12 Questions From Appendix 6

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- The following 12 Questions are from the Appendix for Chapter 6
- They capture issues in cost based pricing

#1

- Which of the following is not considered one of the three basic approaches to setting the selling price?
- a) the cost-based approach
- b) the engineering-based approach
- c) the competitor-based approach
- d) the customer-based approach

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- **b) the engineering-based approach**
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#2

- The basic profit equation is presented as
- Z = P(Q) – V(Q) – F
- where P = the selling price, Q = the quantity sold, V = the variable cost per unit, and F = the fixed costs for the period
- The basic profit equation is transformed into the equation for calculating the breakeven quantity, BEQ, by setting the profit equal to zero, Z =0, and rewriting the profit equation as
- Breakeven Q = F/(P-V)
- True or False?

#2

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- where P = the selling price, Q = the quantity sold, V = the variable cost per unit, and F = the fixed costs for the period
- The basic profit equation is transformed into the equation for calculating the breakeven quantity, BEQ, by setting the profit equal to zero, Z =0, and rewriting the profit equation as
- Breakeven Q = F/(P-V)
- **This is True**

#3

- The average cost per unit or the breakeven price, BEP, for the last period could be calculated by taking the total cost, C, (i.e., the difference between total revenue, R, and net profit, Z, and dividing the total cost by the quantity sold, Q. That is to say, the average cost per unit could be calculated as
- Average cost per unit or BEP = (R-Z)/Q
- True or False?

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- **This is True**

#4

- The manufacturing and sale of 1,100 pairs of wooden shoes resulted in a Breakeven Price or average cost of $16 per pair. The average cost was the sum of the following costs:
- Average cost of direct materials = $7 per pair
- Average advertising cost = $4 per pair
- Average sales commission = $2 per pair
- Average warehouse storage cost = $3 per pair
- What is the variable cost per unit?

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- Average cost of direct materials = $7 per pair
- Average advertising cost = $4 per pair
- Average sales commission = $2 per pair
- Average warehouse storage cost = $3 per pair
- What is the variable cost per unit? **$9 per shoe**

#5

- Advertising is defined as a variable cost because the amount that the marketing manager chooses to spend on advertising each month varies from month to month. True or False?

#5

- Advertising is defined as a variable cost because the amount that the marketing manager chooses to spend on advertising each month varies from month to month.
- **This is false**

#6

- The average cost per unit or breakeven price is traditionally calculated by including the variable costs of making the product and the average fixed costs per unit involved in advertising and sales force.
  True or False?

#6

- The average cost per unit or breakeven price is traditionally calculated by including the variable costs of making the product and the average fixed costs per unit involved in advertising and sales force.
  This is True

#7

- The marketing manager for manufacturing firm believes that he will achieve a normal sales volume with a normal average cost or breakeven price of $50 per unit in the next period, (BEP = $50). However, he must set a selling price that will earn the owners of the firm a normal profit margin. The owners expect a profit margin of 20% return on sales (ROS = 20%). The marketing manager sets a price of $62.50 to cover the breakeven price of $50 per unit and provide a profit margin of 20%.
- True or False?

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- **This is True**

#8

- The definition of markup on price, Mp, is the ratio of the dollar markup per unit, P-V, divided by the selling price, P, and it is written as
- Mp =(P-V)/P
- True or False?

#8

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- Mp =(P-V)/P
- **This is True**

#9

- The simplest markup pricing formula for setting a selling price could be limited to knowing the invoice cost of the product and the normal percentage of mark on price, such as
- Selling Price = (cost of the inventory item)/(1-markup on price)
- True or False?

#9

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- Selling Price = (cost of the inventory item)/(1-markup on price)
- **This is True**

#10

- If all the firms in an industry have similar cost structures, use similar markup formula for setting their prices, and avoid competing on price, then they have a basis for implicit price fixing.
- True or False?

#10

- If all the firms in an industry have similar cost structures, use similar markup formula for setting their prices, and avoid competing on price, then they have a basis for implicit price fixing.
- **This is true**

#11

- A store manager uses a markup-pricing formula based on the invoice cost of the product and a predetermined markup on price as the profit to set the product's price to customer. This guarantees that the product is generating the amount of gross profit the store needs to justify carrying that product. True or False?

#11

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#12

- All the hospitals in town use similar procedures, have similar cost structures, and use similar cost-based pricing equations to set their prices. The hospitals do not compete on price and pride themselves in competing on the quality of patient care. All the hospitals are using similar markup pricing equations. Any cost increase that is common to all hospitals will be passed on to their customers (e.g., insurance companies) and the normal rate of return will increase the profits earned by the owners of the hospital.
- True or False?

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- **This is True**

- To learn more about the basics of cost-based pricing see che appendix for chapter 6