

CHAPTER 1  
ACCOUNTING: INFORMATION FOR DECISION MAKING

TRUE/FALSE

1. The Decision Framework applies to all business-related decisions, but **not** to personal decisions.  
LO1 – False      The four-step process applies equally to all decisions, whether personal or business-related.
2. Business decisions generally have few options.  
LO1 – False      Business decisions frequently have numerous options.
3. Every option in making a decision presents a unique trade-off between benefits and costs.  
LO1 – True
4. Effective decision makers ensure that the value of the chosen decision option exceeds its opportunity cost.  
LO1 – True
5. The value of an option must always be expressed in monetary terms.  
LO1 – False      Even though most businesses measure value in terms of money, or profit, value need not be a monetary amount.
6. Unlike individuals whose goals might have several factors, organizations tend to have focused goals.  
LO2 – True
7. The key difference between individual and business decisions relate to Step 2 of the four-step framework, that is, identifying options.  
LO2 – False      The key difference between individual and business decisions relates to step 1 of the four-step framework – that is, organizations need to ensure that the goals of individual employees mesh with the focused goals of the organization.
8. To accomplish their goals, organizations not only need to allocate resources effectively, but also need to motivate employees to focus on organizational goals.  
LO2 – True
9. A for-profit business usually specifies organizational goals according to profit motive.  
LO2 – False      A for-profit business usually specifies organizational goals according to ownership.
10. Decisions that best attain individual goals may **not** necessarily agree with the organization's goal of maximizing profit.  
LO2 – True
11. Control decisions relate to motivating, monitoring, and evaluating performance.  
LO3 – True

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12. Examining past performance is not involved in control decisions.  
LO3 – False      Many control decisions involve examining past performance, with the purpose of improving subsequent plans.
13. The planning and control cycle is a long-term cycle normally taking months to complete.  
LO3 – False      The planning and control cycle could happen within moments or take months.
14. Planning decisions relate to choices about acquiring and using resources to deliver products and services to customers.  
LO3 – True
15. The planning and control cycle includes planning, implementing, evaluating, and revising.  
LO3 – True
16. Understanding finance is **not** crucial to organizations when identifying the costs and benefits of funding operations in different ways.  
LO4 – False      Understanding finance is crucial when identifying the costs and benefits of funding operations in different ways.
17. Managerial accounting aims to satisfy the information needs of decision makers outside the firm.  
LO4 – False      Managerial accounting aims to satisfy the information needs of decision makers inside the firm.
18. Firms satisfy the information needs of external makers by issuing a comprehensive set of financial statements at regular intervals that relate to the firm as a whole.  
LO4 – True
19. The primary role of accounting is to help measure the costs and benefits of decision options.  
LO4 – True
20. In the United States, firms follow Generally Accepted Accounting Principles (GAAP) as defined by the Financial Accounting Standards Board when preparing their financial statements.  
LO4 – True
21. Ethics relate primarily to the decision-making step of the Decision Framework.  
LO5 – False      Ethics relates to every aspect of the Decision Framework.
22. *The Foreign Corrupt Practices Act of 1977* prohibits managers from giving or taking bribes unless such acts are part of the normal business practices in another country.  
LO5 – False      The Foreign Corrupt Practices Act of 1977 prohibits managers from giving or taking bribes even if such acts are part of the normal business practices in another country.
23. Many firms conduct surprise audits to increase the odds of detecting **unethical** behavior.  
LO5 – True

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24. *The Sarbanes-Oxley Act of 2002* mandates that the executives and financial officers certify, in writing, the truthfulness of reports filed with the IRS.

LO5 – False      The Sarbanes-Oxley Act of 2002 mandates that the executives and financial officers certify, in writing, the truthfulness of reports filed with the SEC.

25. Some firms impose ethical standards on their suppliers.

LO5 – True

26. An organization's board of directors usually delegates most decisions to the Chief Operating Officer.

Appendix A – False      An organization's board of directors usually delegates most decisions to the Chief Executive Officer, the highest-ranking executive in the organization.

27. The chief financial officer (CFO) manages the internal audit function of a company.

Appendix A – False      The chief internal auditor manages the internal audit function.

28. The controller manages the day-to-day accounting for the firm and oversees corporate accounting policies.

Appendix A – True

29. Division managers are responsible for ensuring that the firm has appropriate monitoring, performance evaluation and incentive systems in place to motivate employees to achieve organizational goals.

