

Impairment of and Disposal of Long Lived Assets and Discontinued Operations and Non Monetary Items,

Multiple Choice Questions

1. Which of the following would qualify as a non-monetary transaction under ASPE?
 - (a) An auto manufacturer enters into a transaction with equipment manufacturer to exchange an automobile in return for manufacturing equipment. The FMV and carrying value of the automobile are \$35,000 and \$15,000 respectively. The carrying value of the manufacturing equipment is \$20,000. As the manufacturing equipment is worth \$150 less than the automobile the equipment manufacturer also pays \$150 in addition to giving up the equipment.
 - (b) Company A transfers to company B a 5% investment in Laidlaw Inc in exchange for mandatorily redeemable preferred shares in GM.
 - (c) Company A, a bank, allows company B, a furniture manufacturer in financial distress, to settle its loan with the bank by giving the bank furniture in lieu of paying off their loan.
 - (d) None of the above

2. Jackal Inc. (JI) decides to purchase a rental property. As they have insufficient cash available and can not get financing, they decided to purchase the property through a barter transaction. The company owned a piece of land they purchased very recently, which they were originally planning to use to build a new plant, but they then decided not to go ahead with building the plant. The company therefore decided to give up the land in return for the rental property. The rental property is in an area of London Ontario, in which similar properties have turned over quite frequently in the recent past. Which of the following correctly describes the accounting for the transaction under IFRS?
 - (a) The company should measure the value of the new building on its balance sheet at date of acquisition, based upon the fair value of the land given up.
 - (b) The company should measure the value of the new building on its balance sheet at date of acquisition, based upon the fair value of the building received.
 - (c) The company should measure the value of the new building on its balance sheet at date of acquisition, based upon the carrying value of the land given up.

- (d) The company should measure the value of the new building on its balance sheet at date of acquisition, based upon the carrying value of the building received..

The following scenario relates to questions 3 and 4

GN Inc. an auto manufacturer has committed to a plan to sell the manufacturing equipment in one of its plants and has found a buyer. It is planning to replace the equipment with new high technology robotics equipment. The carrying value of the equipment is \$500,000. The cost of selling the equipment includes a brokerage fee of \$25,000 and internal charges of \$5,000 based on a proration of salary of those individuals who spent time negotiating and arranging the sale. The sales price is \$520,000.

3. Assuming that GN stipulates that they will not transfer the equipment to the buyer until the new robotics equipment is manufactured, delivered and installed at GN, which of the following most accurately describes the presentation of the existing equipment?
- (a) It would be presented as held for sale
 - (b) It would not be presented as held for sale
 - (c) It would not be presented as held for sale as long as there is a commitment from the manufacturer of the new equipment to deliver and install the equipment with 1 year.
 - (d) It would not be presented as held for sale unless there is an expectation that the manufacturer of the new equipment will deliver and install the new equipment within 1 year.
4. Assuming that GN agrees to transfer the existing equipment to the buyer as soon as the buyer can find a shipper to ship the equipment, regardless of when the new equipment is manufactured, delivered and installed, which of the following is the amount at which the equipment would be valued in the financial statements.
- (a) \$490,000
 - (b) \$500,000
 - (c) \$495,000
 - (d) \$520,000
5. In year 1 Polygast Inc. (PI) purchased a machine to produce an MP3 player that is similar to the Apple I-pod. The cost of the machine was \$300,000. The company was planning to

use the machine for 10 years and was expecting to earn annual profits of \$45,000 per year; it was planning to scrap the machine at the end of year 10. The company uses straight line depreciation. At the end of year 2 another company came out with a similar product and the company therefore determined that future annual profits over the remaining life of the machine will be reduced by 60% per annum. The fair value of the machines at the end of year 2 was \$130,000. Assuming a discount rate of 7%, which of the following is the impairment loss that would have to recognized in year 2 under IFRS?

- (A) \$170,000
- (B) \$132,540
- (C) \$110,000
- (D) \$78,810

6. Panza Inc. owns a plant in Toronto with a carrying value of \$3,600,000 as at October 31, 2013, the company's fiscal year end. The fair value of the plant is \$3,400,000. The net cash flows from the plant, over the next 25 years the company expects to use the plant, amount to \$100,000 per year. The residual value of the plant at the end of 25 years is \$500,000. The present value of the net cash flows of \$100,000 per year, using a reasonable rate is \$1,165,000. The present value of the residual value is \$90,000. Which of the following, is the amount by which the company must write down the plant as at the year end based on ASPE?

