

Chapter 21—Operational Budgeting and Profit Planning

Solutions to Practice Quiz

1. Management by exception:

- a. Advocates the rewarding of exceptional managers
- b. Provides detailed instructions to all employees except top management
- c. Requires the justification for all budget items except the amount budgeted or spent in a previous budget
- d. None of the above

Answer: *d*

Rationale: Under management by exception, management directs attention only to those activities not proceeding according to plan.

2. Which of the following approaches is widely used for budgeting?

- a. The incremental approach
- b. The minimum level approach
- c. The output/input approach
- d. All of the above

Answer: *d*

Rationale: All of the listed items are formal budgeting procedures.

3. Budgeted sales of the Taco El Loco for the first quarter of the year are as follows:

January	\$60,000
February	70,000
March	86,000

The cost of sales averages 30 percent of sales revenue and management desires ending inventories equal to 20 percent of the following month's sales.

Assuming the January 1 inventory is \$7,000, the January purchases budget is:

- a. \$25,200
- b. \$15,200
- c. \$14,600
- d. \$22,200

Answer: *b*

Rationale:

Requirements for January ($\$60,000 \times 0.30$)	\$18,000
Desired January 31 inventory ($\$70,000 \times 0.20 \times 0.30$)	<u>4,200</u>
Total requirements	\$22,200
Less beginning inventory	<u>7,000</u>
January purchases budget	<u>\$15,200</u>

4. Penn Distribution's sales budget for the second quarter follows:

April	\$350,000
May	450,000
June	380,000

All sales are on account (credit) with 50 percent collected in the month of sale, 30 percent collected in the month after sale, and 20 percent collected in the second month after sale. There are no uncollectable accounts.

The June cash receipts are:

- a. \$190,000
- b. \$325,000
- c. \$395,000
- d. None of the above

Answer: *c*

Rationale:

Collections from June sales ($\$380,000 \times 0.50$)	\$190,000
Collections from May sales ($\$450,000 \times 0.30$)	135,000
Collections from April sales ($\$350,000 \times 0.20$)	<u>70,000</u>
June cash receipts	<u>\$395,000</u>

5. Refer to Question 4 and determine the accounts receivable at the end of June:

- a. \$190,000
- b. \$280,000
- c. \$330,000
- d. \$385,000

Answer: *b*

Rationale:

Remaining June sales ($\$380,000 \times 0.50$)	\$190,000
Remaining May sales ($\$450,000 \times 0.20$)	<u>90,000</u>
End of June accounts receivable	<u>\$280,000</u>

6. Presented is selected first quarter budget data for the Barney Company:

Sales	
January	25,000 units
February	20,000 units
March	42,000 units

Additional information:

- Each unit of finished product requires two pounds of raw materials.
- Barney maintains ending finished goods inventories equal to 25 percent of the following month's budgeted sales.
- Barney maintains raw materials inventories equal to 20 percent of the following month's budgeted production.
- January 1 inventories are in line with Barney's inventory policy.

Barney's budgeted purchases (in pounds) for January is:

- 66,000 pounds
- 48,200 pounds
- 51,000 pounds
- None of the above

Answer: *b*

Rationale:

<u>Production Budget (units of finished goods)</u>	<u>January</u>	<u>February</u>	<u>March</u>
Sales requirements	25,000	20,000	42,000
Desired ending inventory (25% following month's sales)	<u>5,000</u>	<u>10,500</u>	
Total requirements	30,000	30,500	
Less beginning inventory (25% current month's sales)	<u>(6,250)</u>	<u>(5,000)</u>	
Production	<u><u>23,750</u></u>	<u><u>25,500</u></u>	

<u>Purchases Budget (pounds of raw materials)</u>	<u>January</u>	<u>February</u>
Required for current production (production in units x 2 pounds per unit)	47,500	51,000
Desired ending inventory (20% following month's production requirements)	<u>10,200</u>	
Total requirements	57,700	
Less beginning inventory (20% current month's production requirements)	<u>(9,500)</u>	
Purchases (pounds)	<u><u>48,200</u></u>	

7. Presented is additional information for the Barney Company (refer to Question 6):

- Price per pound of raw materials \$25
- Direct labor per unit of finished product 0.50 hours at \$20 per hour
- Total monthly factory overhead \$150,000 + \$10 per direct labor hour

Barney's total manufacturing cost budget for January is:

- a. \$1,425,000
- b. \$1,693,750
- c. \$1,575,000
- d. \$1,717,500

Answer: b

Rationale:

Direct materials (47,500 x \$25)	\$1,187,500
Direct labor (23,750 x 0.50 x \$20)	237,500
Variable factory overhead (23,750 x 0.50 x \$10)	118,750
Fixed factory overhead	<u>150,000</u>
Total	<u>\$1,693,750</u>

8. An advantage of the participative budgeting process is:

- a. The elimination of budgetary slack
- b. A reduction in the time required to complete the budget
- c. The increased likelihood of favorable variances
- d. Improved opportunities for problem solving

Answer: d

Rationale: Because participation helps ensure that important issues are considered the participative budgeting process provides improved opportunities for problem solving.