Appendix A – False      Division managers direct the day-to-day operations of product lines and markets.

30. While divisional controllers report to division managers, they also have a "dotted line" relationship with the corporate controller.

Appendix A – True

**MULTIPLE CHOICE**

31. Which of the following is **not** one of the four steps in the decision making process?

- A. Specify the decision problem, including the decision maker's goals.
- B. Identify options.
- C. Separate routine decision problems from non-routine decision problems.
- D. Measure benefits and costs to determine the value of each option.
- E. Make the decision, choosing the option with the highest value.

LO1 – C

32. The value of an option equals its:

- A. Benefits plus its costs.
- B. Benefits less its costs.
- C. Costs.
- D. Profit.
- E. None of the above.

LO1 – B

33. The opportunity cost of any decision option is:

- A. The value to the decision maker of the least-best option.
- B. The total profit of the best option.
- C. The total costs of the least option.
- D. The value to the decision maker of the next best option.
- E. None of the above.

LO1 – D

34. The concepts of value and opportunity cost emphasize that every decision involves:

- A. Eliminating any risks of making the decision.
- B. Estimating the time value of money.
- C. Trading off what the decision maker gets with what the decision maker gives up.
- D. Comparing the current period's opportunity costs with the previous period's opportunity costs.
- E. None of the above.

LO1 – C

35. Which of the following statements is **false**?

- A. Decisions help us accomplish goals.
- B. When determining their goals, individuals generally agree on the factors they consider and the importance they attach to the various factors.
- C. Some decisions involve a small number of options.
- D. For most businesses, identifying the set of options is one of the more important tasks of management.
- E. Value is the contribution of an option to the decision maker's goals.

LO1 – B

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36. Managerial accounting is a branch of accounting which:
- A. Provides financial information to creditors and stockholders.
  - B. Summarizes financial information.
  - C. Assists in predicting future profits.
  - D. Assists in making business decisions.

LO1 – Self-Test – D

37. John has three options for summer work. He can do lawn work for \$100 per week, babysit for \$125 per week, or work at the local pool for \$175 per week. All of the options would require approximately 20 hours of work per week. In addition, if he chooses to work at the pool, he will incur \$20 in gas costs per week. The opportunity cost if he chooses to babysit is:
- A. \$100
  - B. \$175
  - C. \$155
  - D. \$105

LO1 – Self-Test – C

38. Greg, a college student, knows that the opportunity cost of taking a class this summer is \$1,200. This means that:
- A. Instead of taking the class, Greg could earn \$1,200 by working instead.
  - B. Greg will need to pay \$1,200 to take the class.
  - C. The difference between what he would earn working less the cost of the class is \$1,200.
  - D. By taking the class, Greg will have the opportunity to earn \$1,200 more in a job than he would without taking the class.

LO1 – Self-Test – A

39. Which of the following is the best example of an opportunity cost?
- A. The cost of filling up the company car with gasoline.
  - B. The time incurred in reviewing expense reports of key employees in the company.
  - C. Taking two days vacation at the end of the month instead of completing a project for a client.
  - D. Asking the President of the company for a raise.

LO1 – Post-Test – C

40. In applying the four-step decision-making framework, which of the following is a difference in individuals' and organizations' decision making process?
- A. Individuals' goals might have several factors whereas organizations tend to have focused goals.
  - B. Individuals' goals tend to be clear, whereas organizations' goals tend to be unclear.
  - C. Individuals' goals tend to be long-term, whereas organizations' goals tend to be short-term.
  - D. Individuals' goals' may be monetary or nonmonetary, whereas organizations' goals are always monetary.
  - E. All of the above are differences in individual and organizational decisions.

LO2 – A

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41. Which of the following is something owners might do to influence employees to achieve organizational goals?
- A. Maintain policies and procedures to define acceptable behavior.
  - B. Have incentive schemes and performance evaluations to motivate employees to consider organizational goals.
  - C. Monitor to enforce policies and procedures.
  - D. Both A and B.
  - E. A, B and C are things owners might do.

LO2 – E

42. Which of the following is a reason for forming an organization?
- A. To help individuals in need.
  - B. To increase one's wealth.
  - C. To maximize shareholder value.
  - D. To serve the public.
  - E. All of the above are reasons for forming an organization.