- (A) \$200,000
- (B) \$600,000
- (C) \$2,345,000
- (D) \$2,435,000

The following scenario applies to questions 7 to 9

An asset group consists of a plant, equipment, inventory and accounts receivable. The carrying values for the assets in the group as at year end, are as follows:

Accounts receivable	\$100,000
Inventory	60,000
Plant	1,000,000

Equipment	<u>700,000</u>
	\$1,860,000

The total aggregate carrying value is not recoverable and exceeds the fair value by \$400,000. The fair value of the inventory is \$65,000.

7. Which of the following is the amount at which the inventory would be reflected, in the financial statements at year end under ASPE?
 - (A) \$60,000
 - (B) \$65,000
 - (C) \$48,000
 - (D) \$50,000

8. Which of the following is the amount at which the equipment would be reflected, in the financial statements at year end under ASPE, assuming that the fair value of the equipment is not determinable?
 - (A) \$548,000
 - (B) \$536,000
 - (C) \$526,000
 - (D) \$562,000

9. Which of the following is the amount at which the plant would be reflected in the financial statements at year end under ASPE, assuming that the fair value of the equipment is known to be \$550,000?
 - (A) \$764,000
 - (B) \$584,000
 - (C) \$750,000
 - (D) \$749,000

Task based Simulations

Task Based Simulation 1

Items 1 through 4 represent True or False statements the testing of cash generating units for impairment under IFRS. Indicate whether each of the statements is true or false.

		True	False
1.	A company must test all of its CGUs for impairment at least once each fiscal year	<input type="radio"/>	<input type="radio"/>
2.	A company does not have to test any CGU for impairment at the end of each fiscal year, regardless of the nature of the assets included in the CGU	<input type="radio"/>	<input type="radio"/>
3.	If goodwill has been allocated to a CGU it will always be tested for impairment once a year.	<input type="radio"/>	<input type="radio"/>
4.	Whether a company must test a particular CGU for impairment at the end of each fiscal year, is dependent upon whether it acquired any subsidiaries during the year	<input type="radio"/>	<input type="radio"/>

Task Based simulation 2

Items 1 through 7 describe scenarios. For each item indicate whether the the item represents a discontinued operation or would be included in continuing operations based on IFRS.

		Discontinued Operation	Continuing Operations
1.	Company sells 2 stores in a suburb of Calgary and replaces the stores with a new large super store that will sell the same products as the 2 stores which were sold.	<input type="radio"/>	<input type="radio"/>
2.	Manufacturer of soaps and shampoos and other hygiene products, disposes of its Shampoo Division line, which accounts for 25% of company sales. The operations and cash flows of the shampoo product line, can be distinguished operationally and for financial reporting purposes from the rest of the company.	<input type="radio"/>	<input type="radio"/>
3.	Company which manufactures bicycles and paint has committed to a plan to close down its paint operation following year end. The operations and cash flows of the paint business can be distinguished operationally and for financial reporting purposes from the rest of the company.	<input type="radio"/>	<input type="radio"/>
4.	Company involved in residential and commercial construction sold its commercial construction business which accounts for 40% of company sales during the year. Separate records are kept for each division. The company will continue to be significantly involved in the commercial operation, as remuneration for the sale is based upon the profitability of the business.	<input type="radio"/>	<input type="radio"/>
5.	Company involved in manufacturing auto parts and motorcycle parts decided to out source the manufacturing of motorcycle parts and therefore sold the motorcycle plant. The operations and cash flows of the motorcycle division can be distinguished operationally and for financial reporting purposes from the rest of the company	<input type="radio"/>	<input type="radio"/>
6.	Company was involved in manufacturing hockey uniforms and baseball uniforms. The manufacturing took place in the same plant and the same machines were used for both hockey and baseball uniforms. The same employees were involved in the manufacture of both types of uniforms although there were separate production runs for hockey versus baseball uniforms. During the year the company discontinued the production of and sale of baseball uniform, which accounted for 45% of sales	<input type="radio"/>	<input type="radio"/>
7.	Company decided in the current year to dispose of a subsidiary that was purchased 2 years ago	<input type="radio"/>	<input type="radio"/>

