Question 1 - CMA 1291 3-10 - Responsibility Centers and Reporting Segments

A segment of an organization is referred to as a service center if it has

A. Authority to provide specialized support to other units within the organization.
B. Responsibility for combining the raw materials, direct labor, and other factors of production into a final output.
C. Authority to make decisions affecting the major determinants of profit including the power to choose its markets and sources of supply.
D. Responsibility for developing markets and selling the output of the organization.

A. A service center provides specialized support services to other departments of the organization.
B. This is the definition of a production center, not a service center. See the correct answer for a complete explanation.
C. This is the definition of a profit center, not a service center. See the correct answer for a complete explanation.
D. This is the definition of a revenue center, not a service center. See the correct answer for a complete explanation.

Question 2 - CMA 693 3-14 - Responsibility Centers and Reporting Segments

The least complex segment or area of responsibility for which costs are allocated is a(n)

A. Investment center.
B. Contribution center.
C. Cost center.
D. Profit center.

A. An investment center is responsible for revenues, costs and investment. Therefore, it is not the least complex segment or area of responsibility for which costs are allocated.
B. Contribution center is not a term used in responsibility center analysis and reporting.
C. A cost center is the least complex of the different types of centers. It is responsible only for the incurrence of costs.
D. A profit center is responsible for both revenues and expenses. Therefore, it is not the least complex segment or area of responsibility for which costs are allocated.

Question 3 - CMA 1296 3-17 - Responsibility Centers and Reporting Segments

In theory, the optimal method for establishing a transfer price is

A. Budgeted cost with or without a markup.
B. Market price.
C. Flexible budget cost.
D. Incremental cost.

A. Cost based transfer pricing is perhaps the best method of transfer pricing if the department that is buying is not required to buy from another internal department. However, if the buying department is unable to choose its supplier, the manager of the supplying internal department will not have any motivation to control costs, because he or she will know that the costs will simply be charged to the next department.

B. The transfer price is the price charged by one unit of the company to another unit of the same company for the services or goods produced by the first unit and "sold" to the second unit. The goal in setting a transfer price is that the method used will stimulate the department managers — both selling and buying —
to do what will provide the greatest benefit to the company as a whole, rather than to act in their own interest. When there is an external market for the product, market price is almost always the best transfer price to use.

C. Cost based transfer pricing is perhaps the best method of transfer pricing if the department that is buying is not required to buy from another internal department. However, if the buying department is unable to choose its supplier, the manager of the supplying internal department will not have any motivation to control costs, because he or she will know that the costs will simply be charged to the next department.

D. Cost based transfer pricing is perhaps the best method of transfer pricing if the department that is buying is not required to buy from another internal department. However, if the buying department is unable to choose its supplier, the manager of the supplying internal department will not have any motivation to control costs, because he or she will know that the costs will simply be charged to the next department.

Question 4 - CMA 694 3-20 - Responsibility Centers and Reporting Segments

Under a standard cost system, the materials price variances are usually the responsibility of the

A. Production manager.
B. Cost accounting manager.
C. Purchasing manager.
D. Sales manager.

A. The materials price variance is the difference between the actual price and the standard price of material multiplied by the quantity actually consumed by production. The production manager is not involved in the purchasing activity where the price is negotiated.

B. The materials price variance is the difference between the actual price and the standard price of material multiplied by the quantity actually consumed by production. The cost accounting manager is not involved in the purchasing activity where the price is negotiated.

C. The materials price variance is the difference between the actual price and the standard price of material multiplied by the quantity actually consumed by production. The purchasing manager is responsible for purchasing activity where price is negotiated and is therefore usually held responsible for the material price variance.

D. The materials price variance is the difference between the actual price and the standard price of material multiplied by the quantity actually consumed by production. The sales manager is not involved in the purchasing activity where the price is negotiated.

Question 5 - CMA 1296 3-23 - Responsibility Centers and Reporting Segments

The purpose of identifying manufacturing variances and assigning their responsibility to a person/department should be to

A. Use the knowledge about the variances to promote learning and continuous improvement in the manufacturing operations.
B. Determine the proper cost of the products produced so that selling prices can be adjusted accordingly.
C. Pinpoint fault for operating problems in the organization.
D. Trace the variances to finished goods so that the inventory can be properly valued at year-end.

A. The purpose of identifying manufacturing variances and assigning their responsibility to a person/department is to use the knowledge about the variances to promote learning and continuous improvement. One of the main purposes for responsibility centers and responsibility accounting is to enable evaluation of subunits' performance and contribute to measuring the performance of the subunits' managers. This provides motivation for managers of the subunits. By knowing what they are responsible for
and controlling those items, managers should be more motivated than if they were evaluated on something outside of their control.

B. The selling price is mostly determined by the manufacturing costs and other aspects like market price level, service costs allocation, etc. The variances are usually not significant aspects in the process of selling price determination.

C. Reports of variances from the budget should be used to direct attention to problems, and the emphasis should be on information, not on blame.

D. Depending on the significance of a variance, it is either written off to the finished goods account or allocated to the inventory accounts and finished goods on pro-rata basis. Variances are not used to properly value inventory at year end.

Question 6 - CIA 595 III-96 - Responsibility Centers and Reporting Segments

Which of the following techniques would be best for evaluating the management performance of a department that is operated as a cost center?

A. Return on assets ratio.
B. Payback method.
C. Return on investment ratio.
D. Variance analysis.

A. A cost center is a type of center in responsibility accounting classifications that is responsible only for the incurrence of costs. A cost center does not have any revenue, and therefore does not have any profit. Thus, a return on assets ratio cannot be calculated for a cost center.

B. The payback method is used to analyze alternative investment opportunities, not management performance.

C. Cost center is a type of center in responsibility accounting classifications that is responsible only for the incurrence of costs. A cost center does not have any revenue, and therefore does not have any profit. Thus, a return on investment ratio cannot be calculated for a cost center.

D. A cost center is a type of center in responsibility accounting classifications that is responsible only for the incurrence of costs. A cost center does not have any revenue, and therefore does not have any profit. Thus, performance evaluation based on variance analysis of costs is the best basis for performance evaluation of a cost center manager.

Question 7 - CMA 1294 3-21 - Responsibility Centers and Reporting Segments

Sherman Company uses a performance reporting system that reflects the company's decentralization of decision making. The departmental performance report shows one line of data for each subordinate who reports to the group vice president. The data presented show the actual costs incurred during the period, the budgeted costs, and all variances from budget for that subordinate's department. Sherman is using a type of system called

A. Responsibility accounting.
B. Flexible budgeting.
C. Contribution accounting.
D. Cost-benefit accounting.

A. Responsibility accounting is a system in which costs are allocated to managers and/or departments based on who is responsible for the incurrence of the costs. This is the method described in the question.
B. Flexible budgeting is the adaptation of the static budget to the level of activity actually achieved during the period. This is not what is described in the question.

C. Contribution margin analysis focuses on the variable revenues and costs and their behavior as activity levels change. The selling price minus variable costs is the contribution margin. Fixed costs are then subtracted from the contribution to determine the profit.

D. This is not an accounting method.

---

**Question 8** - CIA 588 IV-19 - Responsibility Centers and Reporting Segments

The alpha division of a company, which is operating at capacity, produces and sells 1,000 units of a certain electronic component in a perfectly competitive market. Revenue and cost data are as follows:

<table>
<thead>
<tr>
<th>Description</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>$50,000</td>
</tr>
<tr>
<td>Variable costs</td>
<td>34,000</td>
</tr>
<tr>
<td>Fixed costs</td>
<td>12,000</td>
</tr>
</tbody>
</table>

The minimum transfer price that should be charged to the beta division of the same company for each component is

A. $12  
B. $46  
C. $50  
D. $34

A. Because the alpha division is operating at capacity, the minimum price it will charge an internal division is the market price. See the correct answer for a complete explanation.

