. They include wages or fringe benefits paid to machine operators and assembly-line workers who convert direct materials purchased to finished goods, and (3) Indirect manufacturing costs. These include all manufacturing costs that are related to the cost object but cannot be traced to the cost object. These include supplies, indirect materials, indirect manufacturing labor, plant rent and insurance, plant property taxes, plant depreciation, and the compensation of plant managers.

Diff: 2 Page Ref: 39

LO: 2-5

EOC: E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

## Learning Objective 2-6

1) The term that refers to the cost of goods brought to completion, whether they were started before or during the accounting period is:

- A) cost of goods sold.
- B) cost of goods produced.
- C) cost of goods insured.
- D) cost of goods serviced.
- E) cost of goods manufactured.

Answer: E

Diff: 2 Page Ref: 43

LO: 2-6

EOC: E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) The cost of goods sold is the cost of finished goods inventory sold to customers:

- A) before the previous accounting period.
- B) after the previous accounting period.
- C) during a future accounting period.
- D) during the current accounting period.
- E) during the previous accounting period.

Answer: D

Diff: 2 Page Ref: 43

LO: 2-6

EOC: E2-14; E2-23; E2-24

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

3) When are inventoried unit costs expensed?

- A) Unit costs are never expensed.
- B) Expensed before units are sold.
- C) Not expensed until the units are sold.
- D) Expensed when they are in production.
- E) These costs are period costs not unit costs.

Answer: C

Diff: 3 Page Ref: 44

LO: 2-6

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

4) The Material Handler company reported the following information:

Beginning inventory of direct materials, January 1, 2012	\$15,000
Purchases of direct materials in 2012	70,000
Ending inventory of direct materials, December 31, 2012	<u>7,000</u>

Required:

Compute the Total Cost of Direct Materials used in 2012

- A) \$64,000
- B) \$72,000
- C) \$78,000
- D) \$82,000
- E) \$86,000

Answer: C

Explanation: C)  $[(\$15,000 + \$70,000) - \$7,000] = \$78,000$

Diff: 3 Page Ref: 41

LO: 2-6

EOC: E2-11

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

5) Compute the Total Manufacturing Costs incurred from the data provided by Wize Manufacturing.

Direct materials used in 2012	\$60,000
Direct manufacturing labor in 2012	10,000
Manufacturing overhead costs in 2012	<u>18,500</u>

- A) \$85,000
- B) \$88,500
- C) \$102,500
- D) \$107,300
- E) \$110,000

Answer: B

Explanation: B)  $[(\$60,000 + \$10,000 + \$18,500)] = \$88,500$  total manufacturing costs

Diff: 1 Page Ref: 43

LO: 2-6

EOC: E2-13

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

6) Ice Manufacturing reported the following information:

Beginning work-in-process inventory	\$60,000
Ending work-in-process inventory	58,000
Beginning finished goods inventory	160,000
Ending finished goods inventory	180,000
Cost of goods manufactured	1,200,000

**Required:**

Compute the cost of goods sold.

- A) \$1,000,000
- B) \$1,180,000
- C) \$1,450,000
- D) \$1,540,000
- E) \$1,680,000

Answer: B

Explanation: B) [ $\$160,000 + \$1,200,000 - \$180,000$ ] = \$1,180,000

Diff: 3 Page Ref: 43

LO: 2-6

EOC: E2-23

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

7) Wize Manufacturing reported the following information:

Finished goods inventory	\$40,000
Cost of goods manufactured	105,000
Ending inventory of finished goods	<u>15,000</u>

Required:

Compute the cost of goods sold.

- A) \$120,000
- B) \$125,000
- C) \$130,000
- D) \$135,000
- E) \$140,000

Answer: C

Explanation: C) [ $40,000 + 105,000 - 15,000$ ] = \$130,000

Diff: 3 Page Ref: 43

LO: 2-6

EOC: E2-23; E2-24

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

8) Managers compute the cost of goods sold in a manufacturing entity as:

A) beginning work-in-process inventory + Cost of goods manufactured - Ending work-in-process inventory = Cost of goods sold.