Task based Simulation 3

Farlinger Inc.(FI) is in the business of buying and selling land. (FI) owns a piece of land in Toronto. The company was approached by a developer who is interested in buying their land next year, provided FI can also sell them the plot of land adjacent to their own land, which is owned by Maverick Inc (MI). FI therefore entered into a transaction with MI in which they exchanged a piece of land they own in Vancouver for MI's land which lies adjacent to their land in Toronto, in order to be able to make the sale to the developer.

FI's land located in Vancouver, was purchased in 1966 for only \$500,000. Today the land is worth \$10 million. The land MI will provide to FI in exchange for the Vancouver land, is worth \$9,300,000. Therefore MI will give FI \$700,000 in addition to giving up their land in Toronto, in return for FI's land in Vancouver. The carrying value of the land in Vancouver FI is giving up, is equal to its historic cost of \$500,000. The carrying value of the land MI is giving up is \$950,000.

Both FI and MI use ASPE to prepare their financial statements.

Items 1 through 4 below describe the items that would be reported in FI's and MI's financial statements. For each item, select from the following the correct numerical responses. An amount may be selected once, more than once or not at all.

- A. \$0 D. \$600,000 G. \$1,650,000 J. \$10,000,000
 B. \$100,000 E. \$500,000 H. \$9,300,000
 C. \$200,000 F. \$950,000 I. \$8,350,000

Amount

	A	B	C	D	E	F	G	H	I	J
1 Carrying value of land received in FI's F/S	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
2 Carrying value of land received in MI's F/S	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Items 3 and 4 require a second response. For each item indicate whether a gain or loss would be recognized

Amount

Gain Loss

	A	B	C	D	E	F	G	H	I	J	Gain	Loss
3 Gain or loss reported on transaction in FI's F/S	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
4 Gain or loss reported on transaction in MI's F/S	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Impairment of and Disposal of Long Lived Assets and Discontinued Operations and Non Monetary Items

Multiple Choice Solutions

1. Answer A

Note: the amount of monetary consideration received is not very significant, so the transaction would still be non monetary.

2. Answer A

A rental building would constitute an investment property. Based on IAS 40 which deals with investment properties, when an investment property is acquired in a non monetary transaction and one is able to reliably measure the fair value of the asset given up and received, the asset acquired should be measured based upon the asset given up. Given that there have been numerous recent transactions in similar buildings and the land was only purchased recently, it is likely that one would be able to measure the fair value of the land and building reliably.

3. Answer B

Because the existing equipment will not be transferred until the new equipment is manufactured, delivered and installed it would not be considered available "immediately" in its current condition "subject only to terms that are usual and customary" for the sale of equipment. Accordingly, it would not be classified as held for sale.

4. Answer C

Because the existing equipment will be transferred as soon as a shipper is hired to ship the machine, the equipment would be considered to be available "immediately" in its current condition "subject only to terms that are usual and customary" for the sale of equipment. Therefore it would be treated as held for sale and valued based upon the lower of the carrying value of \$500,000 and fair value of the machine of \$520,000 less incremental direct costs to transact the sale of \$25,000 which equals \$495,000.

5. Correct response (C)

Calculation of Recoverable Amount

Fair value of Asset: \$130,000

Value in Use: \$45,000 X 40% = \$18,000

PV of annuity of \$18,000 per year over 8 years @7% = 5.97 X \$18,000 = \$107,460

Recoverable amount is the higher of the fair value and value in use which is \$130,000

The carrying value at the end of year 2 would be calculated as follows:

Annual depreciation expense: \$30,000 (i.e. \$300,000/10 years)

Accumulated depreciation over 2 years: \$60,000

Carrying value at the end of year 2: \$240,000 (i.e. \$300,000 - \$60,000)

Therefore the impairment loss would be the difference between \$240,000 and \$130,000 = \$110,000.

6. Answer A

A is correct as a writedown should be made when the estimated future net cash flow from use together with its residual value without discounting (i.e. the recoverable amount) is less than the book value of the property. The writedown is based on the difference between the fair value of the plant and the carrying amount of the plant.