B. Because the alpha division is operating at capacity, the minimum price it will charge an internal division is the market price. See the correct answer for a complete explanation.

C. Because the alpha division is operating at capacity, the minimum price it will charge an internal division is the market price. The market price per unit is $50. If they were to charge less than the market price they would be losing money since they could sell that same unit to a different customer at a higher price.

D. Because the alpha division is operating at capacity, the minimum price it will charge an internal division is the market price. See the correct answer for a complete explanation.

---

**Question 9** - CMA 1296 3-2 - Responsibility Centers and Reporting Segments

The segment margin of an investment center after deducting the imputed interest on the assets used by the investment center is known as

A. Return on assets.  
B. Operating income.  
C. Residual income.  
D. Return on investment.

A. Return on assets does not take into account the imputed interest rate on the assets of the investment center. See the correct answer for a complete explanation.

B. Operating income does not take into account the imputed interest rate on the assets of the investment center. See the correct answer for a complete explanation.

C. Residual income is the amount of return after a certain required return on the assets in use by the investment center. See the correct answer for a complete explanation.

(c) HOCK international, page 4
division. The calculation of the required return is based on an imputed interest rate for the cost of funds represented by the assets in use. This describes the situation in the question.

D. Return on investment is calculated as income divided by the invested amount. There is no deduction of an imputed interest rate in the calculation of return on investment.

Question 10 - CIA 592 IV-19 - Responsibility Centers and Reporting Segments

Division Z of a company produces a component that it currently sells to outside customers for $20 per unit. At its current level of production, which is 60% of capacity, Division Z's fixed cost of producing this component is $5 per unit and its variable cost is $12 per unit. Division Y of the same company would like to purchase this component from Division Z for $10. Division Z has enough excess capacity to fill Division Y's requirements. The managers of both divisions are compensated based upon reported profits. Which of the following transfer prices will maximize total company profits and be most equitable to the managers of Division Y and Division Z?

A. $12 per unit.
B. $20 per unit.
C. $22 per unit.
D. $18 per unit.

A. The transfer price should be between the variable costs of production ($12) and the market price ($20). While $12 is at the edge of this range, the selling division would earn no contribution from the sale, so it will not gain anything from this contract.

B. The transfer price should be between the variable costs of production ($12) and the market price ($20). $18 is the only option between these amounts. While $20 is at the edge of this range, the purchasing division will have no savings compared to the outside purchase price so would not gain anything by purchasing internally.

C. The transfer price should be between the variable costs of production ($12) and the market price ($20). $22 is outside of this range.

D. The transfer price should be between the variable costs of production ($12) and the market price ($20). $18 is the best answer because it is the only answer choice that is in between these amounts.

Question 11 - CIA 1193 IV-19 - Responsibility Centers and Reporting Segments

The Eastern division sells goods internally to the Western division of the same company. The quoted external price in industry publications from a supplier near Eastern is $200 per ton plus transportation. It costs $20 per ton to transport the goods to Western. Eastern's actual market cost per ton to buy the direct materials to make the transferred product is $100. Actual per ton direct labor is $50. Other actual costs of storage and handling are $40. The company president selects a $220 transfer price. This is an example of

A. Cost plus 20% transfer pricing.
B. Cost-based transfer pricing.
C. Negotiated transfer pricing.
D. Market-based transfer pricing.

A. This is not an example of cost plus 20% transfer pricing. A cost plus 20% transfer price would be based on the cost of $190.

B. This is not an example of cost-based transfer pricing. A cost-based transfer price would be $190.

C. This is not an example of negotiated transfer pricing. A negotiated transfer price would be one somewhere between $190 and $220 that is agreed on by the parties involved.

D. Since the transfer price that has been set is the market price, this is market based transfer pricing.
Decentralized firms can delegate authority and yet retain control and monitor managers’ performance by structuring the organization into responsibility centers. Which one of the following organizational segments is most like an independent business?

A. Profit center.
B. Investment center.
C. Cost center.
D. Revenue center.

A. A profit center is responsible for both revenues and costs, but a profit center is not responsible for the return on the investment made into it.

B. An investment center is the most like an independent business because it is responsible for revenues, costs and investment; and it is measured on its return on investment as well as on its level of profit.

C. A cost center is responsible only for costs and not revenues. Therefore, it is not like an independent business.

D. A revenue center is not responsible for costs, and in that respect does not resemble an independent business.

What is the contribution margin of Division B?

A. $235,000
B. $265,000
C. $150,000
D. $205,000

A. The contribution margin of Department B is equal to the total revenues of Department B less total variable costs of Department B. See the correct answer for a complete explanation.

B. The contribution margin of Department B is equal to the total revenues of Department B less total variable costs of Department B. It is calculated as follows: $400,000 + $15,000 − $65,000 − $40,000 − $15,000 − 30,000 = $265,000.

C. This answer assumes that fixed costs are also deductible. However, contribution margin is calculated as total
revenues minus total variable costs.

D. The contribution margin of Department B is equal to the total revenues of Department B minus the total variable costs of Department B. See the correct answer for a complete explanation.

---

**Question 14** - CIA 594 III-40 - Responsibility Centers and Reporting Segments

Which of the following is not true about international transfer prices for a multinational firm?

A. Allows the firm to evaluate each division.
B. Allows firms to correctly price products in each country in which it operates.
C. Allows firms to attempt to minimize worldwide taxes.
D. Provides each division with a profit-making orientation.

A. A well-devised transfer price enables the company to evaluate each of its divisions.

B. The transfer price is the price used for internal transactions. This by itself does not enable the firm to determine the appropriate external price in each country in which it operates.

C. Though firms are greatly restricted by tax codes in the setting of transfer prices for tax purposes, some possibilities exist for flexibility in transfer pricing policies to reduce the tax burden, as long as the multinational corporation remains within the legal guidelines. Examples of these possibilities to minimize taxes include charging administrative fees, royalties, and service fees. Each of these alternatives are of course subject to the principle of being arms-length transactions and must be based on actual business activity.

D. If the transfer price is properly set, each division will be able to make decisions that are profit motivated, not governed from above.

---

**Question 15** - CMA 1291 3-8 - Responsibility Centers and Reporting Segments

A segment of an organization is referred to as a profit center if it has

A. Authority to make decisions affecting the major determinants of profit including the power to choose its markets and sources of supply.
B. Authority to make decisions affecting the major determinants of profit including the power to choose its markets and sources of supply and significant control over the amount of invested capital.
C. Authority to provide specialized support to other units within the organization.
D. Authority to make decisions over the most significant costs of operations including the power to choose the sources of supply.

A. By definition, a profit center is a segment of the organization that has authority to make decisions affecting the major determinants of profit, i.e., revenues and expenses. This includes the power to choose its markets and sources of supply.

B. This is the definition of an investment center.

C. This is refers to support center and it is not classified as a center under responsibility accounting.

D. This is the definition of a cost center.

---

**Question 16** - CMA 1296 3-24 - Responsibility Centers and Reporting Segments

(c) HOCK international, page 7
The inventory control supervisor at Wilson Manufacturing Corporation reported that a large quantity of a part purchased for a special order that was never completed remains in stock. The order was not completed because the customer defaulted on the order. The part is not used in any of Wilson's regular products. After consulting with Wilson's engineers, the vice president of production approved the substitution of the purchased part for a regular part in a new product. Wilson's engineers indicated that the purchased part could be substituted providing it was modified. The units manufactured using the substituted part required additional direct labor hours resulting in an unfavorable direct labor efficiency variance in the Production Department. The unfavorable direct labor efficiency variance resulting from the substitution of the purchased part in inventory would best be assigned to the

A. Sales manager.
B. Inventory supervisor.
C. Production manager.
D. Vice president of production.

A. The sales manager was not involved in production and decision making about the substitution of the regular materials for the special order materials.