B) beginning work-in-process inventory + Cost of goods manufactured + Ending work-in-process inventory = Cost of goods sold.

C) cost of goods manufactured - Beginning finished goods inventory - Ending finished goods inventory = Cost of goods sold.

D) cost of goods manufactured + Beginning finished goods inventory - Ending finished goods inventory = Cost of goods sold.

E) cost of goods manufactured - Beginning finished goods inventory + Ending work-in-process inventory = Cost of goods sold.

Answer: D

Diff: 2 Page Ref: 43

LO: 2-6

EOC: E2-14

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

9) Wagner Company reported the following information about revenues and the cost of goods sold:

Revenues	\$250,000
Cost of Goods Sold	<u>\$75,000</u>

Required:

Compute the gross margin.

A) \$100,000

B) \$125,000

C) \$150,000

D) \$175,000

E) \$200,000

Answer: D

Explanation: D) [(\$250,000 - \$75,000) = \$175,000

Diff: 3 Page Ref: 43

LO: 2-6

EOC: E2-19

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

10) Isaac Manufacturing reported the following information for the previous month:

Sales	\$75,000
Variable Costs	5,000
Fixed Costs	<u>11,000</u>
Operating Income	59,000

Required:

Compute the projected operating income if sales doubled in the next month.

- A) \$99,000
- B) \$109,000
- C) \$119,000
- D) \$129,000
- E) \$139,000

Answer: D

Explanation: D)  $[(\$75,000 \times 2) - (\$5,000 \times 2) - 11,000] = \$129,000$

Diff: 3 Page Ref: 44

LO: 2-6

EOC: E2-33; E2-34

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

11) Carpenter Products Company manufactures office furniture. Recently, the company decided to develop a formal cost accounting system and classify all costs into three categories. Categorize each of the following items as being appropriate for (1) cost tracing to the finished furniture, (2) cost allocation of an indirect manufacturing cost to the finished furniture, or (3) as a nonmanufacturing item.

<u>Item</u>	<u>Cost Tracing</u>	<u>Cost Allocation</u>	<u>Nonmanufacturing</u>
Carpenter wages	_____	_____	_____
Depreciation – office building	_____	_____	_____
Glue for assembly	_____	_____	_____
Lathe-department supervisor	_____	_____	_____
Lathe depreciation	_____	_____	_____
Lathe maintenance	_____	_____	_____
Lathe operator wages	_____	_____	_____
Lumber	_____	_____	_____
Samples for trade shows	_____	_____	_____
Metal brackets for drawers	_____	_____	_____
Factory washroom supplies	_____	_____	_____
Answer: Carpenter wages	X		
Depreciation-office building			X
Glue for assembly		X	
Lathe-department supervisor		X	
Lathe depreciation		X	
Lathe maintenance		X	
Lathe operator wages	X		
Lumber	X		
Samples for trade shows		X	
Metal brackets for drawers	X		
Factory washroom supplies		X	

Diff: 3 Page Ref: 44

LO: 2-6

EOC: E2-14

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

12) Indirect costs such as rent, telephone, and depreciation are always costs of the period in which they are incurred and are **not** associated with inventories.

Answer: TRUE

Explanation: Indirect costs such as rent, telephone, and depreciation are always costs of the period in which they are incurred and are not associated with inventories.

Diff: 3 Page Ref: 44

LO: 2-6

EOC: E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.



13) Under GAAP, only manufacturing costs can be assigned to inventories in the financial statements.

Answer: TRUE

Diff: 3 Page Ref: 48

LO: 2-6

EOC: E2-10; E2-17

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

14) The two terms that managers use to describe cost classifications in manufacturing costing systems are prime costs and conversion costs.

Answer: TRUE

Diff: 2 Page Ref: 46

LO: 2-6

EOC: E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

15) As information gathering technology improves, companies can add more and more direct-cost categories.