This is calculated as follows:

Carrying Value of Plant: \$3,600,000

Fair value of plant 3,400,000
\$200,000

Note

Recoverable Amount = (25 X \$100,000) + \$500,000
= \$3,000,000

Recoverable amount of \$3,000,000 is less than the book value of \$3,600,000.

7. Answer A

The inventory is valued at the lower of cost and net realizable value. No portion of the impairment loss is allocated to the inventory, as it is not a long lived asset.

8. Answer B

The impairment loss of \$400,000 is allocated to the group as follows:

Asset Group	Carrying amount	Pro rata allocation factor	Allocation of impairment loss	Adjusted carrying amount
Accounts receivable	\$100,000	—	-	\$100,000
Inventory	60,000	-		60,000
Plant	1,000,000	59%	\$(236,000)	764,000
Equipment	<u>700,000</u>	41%	<u>(164,000)</u>	<u>536,000</u>
Total	<u>\$1,860,000</u>	<u>100%</u>	<u>\$(400,000)</u>	<u>\$1,460,000</u>

9. Answer C

One would not reduce the equipment below its fair value of \$550,000. Therefore only \$150,000 of the total impairment loss of \$400,000 can be allocated to the equipment and the remaining loss of \$250,000 must be allocated to the plant, reducing its carrying value to \$750,000.

Task based Simulations

Task Based Simulation 1

1. False

Not all CGUs have to be tested at least once a year. It would depend on what is in the CGU (e.g. whether goodwill has been allocated to the CGU).

2. True

Regardless of the assets included in the CGU (i.e. even if goodwill is allocated to the CGU), it does not have to be tested at the end of each fiscal year. Rather even if goodwill is included in the CGU, the annual impairment test may be performed at any time during an annual period, provided the test is performed at the same time every year.

3. False

Even if goodwill has been allocated to a CGU it will not always be tested for impairment once a year; it may be tested more than once a year. The rule is that a CGU to which goodwill has been allocated must be tested for impairment annually, and whenever there is an indication that the unit may be impaired. The fact that one must test for impairment whenever there is an indication that the CGU may be impaired could lead to an impairment test being done more than once in a year. A true statement would be that that if goodwill has been allocated to a CGU, it will always be tested for impairment at least once a year.

4. False

If some or all of the goodwill allocated to a cash-generating unit was acquired in a business combination during the current annual period, that unit shall be tested for impairment before the end of the current annual period.

Task Based simulation 2

1. Correct response: Continuing Operation

Given that the superstore will continue to sell the same goods previously sold through the two stores which were sold, there has been no discontinued operation.

2. Correct response: Discontinued Operation

Given that (i) the Shampoo Division meets the definition of a “component”; and (ii) it accounts for a significant proportion of the company’s sales and would therefore represents a separate major line of business, it would qualify as a discontinued operation.

3. Correct response: Continuing Operation

It would not constitute a discontinued operation as a an operation to be disposed of other than by sale would not be classified as “held for sale” and hence can not be a discontinued operation.

4. Correct response: Discontinued Operation

The fact that the company will retain significant involvement in the commercial construction division, does not prevent the operation from being treated as discontinued.

5. Correct response: Continuing Operation

Although the manufacturing plant would be treated as held for sale, the company will continue to operate a motorcycle operation Therefore the motorcycle operation is not presented as a discontinued operation.

6. Correct response: Continuing Operation

The baseball uniform side of the business does not constitute a “component” of the enterprise. A component comprises operations and cash flows that can be clearly distinguished operationally and for financial-reporting purposes from the rest of the enterprise. In this case it would appear that the baseball uniform side of the business can not be distinguished operationally from the rest of the enterprise, given that the uniforms are manufactured using the same plant, machinery and employees as the hockey uniforms.

7. Correct response: Continuing Operation

In order for this situation to be treated as a discontinued operation, the subsidiary would have had to have been acquired exclusively with a view to resale, which was not the case here given that the company decided to sell the operation 2 years after the acquisition.

Task Based Simulation 3

1. Amount: Correct response A

This transaction would be measured by FI using carrying values rather than fair value as the transaction represents an exchange of a product or property held for sale in the ordinary course of business for a product or property to be sold in the same line of business to facilitate sales to customers other than the parties to the exchange. Given that the amount of cash FI received exceeds the carrying value of the asset given up, the land received would have no value on the balance sheet.