B. The inventory supervisor was not involved in production and decision making about the substitution of the regular materials for the special order materials.

C. The production manager was not involved in the decision making about the substitution of the regular materials for the special order materials.

D. The vice president of production made the decision about the substitution of the regular materials for the special order materials. Thus, the unfavorable direct labor efficiency variance resulting from the substitution of the purchased part in inventory would best be assigned to the vice president of production.

---

**Question 17 - CMA 1296 3-21 - Responsibility Centers and Reporting Segments**

David Rogers, purchasing manager at Fairway Manufacturing Corporation, was able to acquire a large quantity of raw material from a new supplier at a discounted price. Marion Conner, inventory supervisor, is concerned because the warehouse has become crowded and some things had to be rearranged. Brian Jones, vice president of production, is concerned about the quality of the discounted material. However, the Engineering Department tested the new raw material and indicated that it is of acceptable quality. At the end of the month, Fairway experienced a favorable materials usage variance, a favorable labor usage variance, and a favorable materials price variance. The usage variances were solely the result of a higher yield from the new raw material. The favorable materials price variance would be considered the responsibility of the

A. Vice president of production.
B. Engineering manager.
C. Purchasing manager.
D. Inventory supervisor.

A. The vice president of production was concerned only about the quality of new material in this situation. The vice president does not participate in purchasing activity and usually can't influence the price of materials.

B. The engineering manager does not participate in purchasing activity and usually can't influence the price of materials.

C. The material price variance is the difference between the actual price and the standard price times the actual quantity of materials consumed by production. The purchasing manager is usually responsible for the material price variance, as the price is determined during the purchasing activity.

D. The inventory supervisor is not responsible for the price variance, because he or she does not participate in purchasing activity and usually can't influence the price of materials.
Question 18 - CMA 694 3-21 - Responsibility Centers and Reporting Segments

Under a standard cost system, the materials efficiency variances are the responsibility of

A. Sales and industrial engineering.
B. Purchasing and industrial engineering.
C. Purchasing and sales.
D. Production and industrial engineering.

A. Industrial engineers are involved in designing product and setting the standards of material usage, thus bearing a part of the responsibility for the efficiency of material usage. However, sales personnel rarely can influence material usage by production workers.

B. Industrial engineers are involved in designing product and setting the standards of material usage, thus bearing a part of the responsibility for the efficiency of material usage. However, purchasing personnel rarely can influence material usage by production workers.

C. Purchasing and sales personnel rarely can influence material usage by production workers.

D. Industrial engineers are involved in designing product and setting the standards of material usage, thus bearing a part of the responsibility for the efficiency of material usage. Production workers are those who actually convert materials into the finished product and directly responsible for efficiency of material usage. Therefore, both of these parties will have some responsibility for the materials efficiency variance.

Question 19 - CIA 1193 IV-18 - Responsibility Centers and Reporting Segments

One department of an organization, Final Assembly, is purchasing subcomponents from another department, Materials Fabrication. The price that will be charged to Final Assembly by Materials Fabrication is to be determined. Outside market prices for the subcomponents are available. Which of the following is the most correct statement regarding a market-based transfer price?

A. Marginal production cost transfer prices provide incentives to use otherwise idle capacity.
B. Overall long term competitiveness is enhanced with a market-based transfer price.
C. Corporate politics is more of a factor in a market-based transfer price than with other methods.
D. Market transfer prices provide an incentive to use otherwise idle capacity.

A. If the marginal cost of production is used as the transfer price there is no incentive to use otherwise idle facilities because there will not be any contribution received from the units that are produced. Also, marginal costs of production would not be the transfer price if a market based transfer price is used.

B. This is a very general, but true, statement. A market based transfer price will lead to the greatest good for the company in the long-term. Other, artificial, transfer prices will lead to behavior that is not in the best interest of the company as a whole.

C. In all methods of transfer pricing, corporate politics will play a role. In market based transfer pricing, corporate politics are probably a little bit less as the market is setting the price and the market is outside the influence of the company, or of individuals within it.

D. A transfer price equal to the market price will provide incentives for the producing department to increase production, but will not provide any incentive for the purchasing department to purchase internally.

Question 20 - CMA 696 3-28 - Responsibility Centers and Reporting Segments

Parkside Inc. has several divisions that operate as decentralized profit centers. Parkside’s Entertainment Division manufactures video arcade equipment using the products of two of Parkside’s other divisions. The Plastics Division manufactures plastic components, one type that is made exclusively for the Entertainment Division, while other less
complex components are sold to outside markets. The products of the Video Cards Division are sold in a competitive market; however, one video card model is also used by the Entertainment Division. The actual costs per unit used by the Entertainment Division are presented below.

<table>
<thead>
<tr>
<th></th>
<th>Plastic Components</th>
<th>Video Cards</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct material</td>
<td>$1.25</td>
<td>$2.40</td>
</tr>
<tr>
<td>Direct labor</td>
<td>2.35</td>
<td>3.00</td>
</tr>
<tr>
<td>Variable overhead</td>
<td>1.00</td>
<td>1.50</td>
</tr>
<tr>
<td>Fixed overhead</td>
<td>.40</td>
<td>2.25</td>
</tr>
<tr>
<td>Total cost</td>
<td>$5.00</td>
<td>$9.15</td>
</tr>
</tbody>
</table>

The Plastics Division sells its commercial products at full cost plus a 25% markup and believes the proprietary plastic component made for the Entertainment Division would sell for $6.25 per unit on the open market. The market price of the video card used by the Entertainment Division is $10.98 per unit.

Assume that the Plastics Division has excess capacity and it has negotiated a transfer price of $5.60 per plastic component with the Entertainment Division. This price will

A. Motivate both divisions as estimated profits are shared.
B. Demotivate the Plastics Division causing mediocre performance.
C. Cause the Plastics Division to reduce the number of commercial plastic components it manufactures.
D. Encourage the Entertainment Division to seek an outside source for plastic components.

A. Because the Plastics Division has excess capacity, this price is a mutually motivating price. The price for the purchasing division is less than it would pay in the market and the price for the selling division is higher than its variable costs of production. So, both divisions end up in a better position because of this price.

B. Given that the transfer price is higher than the variable costs of production, there is no reason for the producing division to be demotivated.

C. Because this price is above the variable costs of production, the Plastics Division would have no reason to reduce production because even what it sells internally generates a contribution.

D. Because the price is lower than the market price, the Entertainment Division will not seek an outside supplier.

---

**Question 21 - CMA 1292 3-22 - Responsibility Centers and Reporting Segments**

When using a contribution margin format for internal reporting purposes, the major distinction between segment manager performance and segment performance is

A. Direct variable costs of producing the product.
B. Direct fixed cost controllable by others.
C. Unallocated fixed cost.
D. Direct fixed cost controllable by the segment manager.

A. The difference between segment manager performance and segment performance is noncontrollable fixed costs that are traceable. Direct variable costs of production are included in both measures.

B. The difference between segment manager performance and segment performance is noncontrollable fixed costs that are traceable. These are fixed costs that are controlled by others.

C. The difference between segment manager performance and segment performance is noncontrollable fixed costs that are traceable. Unallocated fixed costs are not used in either measure.

D. The difference between segment manager performance and segment performance is noncontrollable fixed costs that are traceable. Direct fixed costs controlled by the segment manager are included in both measures.
**Question 22 - CMA 696 3-27 - Responsibility Centers and Reporting Segments**

Parkside Inc. has several divisions that operate as decentralized profit centers. Parkside's Entertainment Division manufactures video arcade equipment using the products of two of Parkside’s other divisions. The Plastics Division manufactures plastic components, one type that is made exclusively for the Entertainment Division, while other less complex components are sold to outside markets. The products of the Video Cards Division are sold in a competitive market; however, one video card model is also used by the Entertainment Division. The actual costs per unit used by the Entertainment Division are presented below.