Answer: TRUE

Diff: 1 Page Ref: 46

LO: 2-6

EOC: E2-11; E2-18

AACSB: Use of Information Technology

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

16) Conversion costs represent all manufacturing costs incurred to convert direct materials into finished goods.

Answer: TRUE

Diff: 2 Page Ref: 46

LO: 2-6

EOC: E2-19; E2-20

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

17) Direct manufacturing labor costs are only a part of prime costs.

Answer: FALSE

Explanation: Direct manufacturing labor costs are a part of both prime and conversion costs.

Diff: 2 Page Ref: 46

LO: 2-6

EOC: E2-19; E2-20; E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

18) Write a short essay and explain why managers are concerned about the flow of inventoriable and period costs in manufacturing and merchandising settings. How do managers determine the flow of these costs?

Answer: Managers differentiate between the flow of inventoriable and period costs. The managers in manufacturing settings classify inventoriable costs as those costs that flow through work-in-process and the finished goods accounts. They are expensed as costs of goods sold.

Managers that work at merchandising firms only treat the cost of merchandise as an inventoriable cost or expense.

Diff: 1 Page Ref: 44

LO: 2-6

EOC: E2-22

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

19) Write an essay and discuss how technology has impacted a manager's ability to track direct costs. Be specific.

Answer: Technological advances have improved the manager's ability to track direct costs. Managers can add more cost categories that result in more accurate accounting of specific products. For example, some computer software manufacturing companies have enhanced the features of the technology. These companies added more manufacturing cost items so managers can trace specific costs. This results in more accurate accounting of direct costs at a firm.

Diff: 3 Page Ref: 46

LO: 2-6

EOC: E2-11

AACSB: Use of Information Technology

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

## Learning Objective 2-7

1) Which of the following is **not** a prominent labor component of overhead?

- A) Direct programming labor that cannot be traced to individual products.
- B) Indirect labor compensation for office staff.
- C) Indirect compensation for idle time.
- D) Indirect labor compensation for rework labor.
- E) Indirect labor compensation for office security.

Answer: A

Diff: 1 Page Ref: 46

LO: 2-7

EOC: E2-20; E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) The wage rate paid to workers (for both direct labor and indirect labor) in excess of their straight time wage rate is:

- A) idle time.
- B) straight-time.
- C) accelerated time.
- D) overtime premium.
- E) direct costing method.

Answer: D

Diff: 2 Page Ref: 47

LO: 2-7

EOC: E2-31

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

3) Mrs. Jones earns \$25.00 per hour for straight time worked in the office; and, she earns \$40.00 per hour when she works overtime. In week one of the new pay period, she reported that she worked 48 hours, which included 8 hours of overtime. Compute Mrs. Jones's total compensation:

- A) \$1,000
- B) \$1,220
- C) \$1,300
- D) \$1,320
- E) \$1,425

Answer: D

Explanation: D) [Direct labor (48 × 25) + Overtime premium (8 hours × 15)] = \$1,320.00

Diff: 2 Page Ref: 47

LO: 2-7

EOC: E2-31

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

4) Ms. Taylor works at an assembly plant that produces footballs. She earns \$18.00 an hour for straight-time and \$36 per hour when she works overtime. She reported that she worked 46 hours during the previous reporting period, which included 6 hours of overtime.

**Required:**

Compute the total compensation for the week; the amount of compensation that was reported as direct manufacturing labor; the amount of compensation that is reported as a manufacturing overhead cost.

- A) \$900; \$810; \$80
- B) \$926; \$822; \$88
- C) \$936; \$828; \$108
- D) \$942; \$832; \$116
- E) \$950; \$860; \$124

Answer: C

Explanation: C) Total Compensation: Direct Labor [(46 hours × \$18) + Overtime premium (6 hrs × \$18)] = \$936

Direct Manufacturing Labor [(46 hours × \$18)] = \$828

Manufacturing overhead costs = Overtime premium [(6 hrs × \$18)] = \$108

Diff: 3 Page Ref: 43-47

LO: 2-6, 2-7

EOC: E2-10; E2-25

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

5) Mr. Foxhound works at a manufacturing plant that makes balloons for holiday parades. He earns \$30 per hour for straight-time and \$50 per hour for overtime. One week he worked 46 hours, which included 6 hours of overtime, and 4 hours of idle time caused by a shortage of materials to make the balloons.