2. Amount: Correct response J

From MI's perspective there is no reason to use carrying value as there is no indication that any of the scenarios that would preclude using fair value are present.

The land that is received would therefore be measured at the fair value of the land that MI gave up (i.e. 9.3 million) plus the \$700,000 of cash consideration that was paid for a total of \$10,000,000.

3. Amount: Correct response C **Gain**

As mentioned in point 1 the transaction would be measured using carrying values rather than fair value as. Farlinger Co. would still however be able to reflect a gain of \$200,000 given that the carrying value of the land is \$500,000 and \$700,000 of cash has been received.

The entry is:

Dr. Cash:	\$700,000	
Cr. Carrying value of land (given up):	\$500,000	
Cr. Gain:		\$200,000

4. Amount: Correct response I **Gain**

As mentioned in point 2 MI would account for the transaction at fair value. The entry would be as follows:

Dr. New land:	\$10,000,000*	
Cr. Carrying value of land (given up):		\$950,000
Cr. Cash:		\$700,000
Cr. Gain		\$8,350,000

*i.e. \$9.3M plus \$700K

MANAGEMENT DECISION – MAKING QUESTIONS

Multiple Choice Questions – Set 1

Use the following information to answer questions 1-4

François International produces fine wine. The direct materials and direct labour standards for one bottle of its most popular wine are as follows:

Direct Materials		Direct Labour	
Standard Quantity	16 oz.	Standard hours	0.5 hours
Standard Price	\$1.20 per oz.	Standard rate	\$8.00/hour

During the most recent month, the following activity was recorded:

- 50,000 ounces of materials were purchased at a cost of \$1.00 per ounce
- All of the material was used to produce 3,000 bottles of fine wine.
- 1,300 hours of direct labour time were recorded at a total labour cost of \$6,500.

1. What is the total direct material price variance for the month?
 - a) \$10,000 Unfavourable
 - b) \$10,000 Favourable
 - c) \$ 2,400 Unfavourable
 - d) \$ 2,400 Favourable
2. What is the total direct material quantity variance for the month?
 - a) \$10,000 Unfavourable
 - b) \$10,000 Favourable
 - c) \$ 2,400 Unfavourable
 - d) \$ 2,400 Favourable
3. What is the total labour rate variance for the month?
 - a) \$3,900 Unfavourable
 - b) \$3,900 Favourable
 - c) \$4,200 Unfavourable
 - d) \$4,200 Favourable
4. What is the total labour efficiency variance for the month?
 - a) \$2,800 Unfavourable
 - b) \$2,800 Favourable
 - c) \$1,600 Unfavourable
 - d) \$1,600 Favourable

Use the following information to answer questions 5 – 6.

Interior Art Company has 2 divisions – an Art Division that sells works of art and a Framing Division. The Art Division purchases frames for a line of prints from an outside supplier for \$94.

The manager of the Framing Division has approached the manager of the Art Division about buying the frames internally.

Cost of Production – 1 frame

Direct Materials	\$20
Direct Labour	18
Variable Overhead	17
Fixed Overhead	<u>30</u>
Total Cost	\$85

Other Information

Frame Division capacity	100,000 frames
Frame Division production	50,000 frames
Art Division requirements	30,000 frames

5. Based on the above information what are the maximum and minimum transfer prices?
 - a) Maximum price of \$94, Minimum Price of \$94
 - b) Maximum price of \$94, Minimum Price of \$55
 - c) Maximum price of \$85, Minimum Price of \$38
 - d) Maximum price of \$85, Minimum Price of \$0

6. Assume now that the Framing Division is operating at capacity of 100,000 units. What are the maximum and minimum transfer prices?
 - a) Maximum price of \$94, Minimum Price of \$94
 - b) Maximum price of \$94, Minimum Price of \$55
 - c) Maximum price of \$85, Minimum Price of \$38
 - d) Maximum price of \$85, Minimum Price of \$0

Use the following information to answer questions 7 - 8

RunFast Shoe Company produces 2 models of shoes that require the use of a special plastic forming machine. The company owns 6 machines that perform this function. Together, the machines provide a total of 12,000 hours per year. The Free Spirit (FS) Model requires 4 hours of machine time, and the True Training (TT) Model requires 2 hours of machine time. The FS Model has a contribution margin of \$12 per unit, and the TT Model has a contribution margin of \$10.

