CMA[Q&As]

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QUESTION 1

Metrejean Industries is analyzing a capital investment proposal for new equipment to produce a product over the next 8 years. At the end of 8 years, the equipment must be removed from the plant and will have a net caring amount of $0. a tax basis of $150,000. a cost to remove of $80,000. and scrap salvage value of $20,000. Metrejean\\'s effective tax rate is 40%. What is the appropriate enc$-of-life" cash flow related to these items that should be used in the analysis?

A. $90,000

B. $54,000

C. $24,000

D. $(36,000)

Correct Answer: C

The tax basis of $150,000 and the $80,000 cost to remove are deductible expenses, but the $20,000 scrap value is an offsetting cash inflow. Thus, the taxable loss is $210,000 ($150,000 + $80,000 --$20,000). At a 40% tax rate, the $210,000 loss will produce a tax savings (inflow) of $84,000. According. the final cash flows will consist of an outflow of $80,000 (cost to remove) and inflows of $20,000 (scrap) and $84,000 (tax savings), a net inflow of $24,000.

QUESTION 2

Sales promotion

A. Provides incentives to buy, and advertising provides reasons.

B. Is directed toward consumers, not the trade.

C. Objectives with respect to retailers include motivating them to do more prospecting.

D. Costs have decreased as a percentage of marketing budgets because consumers are less price conscious.

Correct Answer: A

Sales promotion provides incentives to buy. Advertising provides reasons. Promotions may be directed toward consumers, distributors and retailers (trade promotion), the firm\\'s sales force, and other businesses. Promotion costs have increased as a percentage of marketing budgets because consumers are more price conscious, brands have proliferated and are less differentiated, distributors and retailers have greater bargaining power, advertising has become less efficient, firms are under greater pressure to increase sales in the near term, and managers are more accepting of (and qualified to use) promotional methods.

QUESTION 3

Best Computers believes that its collection costs could be reduced through modification of collection procedures. This action is expected to result in a lengthening of the average collection period from 30 to 35 days; however, there will be no change in uncollectible accounts, or in total credit sales. Furthermore, the variable cost ratio is 60%, the opportunely cost of a longer collection period is assumed to be negligible, the compass budgeted credit sales for the coming year are $45,000 000, and the required rate of return is 6%. To just changes in collection procedures, the minimum annual reduction of costs (using a 360-day year and ignoring taxes) must be

A. $375000

B. $37,500

C. $125,000

D. $22,500

Correct Answer: D

The cost of carrying receivables equals average receivables times the variable cost ratio times the cost of money. Given sales of $45,000,000, regardless of which collection procedures are applied, the average daily sales must be $125,000 ($45,000,000 + 360 days). The increase in the average receivables balance is therefore $625,000 (5 days x $125,000). Given an additional $625,000 of receivables, the compass additional required investment in receivables is $375,000 ($625,000 x 60% variable cost ratio), and the incremental pretax cost of this investment is $22,500 (6% x $375,000). Accordingly, the collection costs must be reduced by a pretax minimum of $22,500 to offset the cost of the increased investment in receivables.

QUESTION 4

Which of the following is the best example of a variable cost?

A. The corporate president\\'s salary.

B. Cost of raw material.

C. Interest charges.

D. Property taxes.

Correct Answer: B

Variable costs vary directly with the level of production. As production increases or decreases, material cost increases or decreases, usually in a direct relationship.

QUESTION 5

Which pricing objective is stated as a percentage ratio of profits to sales?

A. Image enhancement

B. Stabilization.

C. Target margin maximization.

D. Achievement of market share.

Correct Answer: C

Pricing objectives include profit maximization. Classical economic theory assumes all firms a Lays select the price that results in the highest profit. An alternative objective is target margin moralization. This objective is stated as a percentage ratio of profits to sales.