LO2 – E

43. Monitoring to enforce policies and procedures might include:
- A. Perform random drug and alcohol tests on employees.
  - B. Routinely walk around and make sure employees are doing their jobs.
  - C. Keep attendance records to discourage employees from claiming payment for time not worked.
  - D. Both A and B.
  - E. A, B and C are methods of monitoring.

LO2 – D

44. Firms promote goal congruence by:
- A. Requiring all employees to participate in the budgeting process.
  - B. Assuring that all decisions have a small number of options.
  - C. Reducing opportunity cost to a minimum.
  - D. Tailoring policies and procedures to fit the organization's specific needs.
  - E. None of the above promotes goal congruence.

LO2 – D

45. The owner of a driving range is trying to determine the value of hiring additional part time help. If she is able to hire someone to work in the shop for 15 hours per week for \$10 per hour, she estimates that she can teach approximately 10 additional lessons for which she charges \$40 per lesson. The value of hiring a new employee is:
- A. \$400
  - B. \$250
  - C. \$150
  - D. \$100

LO2 – Self-Test – B

## Accounting: Information for Decision Making

46. What is the first step in the decision-making process?

- A. Identify available options.
- B. Specify the problem and goals.
- C. Measure costs and benefits.
- D. Make a final decision.

LO2 – Self-Test – B

47. Janice is traveling to see a friend in New York next month and she is trying to decide whether to fly or take the train. She found a round-trip airline ticket for \$170. Janice feels that traveling on the train would be more convenient and she was able to find a ticket for \$159, however the total trip time traveling by train will take two hours more than by plane. Janice should:

- A. Take the train because it is the least expensive option.
- B. Take the train because it is the most convenient option.
- C. Take the plane if her goal is to spend as much time as possible with her friend.
- D. Take the plane because it has been proven to be the safest mode of transportation.

LO2 – Self-Test – C

48. Groceries R Us is considering two different options: install four self-service registers which would increase profits by \$1,800, or install 2 additional full-service registers which would increase profits by \$400. What is the value and opportunity cost of the option of installing the full-service registers?

	<u>Value</u>	<u>Opportunity Cost</u>
A.	\$1,800	\$1,800
B.	\$400	\$1,800
C.	\$1,800	\$400
D.	\$400	\$400

LO2 – Self-Test – B

49. The proper order for the steps in a planning and control cycle are:

- A. Plan, revise, implement, and evaluate.
- B. Implement, evaluate, revise, and plan.
- C. Implement, revise, evaluate, and plan.
- D. Plan, implement, evaluate, and revise.

LO2 – Self-Test – D

50. Which part of the four step framework for making decisions is linked directly to the formulation of the decision maker's goals?

- A. Step 1: Specify the decision problem.
- B. Step 2: Identify options.
- C. Step 3: Measure benefits and costs.
- D. Step 4: Make the decision.

LO2 – Pre-Test – A

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51. Which one of the following is the best example of an organizational goal?
- A. Ensuring that costs exceed benefits.
  - B. Maximizing shareholder value.
  - C. Paying significant dividends.
  - D. Launching a new product that is known to have potential defects.

LO2 – Post-Test – B

52. Which of the following is **not** a stage in the planning and control cycle?
- A. Implementing.
  - B. Evaluating.
  - C. Revising.
  - D. Measuring.
  - E. All of the above are stages in the planning and control cycle.

LO3 – D

53. In the planning and control cycle, the Evaluate stage deals with:
- A. Products and services.
  - B. Resources necessary.
  - C. Set performance targets.
  - D. Achievement of performance targets.
  - E. All of the above are part of the Evaluate stage.

LO3 – D

54. In the planning and control cycle, the Revise stage deals with:
- A. Best mix of products and services.
  - B. Reasons for deviations.
  - C. Motivate employees.
  - D. Customer and prices.
  - E. None of the above is a part of the Revise stage.

LO3 – A

55. In the planning and control cycle, the Plan stage deals with:
- A. Use of resources to make products and deliver services.
  - B. Actual results.
  - C. Performance targets.
  - D. Products and services.
  - E. Reasons for deviations.

LO3 – D

56. In the planning and control cycle, the Implement stage deals with:
- A. Products and services.
  - B. Best mix of products and services.
  - C. Motivate employees.
  - D. Actual results.
  - E. Reasons for deviations.