7. What is the optimal number of units of each model that should be produced, assuming that an unlimited number of each model can be sold?
 - a) 0 units of TT, 6000 units of FS
 - b) 6000 units of TT, 0 units of FS
 - c) 500 units of TT, 5000 units is FS
 - d) 5000 units of TT, 500 units of FS

8. Calculate the optimal number of units of each model that should be produced, assuming that no more than 5000 units of each model can be sold.
 - a) 5000 units of TT, 1000 units of FS
 - b) 1000 units of TT, 5000 units of FS
 - c) 500 units of TT, 5000 units is FS
 - d) 5000 units of TT, 500 units of FS

9. Waterloo Beverage Company produces 3 products: Apple Juice, Beer, and Cola. A segmented income statement (in thousands of dollars) follows:

	Apple	Beer	Cola	Total
Sales Revenue	\$ 700	\$ 1,800	\$ 200	\$ 2,700
Less: Variable Expenses	350	1,000	140	1,490
Contribution Margin	350	800	60	1,210
Less: Direct Fixed Expenses	100	300	70	470
Segment Margin	\$ 250	\$ 500	\$ (10)	\$ 740
Less: Common Fixed Expenses				340
Operating Income				<u>\$ 400</u>

Direct fixed expenses include depreciation on equipment dedicated to the product lines - \$20,000 for Apple Juice, \$120,000 for Beer, and \$30,000 for Cola. None of the equipment can be sold.

10 percent of customers that buy Beer from Waterloo Beverage Company choose to buy from the company because it offers a full range of products, including

Cola. If the Cola line were no longer available, these customers would go elsewhere to purchase Beer.

What impact would result from dropping the Cola Line?

- a) \$100,000 decrease in operating income
- b) \$10,000 increase in operating income
- c) \$60,000 decrease in operating income
- d) \$70,000 decrease in operating income

10. Keep Clean Soap Company has been approached by a new customer with an offer to purchase 1,400 units of Keep Clean's product at a price of \$3 each. Keep Clean normally produces 10,000 units, but plans to produce and sell only 8,000 in the coming year. The normal sale price is \$5 per unit. Cost information is as follows:

Direct Materials	\$ 0.75
Direct Labour	0.80
Variable Overhead	0.40
Fixed Overhead	2.00
Total	<u>\$ 3.95</u>

The distribution centre at the warehouse is operating at full capacity and would need to add capacity costing \$1,000 for every 5,000 units shipped.

Should Keep Clean accept the special order? By how much will profit increase or decrease if the order is accepted?

- a) Yes, the order should be accepted. It will increase profit by \$470.
 - b) Yes, the order should be accepted. It will increase profit by \$230.
 - c) No, the order should not be accepted. It will decrease profit by \$400.
 - d) No, the order should not be accepted. It will decrease profit by \$230.
11. You, CPA, work for Planes Inc., a manufacturing company that produces large commercial aircrafts used by many of the major North American airlines. Your company is part of an intricate network of suppliers. For example, Planes Inc. purchases its engines from Engines Inc. and its passenger safety systems (flotation devices, air masks, etc.) from Safety Inc. and both Engines Inc. and Safety Inc. purchase components of their products from other suppliers.

In regards to Planes Incorporated supply chain which of the following statements is most accurate?

- a) Participation in this supply chain protects Planes Inc. from the effects of any work stoppages at Safety Inc.