<table>
<thead>
<tr>
<th></th>
<th>Plastic Components</th>
<th>Video Cards</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct material</td>
<td>$1.25</td>
<td>$2.40</td>
</tr>
<tr>
<td>Direct labor</td>
<td>2.35</td>
<td>3.00</td>
</tr>
<tr>
<td>Variable overhead</td>
<td>1.00</td>
<td>1.50</td>
</tr>
<tr>
<td>Fixed overhead</td>
<td>.40</td>
<td>2.25</td>
</tr>
<tr>
<td><strong>Total cost</strong></td>
<td><strong>$5.00</strong></td>
<td><strong>$9.15</strong></td>
</tr>
</tbody>
</table>

The Plastics Division sells its commercial products at full cost plus a 25% markup and believes the proprietary plastic component made for the Entertainment Division would sell for $6.25 per unit on the open market. The market price of the video card used by the Entertainment Division is $10.98 per unit.

Assume that the Entertainment Division is able to purchase a large quantity of video cards from an outside source at $8.70 per unit. The Video Cards Division, having excess capacity, agrees to lower its transfer price to $8.70 per unit. This action would

A. Allow evaluation of both divisions on the same basis.
B. Optimize the overall profit goals of Parkside Inc.
C. Optimize the profit goals of the Entertainment Division while subverting the profit goals of Parkside Inc.
D. Subvert the profit goals of the Video Cards Division while optimizing the profit goals of the Entertainment Division.

A. A transfer price of $8.70 per unit is less than the Video Cards Division's total cost of production, whereas the price is the Entertainment Division's market price. This would not allow the evaluation of both divisions on the same basis.

B. This action is goal congruent. The Entertainment Division is indifferent as to where to buy video cards, since the external price is the same as the internal price. The overall profit goals of Parkside Inc. would be optimized because the variable cost of production of the Video Cards division is less than the suggested discounted price. Thus, the use of idle capacity enhances profits.

C. The Entertainment Division's profit goals are not optimized because the Entertainment Division is indifferent as to where to buy the video cards, since the external price is the same as the internal price. The profit goals of Parkside Inc. would not be subverted because this action would be congruent with overall profit goals of the company. The suggested discounted price is above the variable cost of production for the Video Cards Division; thus, the use of idle capacity enhances profits.

D. The profit goals of the Video Cards Division would be subverted in this case. However, the Entertainment Division's profit goals are not optimized because the Entertainment Division is indifferent as to where to buy the video cards, since the external price is the same as the internal price.

**Question 23 - CMA 696 3-26 - Responsibility Centers and Reporting Segments**

Parkside Inc. has several divisions that operate as decentralized profit centers. Parkside's Entertainment Division manufactures video arcade equipment using the products of two of Parkside’s other divisions. The Plastics Division manufactures plastic components, one type that is made exclusively for the Entertainment Division, while other less complex components are sold to outside markets. The products of the Video Cards Division are sold in a competitive market; however, one video card model is also used by the Entertainment Division. The actual costs per unit used by the Entertainment Division are presented below.

(c) HOCK international, page 11
market; however, one video card model is also used by the Entertainment Division. The actual costs per unit used by the Entertainment Division are presented below.

<table>
<thead>
<tr>
<th>Component</th>
<th>Plastic</th>
<th>Video Cards</th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct material</td>
<td>$1.25</td>
<td>$2.40</td>
</tr>
<tr>
<td>Direct labor</td>
<td>2.35</td>
<td>3.00</td>
</tr>
<tr>
<td>Variable overhead</td>
<td>1.00</td>
<td>1.50</td>
</tr>
<tr>
<td>Fixed overhead</td>
<td>.40</td>
<td>2.25</td>
</tr>
<tr>
<td>Total cost</td>
<td>$5.00</td>
<td>$9.15</td>
</tr>
</tbody>
</table>

The Plastics Division sells its commercial products at full cost plus a 25% markup and believes the proprietary plastic component made for the Entertainment Division would sell for $6.25 per unit on the open market. The market price of the video card used by the Entertainment Division is $10.98 per unit.

A per-unit transfer price from the Video Cards Division to the Entertainment Division at full cost, $9.15, would

A. Allow evaluation of both divisions on a competitive basis.
B. Encourage the Entertainment Division to purchase video cards from an outside source.
C. Provide no profit incentive for the Video Cards Division to control or reduce costs.
D. Satisfy the Video Cards Division's profit desire by allowing recovery of opportunity costs.

A. This transfer price does not allow for the evaluation of both divisions on a competitive basis. The Entertainment Division would be 'buying' video cards from the Video Cards Division at a 'full cost' transfer price; but it would be selling its product at market price. Therefore, the Entertainment Division would have an opportunity to be more profitable than the Video Cards Division would.

B. A transfer price of full cost would be beneficial to the Entertainment Division, the buying department, as it is less than market price.

C. This transfer price does not provide a profit incentive to the Video Cards Division, as it covers only the costs of production and does not allow a profit. It also does not encourage the Video Cards Division to reduce costs, as the full cost transfer price is being passed on to the Entertainment Division.

D. This transfer price does not satisfy the Video Cards Division's profit desire by allowing the recovery of opportunity costs because the transfer price is a full cost price and it does not include any profit for the Video Cards Division.

**Question 24 - CIA 1190 IV-20 - Responsibility Centers and Reporting Segments**

A limitation of transfer prices based on actual cost is that they

A. Charge inefficiencies to the department that is transferring the goods.
B. Can lead to suboptimal decisions for the company as a whole.
C. Lack clarity and administrative convenience.
D. Must be adjusted by some markup.

A. Inefficiencies are charged to the department that is receiving, not transferring, the goods.

B. The basic issue of transfer prices is how much should one unit of a company charge another unit of the same company for its goods or services. The goal in setting a transfer price is that the method used will stimulate the department managers to do what will provide the greatest benefit to the company as a whole, rather than to act in their own interest. Transfer price based on actual cost does not motivate managers to use resources more efficiently which can lead to suboptimal decisions for the company as a whole.

C. Cost-based transfer price provide clarity and administrative convenience.

D. In cost-based transfer pricing, costs do not need to be adjusted by any markup.
Question 25 - CIA 587 IV-15 - Responsibility Centers and Reporting Segments

Overtime conditions and pay were recently set by the personnel department. The production department has just received a request for a rush order from the sales department. The production department protests that additional overtime costs will be incurred as a result of the order. The sales department argues that the order is from an important customer. The production department processes the order. To control costs, which department should never be charged with the overtime costs generated as a result of the rush order?

A. Shared by production department and sales department.  
B. Production department.  
C. Sales department.  
D. Personnel department.

A. The overtime premium should be charged to the department that is responsible for the overhead being worked. If the reason that overtime is worked is simply that the volume of work requires it, the overtime premium is charged to overhead and allocated to all of the units produced. Given the situation in this question, it is reasonable that the overtime premium be charged to both the production and sales departments.

B. The overtime premium should be charged to the department that is responsible for the overhead being worked. If the reason that overtime is worked is simply that the volume of work requires it, the overtime premium is charged to overhead and allocated to all of the units produced. Given the situation in this question, it is reasonable that at least some of the overtime premium be charged to the production department.

C. The overtime premium should be charged to the department that is responsible for the overhead being worked. If the reason that overtime is worked is simply that the volume of work requires it, the overtime premium is charged to overhead and allocated to all of the units produced. Given the situation in this question, it is reasonable that at least some of the overtime premium be charged to the sales department.