**Required:**

Compute Mr. Foxhound's total compensation for the week; the amount of compensation reported as direct manufacturing labor; and the amount of compensation that would be reported as manufacturing overhead.

- A) \$1,200; \$1,100; \$220
- B) \$1,250; \$1,200; \$160
- C) \$1,500; \$1,260; \$240
- D) \$1,600; \$1,280; \$260
- E) \$1,750; \$1,300; \$280

Answer: C

Diff: 3 Page Ref: 47

LO: 2-7

EOC: E2-31

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

6) For the purpose of calculating inventory, product costs include only:

- A) direct costs.
- B) indirect costs.
- C) variable costs.
- D) inventoriable (manufacturing) costs.
- E) mixed costs.

Answer: D

Diff: 2 Page Ref: 48

LO: 2-7

EOC: E2-13; E2-22

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

7) Pricing and product-mix decisions include:

- A) manufacturing costs only.
- B) design costs plus manufacturing costs.
- C) all costs incurred along the value chain.
- D) distribution costs only.
- E) production costs only.

Answer: C

Diff: 3 Page Ref: 48

LO: 2-7

EOC: E2-13

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

8) In government contracts, product costs include:

- A) manufacturing costs only.
- B) design costs plus manufacturing costs.
- C) all costs incurred along the value chain.
- D) distribution costs only.
- E) production costs only.

Answer: B

Diff: 3 Page Ref: 48

LO: 2-7

EOC: E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

9) The sum of the costs assigned to a product for a specific purpose are:

- A) manufacturing costs.
- B) design costs.
- C) product costs.
- D) service-sector costs.
- E) technology costs.

Answer: C

Diff: 2 Page Ref: 48

LO: 2-7

EOC: E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

10) Under Generally Accepted Accounting Principles (GAAP), only \_\_\_\_\_ costs can be assigned to inventories in the financial statements.

- A) period
- B) direct
- C) indirect
- D) variable
- E) manufacturing

Answer: E

Diff: 3 Page Ref: 48

LO: 2-7

EOC: E2-22

AACSB: Ethical Understanding and Reasoning Abilities

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

11) Which of the following is **not** true about payroll fringe costs?

- A) Managers do not need to classify payroll fringe costs.
- B) Contracts and laws should be as specific as possible regarding definitions and measurements.
- C) Disputes arise about whether they should be included as part of direct labor costs when calculating percentage of direct labor.
- D) Managers classify them as part of direct labor costs to make direct labor costs a higher percentage of total costs.
- E) Tax authorities argue that the costs are part of overhead.

Answer: E

Diff: 3 Page Ref: 48

LO: 2-7

EOC: E2-20; E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

12) \_\_\_\_\_ is the wage rate paid to workers for both direct labor and indirect labor in excess of their straight-time wage rates.

- A) Overtime payout
- B) One payment
- C) Overtime premium
- D) Premier pay
- E) Objection pay

Answer: C

Diff: 2 Page Ref: 48

LO: 2-7

EOC: E2-20; E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

13) Depending on the purpose, a manager can assign different costs to the same cost object.

Answer: TRUE

Diff: 1 Page Ref: 49

LO: 2-7

EOC: E2-19; E2-20

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

14) The idle time associated with direct labor and indirect labor is a subclassification of indirect labor.

Answer: TRUE

Diff: 2 Page Ref: 47

LO: 2-7

EOC: E2-31

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

15) Although labor cost classifications vary among companies, many companies use multiple labor cost categories.