LO3 – C



## Accounting: Information for Decision Making

57. The organizational goal of management at Friedman Enterprises is to maximize profits. The goal of individual employees is to maximize their paychecks. One way in which management can try to align these goals would be to:
- A. Increase employee pay, after all this should make employees more efficient.
  - B. Eliminate stringent policies and procedures, thus giving employees more freedom in their work.
  - C. Increase employee incentives for exceptional work.
  - D. Decrease the amount of supervision of the employees, as this can be distracting to employees.

LO3 – Self-Test – C

58. In order to make a good decisions, management must rely on:
- A. The company's audited financial statements.
  - B. Historical documents such as bank statements.
  - C. Employee input.
  - D. The evaluation of the costs and benefits of each decision.

LO3 – Self-Test – D

59. Which of the following is **not** associated with how organizations motivate employees to achieve their goals?
- A. Policies and procedures.
  - B. Incentive schemes and performance evaluation.
  - C. Terminating employees.
  - D. Monitoring employees for enforcement of policies and procedures.

LO3 – Pre-Test – C

60. Which one of the following is considered a stage of the planning and control cycle?
- A. Analyze markets.
  - B. Revise.
  - C. Develop budgets.
  - D. Modify.

LO3 – Pre-Test – B

61. Which of the following best describes the nature of control decisions of the planning and control cycle?
- A. Deciding which products to sell.
  - B. Evaluating future advertising based on the effectiveness of a past ad campaign.
  - C. Creating a management report that is typically not reviewed.
  - D. Giving employees pay increases without regard to performance.

LO3 – Post-Test – B

62. The primary role of accounting is to:
- A. Detect and prevent fraud.
  - B. Maintain employee pay records.
  - C. Measure the costs and benefits of decision options.
  - D. Prepare reports for the government.
  - E. None of the above.

LO4 – C

## Accounting: Information for Decision Making

63. The two classes of decision makers who rely on accounting information are:
- A. Managers and employees.
  - B. Stockholders and creditors.
  - C. Governmental agencies and owners.
  - D. Decision makers inside the firm and decision makers outside the firm.
  - E. Auditors and executives.

LO4 – D

64. Which of the following is **not** a decision maker outside the firm?
- A. Employee.
  - B. Stockholder.
  - C. Potential Investor.
  - D. Bank.
  - E. Board of Directors.

LO4 – A

65. An organization's employees use managerial accounting data to determine:
- A. Who to hire and how to pay them.
  - B. Which products and services to offer.
  - C. The prices of products and services.
  - D. What equipment to purchase.
  - E. All of the above.

LO4 – E

66. Which of the following is **not** a key difference between managerial accounting and financial accounting?
- A. The emphasis of financial accounting is information reliability while the emphasis of managerial accounting is information relevance.
  - B. Financial accounting focuses on past financial data while managerial accounting uses all available data.
  - C. Financial accounting focuses on external users while managerial accounting focuses on internal users.
  - D. Financial accounting uses financial and non-financial data while managerial accounting only uses non-financial data.
  - E. Financial accounting reports are released periodically while managerial accounting reports are generated on an as-needed basis.

LO4 – D

67. The Sarbanes-Oxley Act of 2002 requires that:
- A. Executives of publicly-traded companies take responsibility for the accuracy of financial reports.
  - B. Publicly-traded companies release financial statements on a quarterly basis.
  - C. Publicly-traded companies notify stockholders if there is any turnover in executive positions.
  - D. Publicly-traded companies provide a dividend to stockholders at least every other year.

LO4 – Self-Test – A

## Accounting: Information for Decision Making

68. Which one of the following is a characteristic of managerial accounting?

- A. Involves only quantitative information.
- B. Involves decision makers internal to the company.
- C. Prepared based on fixed periods of reporting.
- D. Required by GAAP.

LO4 – Pre-Test – B

69. Which one of the following is a primary user of managerial accounting?

- A. An ex employee.
- B. A county taxing authority.
- C. A sales manager of one of the company's divisions.
- D. A bank that loaned a company \$2,000,000.

LO4 – Post-Test – C

70. Which of the following outside forces stop an individual from **unethical** decision making?

- A. Governments.
- B. Societies.
- C. Laws.
- D. Organizations.
- E. All of the above.