D. The overtime premium should be charged to the department that is responsible for the overhead being worked. If the reason that overtime is worked is simply that the volume of work requires it, the overtime premium is charged to overhead and allocated to all of the units produced. Because the personnel department would not have been able to cause or prevent the overtime work, the costs should not be charged to the personnel department.

Question 26 - CMA 692 3-23 - Responsibility Centers and Reporting Segments

The WK Company uses a performance reporting system that reflects the company's decentralization of decision making. The departmental performance report shows one line of data for each subordinate who reports to the group vice president. The data presented show the actual costs incurred during the period, the budgeted costs, and all variances from budget for that subordinate's department. The WK Company is using a system called

A. Program budgeting.  
B. Responsibility accounting.  
C. Flexible budgeting.  
D. Cost-benefit accounting.

A. This is a budgeting system and it does not describe the situation in the question.

B. Responsibility accounting is a system in which costs are allocated to managers and/or departments based on who is responsible for the incurrence of the costs. This is the method described in the question.

C. Flexible budgeting is the adaptation of variable items in the static budget to reflect the actual level of activity achieved during the period. This is not what is described in the question.

D. Cost-benefit accounting is not an accounting method or a reporting system.
Question 27 - CIA 1183 IV-5 - Responsibility Centers and Reporting Segments

A company has two divisions, A and B, each operated as a profit center. A charges B $35 per unit for each unit transferred to B. Other data follow:

- A's variable cost per unit: $30
- A's fixed costs: $10,000
- A's annual sales to B: 5,000 units
- A's sales to outsiders: 50,000 units

A is planning to raise its transfer price to $50 per unit. Division B can purchase units at $40 each from outsiders, but doing so would idle A's facilities now committed to producing units for B. Division A cannot increase its sales to outsiders. From the perspective of the company as a whole, from whom should Division B acquire the units, assuming B's market is unaffected?

A. Division A, despite the increased transfer price.
B. Division A, but only until fixed costs are covered, then from outside vendors.
C. Outside vendors.
D. Division A, but only at the variable cost per unit.

A.

When the variable costs plus the opportunity cost of lost outside sales for the internal supplier are lower than the price of the external supplier, the company as a whole is better off if the buying department buys internally, even if the transfer price is higher than an outside supplier’s price. In this case, there is no opportunity cost of lost sales, because the question tells us that purchasing from outside would idle A’s facilities now committed to producing units for B, and Division A cannot increase its sales to outsiders. Therefore, the total cost of producing the units internally is the variable cost of $30, which is lower than the outside price of $40. Thus, from the perspective of the company as a whole, Division B should continue purchasing from Division A, despite the increased transfer price.

In reality, Department B should not simply accept the new transfer price of $50. The managers of the two divisions should agree on a transfer price that is acceptable to both of them. It may be that senior management will need to get involved in order to make that happen, if the two division heads cannot agree. However, that is not given as an answer choice, and of the answer choices given, this is the best choice.

B.

The fixed costs are not relevant, since they will be the same regardless of where Division B gets the parts.

C. Purchasing from outside in this situation will cause the company to pay more for each unit and to lose some contribution to its fixed costs from the internal sales. When the variable costs plus the opportunity cost of lost outside sales for the internal supplier are lower than the price of the external supplier, the company as a whole is better off if the buying department buys internally, even if the transfer price is higher than an outside supplier’s price. In this case, there is no opportunity cost of lost sales, because the question tells us that purchasing from outside would idle A’s facilities now committed to producing units for B, and Division A cannot increase its sales to outsiders. Therefore, the total cost of producing the units internally is the variable cost of $30, which is lower than the outside price of $40.

D. There are many acceptable methods of determining a transfer price. The best method for a particular situation depends upon the circumstances. This question asks what is the best course of action from the perspective of the company as a whole. Whenever the variable costs plus the opportunity cost of lost outside sales for the internal supplier are lower than the price of the external supplier, the company as a whole is better off if the buying department buys internally, even if the transfer price is higher than an outside supplier’s price. In this case, there is no opportunity cost of lost sales, because the question tells us that purchasing from outside would idle A’s facilities now committed to producing units for B, and Division A cannot increase its sales to outsiders. Therefore, the total cost of producing the units internally is the variable cost of $30, which is lower than the outside price of $40. Thus, in this situation, the transfer cost used is not relevant to the decision.
Question 28 - CMA 694 3-28 - Responsibility Centers and Reporting Segments

DigitalTech uses an accounting system that charges costs to the manager who has the authority to make decisions incurring the costs. For example, if a sales manager authorizes a rush order that results in additional manufacturing costs, these additional costs are charged to the sales manager. This type of accounting system is known as

A. Functional accounting.
B. Responsibility accounting.
C. Contribution accounting.
D. Transfer-pricing accounting.

A. Functional accounting assigns costs based on the function that is performed. See the correct answer for a complete explanation.

B. Responsibility accounting is a system in which an individual is held accountable (responsible) for things that he or she is able to control. It is this person’s responsibility to address any issues that arise related to these costs that they control.

C. Contribution margin analysis focuses on the variable revenues and costs and their behavior as activity levels change. The selling price minus variable costs is the contribution margin. Fixed costs are then subtracted from the contribution to determine the profit.

D. Transfer prices are the prices used in the ‘sale’ of goods within the company. See the correct answer for a complete explanation.

Question 29 - CIA 594 III-44 - Responsibility Centers and Reporting Segments

A firm prepared a segmented income statement that included the following data for its suburban marketing segment:

Fixed costs controllable by the suburban marketing segment manager $150,000
Fixed suburban marketing costs controllable by corporate management $250,000
Fixed manufacturing costs allocated to the suburban marketing segment $110,000
Variable manufacturing costs $200,000
Variable selling costs $100,000
Variable administrative costs $130,000
Net sales $950,000

The best measure of the economic performance of the suburban marketing segment is:

A. $10,000
B. $520,000
C. $120,000
D. $370,000

A. This answer incorrectly includes the allocated fixed costs. See the correct answer for a complete explanation.

B. This answer is the contribution margin of sales minus variable costs and fails to take into account the fixed costs that are controllable by the segment.

C. The suburban marketing segment should be measured by what it controls and by fixed costs traceable to it, even if not controlled by it. This is called the segment margin, and the expenses included in it are the segment’s variable costs, fixed costs it controls and fixed costs that are controllable by corporate management.
Segment manager performance includes only costs controllable by the segment manager. Segment manager performance would not include fixed costs controllable by the corporate management.

However, in this question we are measuring the segment, not the segment manager, because the question asks for the best measure of the economic performance of the segment. The segment margin includes the following items: Fixed costs controllable by the suburban marketing manager ($150,000), fixed costs controllable by corporate management ($250,000), the three types of variable costs ($430,000 in total) and the sales ($950,000). In total, this gives a margin for the segment of $120,000.

D. This answer does not include the fixed costs controllable by the company's management. This needs to be included in segment performance, but it would not be included in segment manager performance.

Question 30 - CMA 1296 3-16 - Responsibility Centers and Reporting Segments

Rockford Manufacturing Corporation uses a responsibility accounting system in its operations. Which one of the following items is least likely to appear in a performance report for a manager of one of Rockford's assembly lines?

A. Direct labor.
B. Materials.
C. Depreciation on the manufacturing facility.
D. Repairs and maintenance.

A. Direct labor would be controllable by the manager of an assembly line and would therefore be included on the manager's report.

B. Materials would be controllable by the manager of an assembly line and would therefore be included on the manager's report.

C. Depreciation on the manufacturing facility is a cost that is dependent upon past decisions made at a higher level of the organization, as well as on the accounting policies adopted by management. Therefore, it is outside of the control of an assembly line manager and would not be included on the manager's performance report.

D. Repairs and maintenance would be controllable by the manager of an assembly line and would therefore be included on the manager's report.

