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**QUESTION 1**

MS Trucking is considering the purchase of a new piece of equipment that has a net initial investment with a present value of \$300,000. The equipment has an estimated useful life of 3 years. For tax purposes¹ the equipment will be fully depreciated at rates of 30%, 40%, and 30% in years one, two, and three, respectively. The new machine is expected to have a \$20,000 salvage value. The machine is expected to save the company \$170,000 per year in operating expenses. MS Trucking has a 40% marginal income tax rate and a 16% cost of capital. Discount rates for a 16% rate are:

	<u>Present Value of an Ordinary Annuity of \$1</u>	<u>Present Value of \$1</u>
Year 1	.862	.862
Year 2	1.605	.743
Year 3	2.246	.641

What is the net present value of this project?

- A. \$3,278
- B. \$5,842
- C. \$(568)
- D. \$30,910

Correct Answer: B

QUESTION 2

The payback reciprocal can be used to approximate a project's

- A. Profitability index.
- B. Net present value.
- C. Accounting rate of return if the cash flow pattern is relatively stable.
- D. Internal rate of return if the cash flow pattern is relatively stable.

Correct Answer: D

QUESTION 3



Determining what issues must be addressed and considering the objectives of the desired course of action are accomplished during which step of the decision-making process?

- A. Defining the problem.
- B. Obtaining information.
- C. Evaluating solutions.
- D. Implementing the decision.

Correct Answer: B

During the step in the decision-making process of obtaining information, the decision maker determines which issues must be addressed, for example, whether to make or outsource a component. The decision maker also considers the objectives of the desired course of action, for example, to increase return on investment or to enter a new market.

QUESTION 4

According to Philip Kilter, which class of customer produces low profit but is desirable?

- A. Iron.
- B. Gold.
- C. Lead.
- D. Platinum.

Correct Answer: A

Customer profitability analysis determines all revenues and all costs assignable to specific customers. Customers in the iron category produce low profits but are desirable. The firm's marketing investment in these customers is lower than for the platinum and gold categories. However, the firm's objective should be to move them into the gold category.

QUESTION 5

A company enters into an agreement with a firm that will factor the company's accounts receivable. The factor agrees to buy the company's receivables, which average \$100,000 per month and have an average collection period of 30 days. The factor will advance up to 80% of the face value of receivables at an annual rate of 10% and charge a fee of 2% on all receivables purchased. The controller of the company estimates that the company would save \$18,000 in collection expenses over the year. Fees and interest are not deducted in advance. Assuming a 360-day year, what is the annual cost of financing?

- A. 10.0%
- B. 12.0%
- C. 14.0%
- D. 17.5%



Correct Answer: D

In an average month, the company will receive \$80,000 at the time the receivables are sent to the factor. Over a year's time, the interest on this average advance of \$80,000 would be \$8,000 at 10% interest. In addition, the factor will charge a 2% factor fee, or \$24,000 ($\$100,000 \times .02 \times 12$) over the course of a year. However, this \$24,000 fee is offset by the \$18,000 savings in collection expenses, producing a net outlay of only \$6,000. Adding the \$6,000 to the \$8,000 of interest produces an annual net cost of \$14,000. Dividing the \$14,000 cost by the \$80,000 of advanced funds results in a cost of 17.5%.

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