LO5 – E

71. Which of the following is **not** a provision of *The Foreign Corrupt Practices Act of 1977*?

- A. It prohibits managers from giving bribes to foreign officials.
- B. It requires firms to maintain internal control systems to properly execute and record all transactions.
- C. It provides for penalties, including fines and jail time, for executives who knowingly alter, destroy, conceal or falsify records.
- D. Both A and B.
- E. A, B and C.

LO5 – C

72. Which of the following is not a provision of the Sarbanes-Oxley Act of 2002?

- A. It mandates that executives of publicly traded companies take individual responsibility for the accuracy and completeness of financial reports.
- B. It requires executive and financial officers to certify, in writing, the truthfulness of quarterly and annual reports filed with the SEC.
- C. It provides for penalties, including fines and jail time, for executives who knowingly alter, destroy, conceal or falsify records.
- D. It prohibits managers from giving or taking bribes, even if such acts are part of the normal business practices in another country.
- E. All of the above are provisions of the *Sarbanes-Oxley Act of 2002*.

LO5 – D

## Accounting: Information for Decision Making

73. Which of the following is **not** an example of how companies provide guidance regarding ethical standards?
- A. A company may mandate stiff penalties, including fines and jail time, for unethical conduct.
  - B. A company may provide each employee a handbooks which include statements of ethical standards.
  - C. A company may include statements of ethical standards in its employee rights and responsibilities documents.
  - D. A company may impose ethical standards on their suppliers.
  - E. All of the above.

LO5 – A

74. The main responsibility for ethical behavior rests on:
- A. Professional bodies.
  - B. The Government.
  - C. Employers.
  - D. The individuals involved.
  - E. The legal system.

LO5 – D

75. Which law mandates that the financial statements of the organization are accurate and complete when filed with the Securities and Exchange Commission?
- A. The Foreign Corrupt Practices Act.
  - B. The Financial Accountability Act.
  - C. Generally Accepted Accounting Principles.
  - D. The Sarbanes-Oxley Act.

LO5 – Pre-Test – D

76. Ethical standards are often considered difficult to enforce. Which one of the following is a good approach to ensuring ethics are followed?
- A. Randomly inquiring of certain employees whether they are being ethical or not.
  - B. Routinely check to ensure that applicants make truthful statement on their employment applications.
  - C. Ensuring the CEO always includes a comment on the newsletter that ethics are important and must be followed.
  - D. Ensuring that key employees sign conflict of interest statements.

LO5 – Post-Test – D

77. Which of the following is a correct hierarchical relationship among positions in an organization?
- A. Board of Directors, Chief Executive Officer, Treasurer, Functional Manager.
  - B. Board of Directors, Chief Financial Officer, Chief Executive Officer, Division Manager.
  - C. Board of Directors, Chief Financial Officer, Functional Managers, internal Auditor.
  - D. Board of Directors, Chief Executive Officer, Functional Manager, Division Manager.
  - E. Board of Directors, Chief Executive Officer, Division Manager, Functional Manager.

Appendix A – E

78. Which of the following describes the controller's position?
- A. Manages the firm's cash flow.
  - B. A key player in ensuring that the firm has appropriate monitoring, performance evaluation, and incentive systems in place to motivate employees to achieve organizational goals.
  - C. Has a "dotted line" to the Board of Directors.
  - D. Both A and B.
  - E. A, B and C.

Appendix A – B

79. Which of the following is **not** a correct statement regarding the Institute of Management Accountants (IMA)?
- A. Provides personal and professional development opportunities in information management.
  - B. Offers educational programs to further the practice of management accounting.
  - C. Provides members with resources, information and leadership that enable them to provide valuable services in the highest professional manner to benefit the public as well as employers and clients.
  - D. Offers the Certified Financial Manager certification.
  - E. All of the above are correct statements regarding the IMA.

Appendix A – C

80. Which of the following organizations advocates on behalf of its members before the government and standard setters?
- A. AICPA.
  - B. IMA.
  - C. IIA.
  - D. CMA.
  - E. GAAP.

Appendix A – A

81. Which of the following is **not** a correct statement regarding the Institute of Internal Auditors (IIA)?
- A. Offers a certification that designates an accounting professional as Certified Financial Manager.
  - B. Advocates the value of internal auditing.
  - C. Provides education on best practices in internal auditing.
  - D. Provides leadership for the global professional of internal auditing.
  - E. All of the above are correct statements regarding the IIA.