Question 31 - CIA 1192 IV-22 - Responsibility Centers and Reporting Segments

An organization employs a system of internal reporting that furnishes departmental managers with revenue and cost information on only those items that are subject to their control. Items not subject to the manager's control are not included in the performance reports. This method of accounting is known as

A. Segment reporting.
B. Contribution margin reporting.
C. Responsibility accounting.
D. Absorption cost accounting.

A. Segment reporting is the reporting of results by segment: product line, geography or some other distinguishing characteristic. This is not descriptive of the method used by this company.

B. Contribution margin reporting breaks costs down into fixed and variable costs. While this may be used in conjunction with responsibility accounting, this by itself is not describing the method used by the company.

C. Responsibility accounting is a system in which cost and revenue data is reported based on who (manager or division) is able to control them or is responsible for them. This is the system described in the
question.

D. Absorption cost accounting relates to the allocation of fixed costs. This is not descriptive of the method used by this company.

Question 32 - CIA 1188 IV-23 - Responsibility Centers and Reporting Segments

The price that one division of a company charges another division for goods or services provided is called the

A. Outlay price.
B. Market price.
C. Distress price.
D. Transfer price.

A. The outlay price is one approach to determining a transfer price.
B. The market price is determined purely by the forces of supply and demand without interference from an outside source. This concept assumes that markets are efficient, which is not always true in practice. Market price is one of many possible approaches to determining a transfer price.
C. The distress price is a reduced price (sometimes significantly) that occurs in urgent sales. Distress price is not an approach to determining a transfer price.
D. The transfer price is the price charged by one unit of the company to another unit of the same company for the services or goods produced by the first unit and "sold" to the second unit.

Question 33 - CMA 695 3-28 - Responsibility Centers and Reporting Segments

In responsibility accounting, a center’s performance is measured by controllable costs. Controllable costs are best described as including

A. Direct material and direct labor, only.
B. Those costs about which the manager is knowledgeable and informed.
C. Only those costs that the manager can influence in the current time period.
D. Only discretionary costs.

A. Other types of costs (for example, marketing) are costs that may be controllable by a manager.
B. Just because a manager has knowledge and information about a cost does not mean that the cost is controllable by that manager.
C. A definition of a controllable cost is a cost that the manager is able to influence in the time period under consideration.
D. Other costs besides discretionary costs may also be controllable by a manager.

Question 34 - CMA 694 3-30 - Responsibility Centers and Reporting Segments

An appropriate transfer price between two divisions of The Stark Company can be determined from the following data:

Fabricating Division
Market price of subassembly $50
Variable cost of subassembly $20
Excess capacity (in units) 1,000

**Assembling Division**
Number of units needed 900

What is the natural bargaining range for the two divisions?

A. Any amount less than $50.
B. Between $20 and $50.
C. $50 is the only acceptable price.
D. Between $50 and $70.

A. The transfer price should not be lower than the variable costs of production, even if there is excess capacity. As long as selling price covers the variable costs and even a very small amount of fixed costs in case of excess capacity, it is beneficial to the company.

B. The basic issue of transfer prices is simply how much should one unit of a company charge another unit of the same company for its goods or services. The goal in setting a transfer price is that the method used will stimulate both the buying and selling department managers to do what will provide the greatest benefit to the company as a whole, rather than to act in their own interest. When there is an external market for the product, market price is almost always the best transfer price to use. Thus, market price is at the maximum of the natural range. When the company has idle capacity, the variable cost approach to determining the transfer price also works well. Since the Fabricating Division has enough capacity to fulfill the demand of the Assembling Division without any over-time, the variable cost approach is also acceptable and is at the minimum of the natural range.

C. An acceptable price is within a range, and $50 is not the only acceptable price.

D. It would subvert overall profit goals of the company to choose a transfer price above the free market level.

---

**Question 35** - CMA 686 4-14 - Responsibility Centers and Reporting Segments

The segment margin of the Wire Division of Lerner Corporation should **not** include

A. Variable selling expenses of the Wire Division.
B. The Wire Division's fair share of the salary of Lerner Corporation's president.
C. Fixed selling expenses of the Wire Division.
D. Net sales of the Wire Division.

A. Segment margin includes sales, variable costs, controllable fixed costs and traceable fixed costs. Variable selling expenses should be included in the segment margin of this division.

B. **Segment margin includes sales, variable costs, controllable fixed costs and traceable fixed costs. The allocation of the president's salary is an untraceable fixed cost and should not be included in segment margin of this division.**

C. Segment margin includes sales, variable costs, controllable fixed costs and traceable fixed costs. Fixed selling expenses are controllable and should be included in the segment margin of this division.

D. Segment margin includes sales, variable costs, controllable fixed costs and traceable fixed costs. Sales should be included in the segment margin of this division.

---

**Question 36** - CIA 1193 IV-20 - Responsibility Centers and Reporting Segments

---

(c) HOCK international, page 18
A and B are autonomous divisions of a corporation. They have no beginning or ending inventories, and the number of units produced is equal to the number of units sold. Following is financial information relating to the two divisions.

<table>
<thead>
<tr>
<th>Division</th>
<th>A</th>
<th>B</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sales</td>
<td>$150,000</td>
<td>$400,000</td>
</tr>
<tr>
<td>Other revenue</td>
<td>10,000</td>
<td>15,000</td>
</tr>
<tr>
<td>Direct materials</td>
<td>30,000</td>
<td>65,000</td>
</tr>
<tr>
<td>Direct labor</td>
<td>20,000</td>
<td>40,000</td>
</tr>
<tr>
<td>Variable factory overhead</td>
<td>5,000</td>
<td>15,000</td>
</tr>
<tr>
<td>Fixed factory overhead</td>
<td>25,000</td>
<td>55,000</td>
</tr>
<tr>
<td>Variable selling and administrative expense</td>
<td>15,000</td>
<td>30,000</td>
</tr>
<tr>
<td>Fixed selling and administrative expense</td>
<td>35,000</td>
<td>60,000</td>
</tr>
<tr>
<td>Central corporate expenses (allocated)</td>
<td>12,000</td>
<td>20,000</td>
</tr>
</tbody>
</table>

What is the total contribution to corporate profits generated by Division A before allocation of central corporate expenses?

A. $20,000
B. $18,000
C. $30,000
D. $80,000

A. In this answer the other revenues are not added. These revenues should be included in the calculation. See the correct answer for a complete explanation.
B. In this answer the central corporate expenses allocated are deducted. However, those expenses should not be included in calculation. See the correct answer for a complete explanation.
C. Department A's contribution to the corporate profits is calculated as all revenues minus all expenses except the allocated central corporate expenses. It is calculated as follows: $150,000 + $10,000 − $30,000 − $20,000 − $5,000 − $25,000 − $15,000 − $35,000 = $30,000.
D. In this answer total S&A expenses are not deducted. However, those expenses should be included in the calculation. See the correct answer for a complete explanation.

Question 37 - CIA 589 IV-16 - Responsibility Centers and Reporting Segments

Division A of a company is currently operating at 50% capacity. It produces a single product and sells all its production to outside customers for $13 per unit. Variable costs are $7 per unit, and fixed costs are $6 per unit at the current production level. Division B, which currently purchases this product from an outside supplier for $12 per unit, would like to purchase the product from Division A. Division A will operate at 80% capacity to meet outside customers' and Division B's demand. What is the minimum price that Division A should charge Division B for this product?

A. $13.00 per unit.
B. $12.00 per unit.
C. $9.60 per unit.
D. $7.00 per unit.

A. When operating below capacity, the minimum price that the producing department will sell for is the variable cost of production. See the correct answer for a complete explanation.
B. When operating below capacity, the minimum price that the producing department will sell for is the variable cost of production. See the correct answer for a complete explanation.
C. When operating below capacity, the minimum price that the producing department will sell for is the variable cost

(c) HOCK international, page 19
of production. See the correct answer for a complete explanation.