Answer: TRUE

Diff: 2 Page Ref: 46

LO: 2-7

EOC: E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

16) Managers achieve clarity about direct labor costs because it may prevent disputes regarding cost reimbursement contracts, income tax payments, and labor union matters.

Answer: TRUE

Diff: 2 Page Ref: 48

LO: 2-7

EOC: E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

17) Write a brief summary and discuss the concepts of how managers assign costs to the same cost objects.

Answer: Managers consider the purpose of the cost before they assign costs to the same cost object. Students could provide various examples per any industry sector: In the external reporting purpose in manufacturing companies, the managers review the inventoriable cost of a product that only includes the manufacturing costs. If a manager reviews other costs from the other business functions of the value chain, the costs are assigned to a product for pricing and product-mix decisions.

Diff: 3 Page Ref: 49

LO: 2-7

EOC: E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

## Learning Objective 2-8

1) A sunk cost:

A) is a cost that occurs in the present.

B) is not categorized as a cost.

C) is a relevant cost.

D) is a cost that occurred in the past.

E) is expected to occur in the future.

Answer: D

Diff: 2 Page Ref: 50

LO: 2-8

EOC: Case Study

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) A key aspect of making decisions is:

A) analyzing relevant information.

B) analyzing irrelevant information.

C) analyzing unimportant information.

D) analyzing only future information.

E) analyzing only past information.

Answer: A

Diff: 2 Page Ref: 50

LO: 2-8

EOC: E2-21

AACSB: Communication Abilities

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.



3) Managers compare actual results to planned performance:

- A) at the end of the reporting period.
- B) at the beginning of the reporting period.
- C) at the middle of the reporting period.
- D) at the middle of the first quarter.
- E) at the future planning meetings.

Answer: A

Diff: 3 Page Ref: 50

LO: 2-8

EOC: E2-21

AACSB: Communication Abilities

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

4) Managers must know how revenues and costs vary with changes in:

- A) costs.
- B) profits.
- C) revenues.
- D) decisions.
- E) output levels.

Answer: E

Diff: 3 Page Ref: 50

LO: 2-8

EOC: E2-13; E2-23

AACSB: Communication Abilities

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

5) Whatever the purpose, the \_\_\_\_\_ \_\_\_\_\_ trace direct costs and allocates indirect costs to products.

- A) cargo systems
- B) catering systems
- C) costing systems
- D) cooperative systems
- E) coordinating systems

Answer: C

Diff: 2 Page Ref: 50

LO: 2-8

EOC: E2-20; E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

6) Budgeting is **not** an important tool that managers use in planning and control.

Answer: FALSE

Explanation: Budgeting is an important tool in planning and control endeavors.

Diff: 1 Page Ref: 50

LO: 2-8

EOC: E2-21

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

7) Analyzing relevant information is a key aspect of making appropriate decisions.

Answer: TRUE

Diff: 1 Page Ref: 50

LO: 2-8

EOC: E2-21

AACSB: Ethical Understanding and Reasoning Abilities

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

8) Management accountants help managers distinguish between relevant and irrelevant information.

Answer: TRUE

Diff: 1 Page Ref: 50

LO: 2-8

EOC: E2-21

AACSB: Ethical Understanding and Reasoning Abilities

Learning Outcome: MA-2: Discuss the legal, ethical, and business concepts that affect managerial accounting.

9) List the three key features of cost accounting and cost management.

Answer: The three features of cost accounting and cost management include (1) calculating the cost of products, services, and other cost objects; (2) analyzing relevant information for making decisions, and (3) obtaining information for planning and control and performance evaluation.

Diff: 2 Page Ref: 49

LO: 2-8

EOC: E2-18

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

## Appendix Chapter 2

1) Which of the following methods is **not** used to reduce the undesirable affects of absorption costing?

- A) Focus on careful planning and budgeting of inventory amounts.
- B) Incorporate carrying charges for inventory in the internal accounting system.
- C) Place greater weight on reporting performance over longer periods.
- D) Include only financial variables in the measures used to evaluate performance.
- E) Use alternative methods of inventory costing for internal purposes that does not create incentives for managers to produce for inventory.