Appendix A – A

82. A company's Chief Executive Officer (CEO) reports to:
- A. The company's Board of Directors.
  - B. The company's Chief Operating Officer.
  - C. The company's internal auditors.
  - D. Nobody – the CEO is the head of the company.

Appendix A – Self-Test – A

## Accounting: Information for Decision Making

83. The position of Treasurer typically includes the following responsibilities **except**:
- A. Managing daily cash flow needs.
  - B. Ensuring that capital is used wisely.
  - C. Serving as the company's liaison with creditors, particularly banks.
  - D. Ensuring that the financial statements are presented fairly and are in compliance with Generally Accepted Accounting Principals (GAAP).

Appendix A – Self-Test – D

84. According to the IMA Code of Ethics, two good questions to ask when faced with an ethical dilemma are:
- A. "Will my actions be fair and just to all parties affected?" and "Would I be pleased to have my closest friends learn of my actions?"
  - B. "Will the personal benefits outweigh the costs of my decision?" and "Would I be pleased to have my closest friends learn of my actions?"
  - C. "Will my actions be fair and just to all parties affected?" and "Will the personal benefits outweigh the costs of my decision?"
  - D. "Have I considered all the consequences of my decision?" and "Will my actions be fair and just to all parties affected?"
  - E. "Will the personal benefits outweigh the costs of my decision?" and "Have I considered all the consequences of my decision?"

Appendix B – A

85. According to the IMA Code of Ethics, to determine whether a decision is good or bad:
- A. The decision-maker must compare his/her options with some standard of perfection.
  - B. The decision-maker must assess the situation and the values of the parties affected by the decision.
  - C. The decision maker must estimate the outcome of the decision and be responsible for its results.
  - D. Both B and C.
  - E. A, B and C.

Appendix B – E

86. The standards of ethical conduct for members of the IMA include standards relating to:
- A. Competence.
  - B. Confidentiality.
  - C. Integrity.
  - D. Objectivity.
  - E. All of the above.

Appendix B – E

## Accounting: Information for Decision Making

87. Which of the following is **not** a competence requirement as stated by the IMA Standards of Ethical Conduct for Members?
- A. Maintain an appropriate level of professional competence by ongoing development of their knowledge and skills.
  - B. Refrain from engaging in or supporting any activity that would discredit their profession.
  - C. Perform their professional duties in accordance with relevant laws, regulations, and technical standards.
  - D. Prepare complete and clear reports and recommendations after appropriate analysis of relevant and reliable information.
  - E. All of the above are competence requirements.

Appendix B – B

88. Which of the following is **not** an integrity requirement as stated by the IMA Standards of Ethical Conduct for Members?
- A. Avoid actual or apparent conflicts of interest and advise all appropriate parties of any potential conflict.
  - B. Refrain from engaging in any activity that would prejudice their ability to carry out their duties ethically.
  - C. Refrain from using or appearing to use confidential information acquired in the course of their work for unethical or illegal advantage either personally or through third parties.
  - D. Refuse any gift, favor, or hospitality that would influence or would appear to influence their actions.
  - E. All of the above are integrity requirements.

Appendix B – C

89. The Institute of Management Accountant's (IMA) Code of Ethics includes standards covering all of the following **except**:
- A. Objectivity.
  - B. Confidentiality.
  - C. Employee hiring.
  - D. Competence.

Appendix B – Self-Test – C

90. Christina Lee is a managerial accountant for The GreatStone Manufacturing Company. She discovered that some of the members of the sales department were inflating their expense reports in order to receive more money from the company. According to the Institute of Management Accountants' Code of Ethics Christina should:
- A. Notify the company's chief executive officer.
  - B. Notify the controller, assuming that he/she is not involved in the fraud.
  - C. Notify the employees involved.
  - D. Do nothing since she is not a member of the sales department.

Appendix B – Self-Test - B

**Problems**

1. Your roommate, Jerry, has used his credit card to excess and has realized that the interest he is paying is outrageous. He decides to get a part-time job for the remainder of the semester. He has three job opportunities. First, he has been offered a tutoring position with the athletic department for the remainder of the semester where he will earn \$960. Second, he has been offered a job as a waiter at a popular restaurant where he estimates his earnings will be \$1,200. Third, he has been offered a sales position at a local department store where he expects his salary to produce earnings of \$700. Jerry chooses to accept the tutoring position.

*Required:*

- a. Considering only money, what is Jerry's opportunity cost of choosing the tutoring position?
  