**D. When operating below capacity, the minimum price that the producing department will sell for is the variable cost of production. This is $7 in this question.**

---

**Question 38 - CMA 1295 3-5 - Responsibility Centers and Reporting Segments**

Responsibility accounting defines an operating center that is responsible for revenue and costs as a(n)

A. Division.
B. Profit center.
C. Operating unit.
D. Revenue center.

A. A division could be any of the different types of responsibility centers.

**B. A profit center is responsible for both revenues and costs.**

C. An operating unit could be any of the different types of responsibility centers.

D. A revenue center is responsible only for revenues and not for costs.

---

**Question 39 - CMA 1293 3-21 - Responsibility Centers and Reporting Segments**

A successful responsibility accounting reporting system is dependent upon

A. A reasonable separation of costs into their fixed and variable components since fixed costs are not controllable and must be eliminated from the responsibility report.
B. Identification of the management level at which all costs are controllable.
C. The correct allocation of controllable variable costs.
D. The proper delegation of responsibility and authority.

A. Some fixed costs are controllable by the different managers so they should be included in the responsibility report. See the correct answer for a complete explanation.

B. Not only is the control of a cost relevant in responsibility accounting, but in some cases the responsibility for the cost being incurred may also be relevant to the allocation of costs for the responsibility report. For example, if a manager makes a decision that causes additional costs to be incurred in a different department, those additional costs should be 'allocated' to the manager who caused them to be incurred, even if that manager is unable to control the costs themselves. Therefore, costs are not controlled at any specific management level but by individual managers' actions.

C. There are some fixed costs that will also be controllable and therefore should also be included on the responsibility report.

**D. The identification of who is responsible for the costs being incurred and the control over the costs themselves is critical to the effectiveness of a responsibility accounting system. This can be done through the proper delegation of responsibility and authority.**

---

**Question 40 - CMA 694 3-27 - Responsibility Centers and Reporting Segments**

The Stonebrook Company uses a performance reporting system that reflects the company's decentralization of decision making. The departmental performance reports show actual costs incurred during the period against

(c) HOCK international, page 20
budgeted costs. Any variances from the budget are assigned to the individual department manager who controls the costs. Stonebrook is using a type of system called

A. Responsibility accounting.
B. Activity-based budgeting.
C. Flexible budgeting.
D. Transfer-pricing accounting.

A. Responsibility accounting is a system in which an individual is held accountable (responsible) for things that he or she is able to control. It is this person's responsibility to address any issues that arise related to these items that they control.

B. Activity based budgeting is a budgeting concept in which the budget is built using activities that cause costs to be incurred. See the correct answer for a complete explanation.

C. Flexible budgeting is the adaptation of variable revenues and expenses in the static budget to reflect the actual level of activity achieved during the period. See the correct answer for a complete explanation.

D. Transfer prices are the prices used in the ‘sale’ of goods within the company. See the correct answer for a complete explanation.

Question 41 - CMA 1294 3-22 - Responsibility Centers and Reporting Segments

If a manufacturing company uses responsibility accounting, which one of the following items is least likely to appear in a performance report for a manager of an assembly line?

A. Supervisory salaries.
B. Materials.
C. Repairs and maintenance.
D. Equipment depreciation.

A. In accordance with responsibility accounting, a manager should be held responsible only for those factors which he or she can control. The assembly line manager will have input into determining the salaries of supervisors under him or her. Therefore, supervisory salaries are controllable by the manager, so they should be included in the assembly line manager's performance report.

B. In accordance with responsibility accounting, a manager should be held responsible only for those factors which he or she can control. The assembly line manager will have control over the materials used and therefore those costs should be included in the performance report of the assembly line manager.

C. In accordance with responsibility accounting, a manager should be held responsible only for those factors which he or she can control. The assembly line manager will have control over repairs and maintenance and therefore those costs should be included in the performance report of the assembly line manager.

D. In accordance with responsibility accounting, a manager should be held responsible only for those factors which he or she can control. Costs of fixed assets and depreciation methods and policies are not under the control of an assembly line manager, because those things are decided at a higher level. Therefore, equipment depreciation expense would not normally be included in a performance report for the assembly line manager under responsibility accounting.

Question 42 - CIA 593 IV-16 - Responsibility Centers and Reporting Segments

Which of the following is the most significant disadvantage of a cost-based transfer price?

A. Requires internally developed information.
B. Imposes market effects on company operations.
C. May not promote long-term efficiencies.
D. Requires externally developed information.

A. Other transfer price methods require internally generated information and the information that is needed for transfer pricing decisions is information that is needed for other purposes as well and is probably already produced by the company.

B. Market conditions being imposed within the company are a result of a market-based transfer price.

C. When the transfer price is based on the costs of production, the producing department has no incentive to control costs. Therefore, because there is no need to control costs, inefficiencies may creep into the process over time.

D. Externally generated information is required for market-based transfer pricing.

---

**Question 43 - CMA 1294 3-20 - Responsibility Centers and Reporting Segments**

Fairmount Inc. uses an accounting system that charges costs to the manager who has been delegated the authority to make the decisions incurring the costs. For example, if the sales manager accepts a rush order that will result in higher than normal manufacturing costs, these additional costs are charged to the sales manager because the authority to accept or decline the rush order was given to the sales manager. This type of accounting system is known as

A. Functional accounting.
B. Transfer price accounting.
C. Responsibility accounting.
D. Reciprocal allocation.

A. Functional accounting allocates costs according to the function they represent. Functional accounting does not use the responsibility for the incurrence of cost to allocate the costs.

B. Transfer price accounting is related to the determination of the price to charge for intercompany sales.

C. Responsibility accounting is a system in which costs are allocated to managers and/or departments based on who is responsible for the incurrence of the costs. This is the method described in the question.

D. Reciprocal allocation is a method of allocating the costs of service departments to other service departments and the production departments.

---

**Question 44 - CMA 1292 3-13 - Responsibility Centers and Reporting Segments**

When comparing performance report information for top management with that for lower-level management,

A. Top management reports show control over fewer costs.
B. Lower-level management reports are likely to contain more quantitative data and less financial data.
C. Top management reports are more detailed.
D. Lower-level management reports are typically for longer time periods.

A. Top management reports show control over more costs.

B. Lower-level management reports are likely to contain more quantitative data and less financial data. This is because lower-level management is responsible for day-to-day operations and their reports contain information about units of production, number of hours worked, etc. Top management, on the other hand, is concerned about company’s strategic goals, objectives and overall financial results.

C. Top management reports are less detailed than those for lower management.
D. Lower-level management reports are typically for shorter time periods.

---

**Question 45 - CMA 692 3-14 - Responsibility Centers and Reporting Segments**

The most fundamental responsibility center affected by the use of market-based transfer prices is a(n)

A. Investment center.
B. Cost center.
C. Profit center.
D. Production center.

A. While an investment center would be affected by the transfer prices being used, an investment center is not the most fundamental (basic) of the centers that is affected by transfer prices.

B. A cost center is not responsible for revenues, so it would not be affected by transfer prices.

C. A profit center is responsible for both revenues and costs (and therefore profit). A transfer price, whether received as revenue or paid as a cost, does affect a profit center; and a profit center is the most fundamental (basic) responsibility center that would be affected.

An investment center, which is responsible for revenues, costs, and investment, would also be affected by transfer prices; but an investment center is not the most basic, or fundamental, responsibility center to be affected by transfer prices.

D. Production centers are not always responsible for revenues and costs so the transfer prices that are used would not always affect a production center.