- b) Participation in this supply chain allows Planes Inc. to more easily identify the source of quality issues with any of the parts of the plane.
 - c) Participation in this supply chain enables Planes Inc. to enjoy the benefits of greater production efficiencies.
 - d) Participation in this supply chain prevents Planes Inc. from incurring additional costs caused by the increase in the price of engine parts.
12. The Toy Car Company is currently experience several quality issues with the paint finish on its toy car product. For example, one issue is that the paint on the body of the car chips and scratches very easily. In regards to the paint quality issues, which of the following describes the findings that would be identified by using pareto analysis?
- a) The Toy Car Company identifies the root cause of the chipped paint issue.
 - b) The Toy Car Company identifies several possible causes of the chipped paint issue.
 - c) The Toy Car Company identifies a few causes that address most of paint issue.
 - d) The Toy Car Company identifies one cause that will address all of the paint issues.
13. Techno Inc. has recently developed a new, innovative personal communication device into the market place. Management anticipates that this product will be extremely successful once in enters the marketplace. The company's objective is to maximize the profits from this product over its expected lifecycle of 3 years. To meet their objective at which phase is it most important to focus on cost reductions?
- a) Product introduction
 - b) Product growth
 - c) Product maturity
 - d) Product decline.

Task Based Questions

Task Based Questions 1

Items 1 through 4 represent True or False statements concerning transfer pricing .
Indicate whether each of the statements is true or false.

		True	False
1.	Using market prices fosters divisional autonomy	<input type="radio"/>	<input type="radio"/>
2.	When market process are used suboptimization is avoided	<input type="radio"/>	<input type="radio"/>
3.	The use of variable costing will lead to the best long run utilization of facilities	<input type="radio"/>	<input type="radio"/>
4.	The use of market process simplifies the costing of finished goods	<input type="radio"/>	<input type="radio"/>
5.	Dual pricing generally enhances decision making from the perspective of the organization as a whole	<input type="radio"/>	<input type="radio"/>

Task Based Questions 2

The Sofa and Chair division of a furniture company has the opportunity to invest in a 2 new product lines next year.

The outlay required for each investment and the dollar returns are as follows:

	Leather Sofa	Easy Chair
Investment	\$10 250 000	\$4 650 000
Op. Income	1 400 000	740 000

The division is currently earning an ROI of 18%, using operating assets of \$75 million. Operating income on the current investment is \$13.5 million in new investment capital. The company's WACC is 12%.

Each of the responses below indicates a course of action that a manger could choose. For each of the items below, choose a response that describes what the manager would choose to do. Responses may be selected once, more than once or not at all.

Responses to be selected

- A. Invest in leather sofa
- B. Invest in reclining easy chair
- C. Invest in both product lines
- D. Invest in neither product line

		(A)	(B)	(C)	(D)
1.	The manager is evaluated based on ROI and is considering investing in the sofa and reclining easy chair product lines	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>
2.	The manager is evaluated based on Residual Income and is considering investing in the sofa and reclining easy chair product lines	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>	<input type="radio"/>

Task Based Questions 3

Toronto Fashion is a clothing manufacturer specializing in denim apparel. The company's has just completed its first season of production of a new denim jackets.

Direct Materials

Standard Price	\$5.00/metre	Actual Price	\$5.15/metre
Standard Quantity	1.50 metres/shirt	Actual Quantity	1.75 metres/shirt

Direct Labour

Standard Usage	2 hours/unit	Actual Usage	1.5 hours
Standard Rate	\$10/hour	Actual Rate	\$18/hour

Variable Overhead (V/O)

Standard V/O Rate	\$3.85/DLH	Actual V/O Rate	\$4.00/DLH
Standard Hours	378.5 hours	Actual Hours	400 hours

Fixed Overhead

Budgeted Fixed Overhead	\$5,000
Actual Fixed Overhead	\$5,235
Standard Machine Hours	1,000 hours
Actual Machine Hours	950 hours

MANAGEMENT DECISION – MAKING - SET 1

1. The correct answer is B.
 $(\$1 \times 50,000) - (\$1.20 \times 50,000) = \$10,000$ Favourable
2. The correct answer is C.
 $(\$1.20 \times 50,000) - (\$16oz \times 3000 \times \$1.20) = \$2\,400$ Unfavourable
3. The correct answer is B.
 $(0.43 \text{ hrs} \times 3000 \times \$5/\text{hr}) - (0.43\text{hrs} \times 3000 \times \$8/\text{hr}) = \$3,900$ Favourable
4. The correct answer is D.
 $(0.43 \text{ hrs} \times 3000 \times \$8/\text{hr}) - (0.5\text{hrs} \times 3000 \times \$8/\text{hr}) = \$1,600$ Favourable
5. The correct answer is B. The maximum transfer price should be the market price of \$94. When excess capacity exists, the correct minimum transfer price should only be the variable costs of \$55.
6. The correct answer is A. When excess capacity does not exist, the only price that the framing division should accept is the market value.
7. The correct answer is B. Runfast Shoe Co. should sell 6000 units of TT and no units of FS.