Answer: D

Diff: 3 Page Ref: 54

LO: A2

EOC: Case Study

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

2) Under the variable costing method:

- A) fixed manufacturing costs are not inventoried.
- B) fixed manufacturing costs are inventoried.
- C) costs are absorbed into the finished goods inventory.
- D) does not distinguish fixed manufacturing costs from variable manufacturing costs.
- E) is only useful in long-term decision making processes in manufacturing firms.

Answer: A

Diff: 2 Page Ref: 58

LO: A2

EOC: E2-15; E2-16; E2-21; E2-22

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

3) Which of the following is **not** a characteristic of absorption costing?

- A) It is only useful in long-term manufacturing decisions.
- B) Costs are absorbed into finished goods inventory.
- C) Measures the costs of all manufacturing resources to produce inventory.
- D) All manufacturing costs are included in inventoriable costs.
- E) It is not the required inventory method for external reporting in most countries.

Answer: E

Diff: 3 Page Ref: 54

LO: A2

EOC: E2-21; E2-22

AACSB: Dynamics of the Global Economy

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

4) A production system under which products are manufactured only when needed is:

- A) absorption system production.
- B) now system production.
- C) future system production.
- D) current system production.
- E) just-in-time production.

Answer: E

Diff: 2 Page Ref: 60

LO: A2

EOC: E2-14

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

5) The difference between total revenues and total variable costs is the \_\_\_\_\_.

- A) common margin
- B) carrying margin
- C) continental margin
- D) continuing margin
- E) contribution margin

Answer: E

Diff: 3 Page Ref: 58

LO: A2

EOC: E2-20; E2-21

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

6) In \_\_\_\_\_, the operating income depends only on the level of sales and it is invariant to the quantity produced.

- A) method costing
- B) invariable costing
- C) variable costing
- D) continued costing
- E) lateral costing

Answer: C

Diff: 3 Page Ref: 58

LO: A2

EOC: Case Study

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

7) In the absorption-costing method, all of the manufacturing costs are included as inventoriable costs.

Answer: TRUE

Diff: 2 Page Ref: 58

LO: A2

EOC: E2-21; E2-22

AACSB: Reflective Thinking Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

8) A manager at a company that uses both variable costing and absorption costing methods can benefit from the different advantages of both.

Answer: TRUE

Diff: 1 Page Ref: 60

LO: A2

EOC: E2-21; E2-22

AACSB: Ethical Understanding and Reasoning Abilities

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.

9) The distinction between variable costs and fixed costs is central to variable costing, and it is highlighted by the gross-margin format.

Answer: FALSE

Explanation: The distinction between variable costs and fixed costs is central to absorption costing, and it is highlighted by the gross-margin format.

Diff: 2 Page Ref: 58

LO: A2

EOC: E2-16

AACSB: Analytic Skills

Learning Outcome: MA-2: Describe the components of and prepare the four basic financial statements.

10) Write a brief essay and explain why managers use variable costing and why they use absorption costing when they account for fixed manufacturing costs. Discuss the differences between variable costing and absorption costing.

Answer: Managers differentiate between variable costing when they make short-term decisions; and, absorption costing when they need to make long-term decisions. For example, to account for variable costing in manufacturing costs, managers treat the cost as an expense of the period. The fixed manufacturing costs are not inventoried. Under absorption costing, the costs are absorbed into the finished goods inventory. A benefit of the variable costing method is focusing on distinguishing the variable manufacturing costs from the fixed manufacturing costs. Managers use the variable costing method for internal reporting because it removes the undesirable incentives to build up inventories that absorption costing can create.

Diff: 3 Page Ref: 60

LO: A2

EOC: E2-22

AACSB: Analytic Skills

Learning Outcome: FA-2: Describe the components of and prepare the four basic financial statements.