---

**Question 46 - CIA 1191 IV-19 - Responsibility Centers and Reporting Segments**

A carpet manufacturer maintains a retail division consisting of stores stocking its brand and other brands, and a manufacturing division that makes carpets and pads. An outside market exists for carpet padding material in which all padding produced can be sold. The proper transfer price for padding transferred from the manufacturing division to the retail division is

A. The market price at which the retail division could purchase padding.
B. Variable manufacturing division production cost plus allocated fixed factory overhead.
C. Variable manufacturing division production cost plus variable selling and administrative cost.
D. Variable manufacturing division production cost.

A. The basic issue of transfer prices is how much should one unit of a company charge another unit of the same company for its goods or services. The goal in setting a transfer price is that the method used will stimulate the department managers to do what will provide the greatest benefit to the company as a whole, rather than to act in their own interest. Since an outside market exists for padding produced in which all padding produced can be sold, the best transfer price is the market price.

B. When there is an external market for the product, market price is almost always the best transfer price to use.

C. When there is an external market for the product, market price is almost always the best transfer price to use.

D. When there is an external market for the product, market price is almost always the best transfer price to use.
**Question 47** - CMA 1291 3-9 - Responsibility Centers and Reporting Segments

A segment of an organization is referred to as an investment center if it has

A. Authority to make decisions affecting the major determinants of profit including the power to choose its markets and sources of supply.
B. Authority to make decisions over the most significant costs of operations including the power to choose the sources of supply.
C. Authority to provide specialized support to other units within the organization.
D. Authority to make decisions affecting the major determinants of profit including the power to choose its markets and sources of supply and significant control over the amount of invested capital.

A. This is the definition of a profit center. An investment center also has a responsibility for invested capital.
B. This is the definition of a cost center.
C. This is the definition of a service center, which is a type of cost center.
D. By definition, an investment center is a part of the business that has the authority to make decisions affecting the major determinants of profit including the power to choose its markets and sources of supply and significant control over the amount of invested capital.

---

**Question 48** - CIA 589 IV-15 - Responsibility Centers and Reporting Segments

In a responsibility accounting system, managers are accountable for

A. Costs over which they have significant influence.
B. Product costs but not for period costs.
C. Incremental costs.
D. Variable costs but not for fixed costs.

A. In a responsibility accounting system, managers are responsible for the costs that they control. Costs over which a manager has significant influence are costs that they control.
B. In a responsibility accounting system, managers are responsible for the costs that they control, whether they are product or period costs.
C. In a responsibility accounting system, managers are responsible for the costs that they control, whether they are incremental costs or not.
D. In a responsibility accounting system, managers are responsible for the costs that they control, whether they are fixed or variable.

---

**Question 49** - CIA 594 III-71 - Responsibility Centers and Reporting Segments

Which of the following is not true of responsibility accounting?

A. The focus of cost center managers will normally be more narrow than that of profit center managers.
B. Every factor that affects a firm’s financial performance ultimately is controllable by someone, even if that someone is the person at the top of the firm.
C. When a responsibility accounting system exists, operations of the business are organized into separate areas controlled by individual managers.
D. Managers should only be held accountable for factors over which they have significant influence.

A. A cost center has only costs under its control while a profit center has both costs and revenues under its control. Therefore, it is true that the focus of a cost center manager will be more narrow that the focus of a profit center.
manager.

B. Unfortunately, not everything that impacts a firm's performance is controllable by someone in the firm. A good example of this type of exogenous variable is the economy. As the economy itself improves or weakens, the company will also be affected. But no person in the company is in a position to influence the economy. Therefore, this statement is not true.

C. In order for a responsibility system to work, the company needs to be organized into areas or divisions or some other breakdown based upon what a position is able to influence and control. Therefore, this statement is true.

D. In responsibility accounting, managers should be held accountable only for the things that they are able to control. Therefore, this statement is true.

Question 50 - CIA 1191 IV-17 - Responsibility Centers and Reporting Segments

The receipt of raw materials used in the manufacture of products and the shipping of finished goods to customers is under the control of the warehouse supervisor. The warehouse supervisor's time is spent approximately 60% on receiving activities and 40% on shipping activities. Separate staffs are employed for the receiving and shipping operations. The labor-related costs for the warehousing function are as follows:

- Warehouse supervisor's salary: $40,000
- Receiving clerks' wages: $75,000
- Shipping clerks' wages: $55,000
- Employee benefit costs (30% of wage and salary costs): $51,000

Total: $221,000

The company employs a responsibility accounting system for performance reporting purposes. The costs are classified on the report as period or product costs. The total labor-related costs that would be listed on the responsibility accounting performance report as product costs under the control of the warehouse supervisor for the warehousing function would be

A. $128,700
B. $130,000
C. $169,000
D. $97,500

A. This answer results from including the receiving clerks' wages and related benefits, plus 60% of the supervisor's salary and related benefits. This incorrectly assumes that the supervisor's salary is controllable by the supervisor. The answer to this question should be the total product costs that the warehouse supervisor can control; and the warehouse supervisor is not able to control his/her own salary.

B. This answer is a total of the receiving clerks' wages and the shipping clerks' wages. The answer to this question should be the total product costs that the warehouse supervisor can control.

C. This answer is a total of the receiving clerks' wages and the shipping clerks' wages, plus their related benefits. The answer to this question should be the total product costs that the warehouse supervisor can control.

D. In a responsibility accounting system, the only costs that a manager should be evaluated on are those costs that the manager can control.

The warehouse supervisor can control the receiving clerks' wages and the shipping clerks' wages. However, this problem asks for the total labor-related costs that would be listed on the responsibility accounting performance report as product costs. Receiving costs are product costs. Shipping expenses are selling expenses, and so they are classified as period costs, not product costs. So the only product costs that the warehouse supervisor can control are the costs for the receiving clerks. Those will include $75,000.
for the receiving clerks' wages plus 30% of the receiving clerks' wages for benefits which is $22,500 ($75,000 × .30), for a total of $97,500.

The supervisor's salary cannot be controlled by the supervisor and therefore it is not included.

---

**Question 51** - CIA 1191 IV-18 - Responsibility Centers and Reporting Segments

A company plans to implement a bonus plan based on segment performance. In addition, the company plans to convert to a responsibility accounting system for segment reporting. The following costs, which have been included in the segment performance reports that have been prepared under the current system, are being reviewed to determine if they should be included in the responsibility accounting segment reports:

I. Corporate administrative costs allocated on the basis of net segment sales.

II. Personnel costs assigned on the basis of the number of employees in each segment.

III. Fixed computer facility costs divided equally among each segment.

IV. Variable computer operational costs charged to each segment based on actual hours used times a predetermined standard rate; any variable cost efficiency or inefficiency remains in the computer department.

Of these four cost items, the only item that could logically be included in the segment performance reports prepared on a responsibility accounting basis would be the

A. Corporate administrative costs.

B. Fixed computer facility costs.

C. Variable computer operational costs.

D. Personnel costs.

A. An allocation basis should be one in which the managers are able to control the incurrence of costs by their department. In an allocation basis of sales, an individual segment manager is able to control only their own sales, not the sales of other segments. Therefore, this allocation of costs would not be appropriate for responsibility accounting.

B. The equal allocation of fixed computer costs is not appropriate for responsibility accounting because the individual managers are not able to control how much the computer department spends. This also does not relate to the usage of the computer department by each segment.

C. An allocation basis should be one in which the managers are able to control the incurrence of costs by their department. An allocation based on the actual usage of the item being allocated is an appropriate method of allocation for responsibility accounting. Therefore, these variable computer costs can be included in the responsibility accounting report. The other answer choices all represent costs that segment managers are not able to control.

D. An allocation basis should be one in which the managers are able to control the incurrence of costs by their department. In an allocation basis of personnel, an individual segment manager is able to control only their own staff numbers, not the staff numbers of other segments. Therefore, this allocation of costs would not be appropriate for responsibility accounting.