Calculation of contribution margin per machine hour

$$\text{FS} = \$12 / 4 \text{ hours} = \$3 / \text{hr}$$

$$\text{TT} = \$10 / 2 \text{ hours} = \$5 / \text{hr}$$

8. The correct answer is D. Runfast should sell 5,000 units of TT (using 10,000 hours of machine time) and use the remaining 2000 hours of machine time to produce 500 units of FS (2000/4).

9. The correct answer is A. Dropping the cola line would cause a decrease of \$100,000 in operating income.

Restatement of Income Statement without Cola Line (in thousands):

	Apple	Beer (10% decrease)	Total
Sales	\$700	\$1,620	\$2,320
Less: VC	350	900	1,250
Contribution Margin	350	720	1,070
Less: Direct Fixed	100	300	400
Segment Margin	250	420	770
Less: Common Fixed			340
Less: Depreciation			30
Operating Income			300

10. The correct answer is A. The order should be accepted, and it will increase profit by \$470.

Calculation:

Relevant Manufacturing Costs	$\$0.75 + 0.80 + 0.40 = \$1.95/\text{unit}$
Gross profit from special order	$\$3.00 - 1.95 = \$1.05/\text{unit}$
Total gross profit	$\$1.05 \times 1,400 = \$1,470$
Gross Profit less Capacity Costs	$\$1,470 - 1,000 = \470

11. C is correct. One of the main benefits of supply chain management is the increased production efficiencies realized by the members of the supply chain.
12. C is correct. A pareto analysis identifies a limited number of causes that, if addressed, are likely to address most of the quality issues.
13. A is correct. Cost reduction is an important component in all phases of the life-cycle but most important in the early stages (e.g., production introduction) because decisions that will affect the cost of the product throughout the life cycle are made in this phase.

Task Based Questions

Task Based Questions 1

1. True

Market prices fosters divisional autonomy as market prices approximate an arm's length transaction as if external parties are dealing with the division in question. Also because there is usually a profit component in market prices, market prices provide an appropriate measure when divisions are either profit or investment centres.

2. False

This statement is not always true. It is only true when there is a competitive market for the selling division's product.

3. False

The use of variable costing will lead to good short run utilization of facilities; but not good long term utilization given that in the long run fixed costs can not be ignored.

4. False

When market prices are used, the actual costs of finished goods is more difficult to determine. When full cost is used (rather than market), the costing of goods is simplified.

5. True

Dual pricing generally enhances decision making from the perspective of the organization as a whole, as one price may not fulfill all of the needs of management. For example one price may be more useful for evaluating performance but another may be more useful in determining whether a transfer should take place. A dual price will allow for such flexibility.

Task Based Simulation 2

1. Correct answer D

The ROI is highest (18%) for when the manager does not invest in either project.

	Leather Sofa	Reclining Chair	Both Projects	Neither Project
Operating Income	\$1,400	\$740	\$2,140	\$13,500
Operating Assets	10,250	4,650	\$14,900	\$75,000
ROI	14%	16%	14%	18%

2. Correct response C

The RI is positive for both projects; therefore to maximize RI the manager will invest in both projects.

Leather Sofa

$$\$1,400,000 - (12\% \times 10,250,000) = \$170,000$$

Reclining Chair

$$\$740,000 - (12\% \times 4,650,000) = \$182,000$$

Task Based Simulation 3

1. Correct answer B Unfavourable

$$(\$5 \times 1.75) - (\$5 \times 1.50) = \$1.25$$

2. Correct response D Unfavourable

$$(\$18 \times 1.5) - (\$10 \times 1.5) = \$12$$

3. Correct response G Unfavourable

$$(\$4 \times 400) - (\$3.85 \times 378.3) = \$144$$

4. Correct response J Unfavourable

$$(\$5 \times 1000) - (\$5 \times 950) = \$250$$

5. Correct response I Unfavourable

$$(\$5,235) - (\$5,000) = \$235$$