  - b. What other factors should Jerry consider in making his decision?
- 
2. Corey has accepted a position as executive director with a local non-profit organization, Haven Home, established to provide a transitional shelter for previously homeless men, women and children. Occupants are required to get a job within one week, pay 15 percent of their salary as rent and save 50 percent of their remaining salary. Part of Corey's job as executive director is to establish policies for the occupants and enforce the rent and savings payments. Although the salary is substantially less than a job he was offered as administrator of a local health club, Corey has told you that the goals of the Haven Home and his individual goals mesh.

*Required:*

- a. Given the above information, list three goals you believe to be those of the Haven Home.
  
- b. Given the above information, list three goals you believe to be those of Corey.
  
- c. Corey's degree is in business. List three policies using business principles that he might implement for the occupants that would help them transition into an independent lifestyle.



## Accounting: Information for Decision Making

3. Canterbury and Hester, CPAs, provide tax service to small businesses and individuals. Their business is growing and tax season is approaching. They have asked you to help them classify several actions or decisions within the context of the planning and control cycle: Plan, Implement, Evaluate, and Revise.

*Required:*

Classify by placing and "X" in the appropriate column each decision according to its stage in the planning and control cycle.

	Plan	Implement	Evaluate	Revise	Decision
a.	_____	_____	_____	_____	Whether to hire two or three new staff accountants based on expected client volume.
b.	_____	_____	_____	_____	Preparing a staffing schedule so tax returns are processed and e-filed in a timely manner.
c.	_____	_____	_____	_____	Tracking the number of tax returns prepared each week.
d.	_____	_____	_____	_____	Re-evaluate the adequacy of current staffing levels.
e.	_____	_____	_____	_____	Purchase the tax practice of a retiring CPA.

4. Financial and managerial accounting information differ on many dimensions.

*Required:*

Indicate by placing an "X" in the appropriate column whether each of the following items describes financial accounting or managerial accounting.

	Financial	Managerial	Description
a.	_____	_____	Primary users are internal to the organization.
b.	_____	_____	In most situations, data are collected, reported, and analyzed as needed, and do not conform to specified standards.
c.	_____	_____	Emphasis is on information reliability, sometimes at the expense of relevance.
d.	_____	_____	Fixed periodicity, with external reports usually released at the end of each quarter.
e.	_____	_____	Focus is on past financial data.

## Accounting: Information for Decision Making

5. Ethics relates to each of the steps in the Decision Framework. Organizations and societies play a significant role in motivating decision makers to act ethically. Laws, regulations, and governments help define behaviors that are considered unethical.

*Required:*

Enter the identifying letters in the blanks below to indicate the term that best matches each description.

A. The Foreign Corrupt Practices Act of 1977

B. Sarbanes-Oxley Act of 2002

- a. \_\_\_\_\_ Mandates that senior executives of publicly traded companies take individual responsibility for the accuracy and completeness of financial reports.
- b. \_\_\_\_\_ Applies to managers in the United States.
- c. \_\_\_\_\_ Prohibits managers from giving or taking bribes, even if part of normal business practice.
- d. \_\_\_\_\_ Provides penalties, including fines and jail time, for executives who knowingly alter, destroy, mutilate, conceal or falsify records.
- e. \_\_\_\_\_ Requires that firms maintain internal control systems to properly execute and record all transactions.

## Accounting: Information for Decision Making

6. An organization has several key financial players with various duties.

*Required:*

Enter the identifying letters in the blanks below to indicate the player that best matches each description.

- B. Chief Executive Officer
- C. Chief Financial Officer
- C. Chief Internal Auditor
- D. Controller
- E. Treasurer

- a. \_\_\_\_\_ Ensures that the organization raises the required capital at the lowest cost and uses the capital wisely to maximize shareholder returns.
- b. \_\_\_\_\_ Reports directly to the audit committee of the board of directors, which helps to maintain the position's objectivity in presenting a full and fair picture of the organization's operations.
- c. \_\_\_\_\_ The highest-ranking executive in the organization.
- d. \_\_\_\_\_ Responsible for all accounting and finance functions.
- e. \_\_\_\_\_ Manages the day-to-day accounting for the firm and oversees corporate accounting policies.

## Accounting: Information for Decision Making

7. Members of the IMA have an obligation to the public, their profession, the organizations they serve and themselves to maintain the highest standards of ethical conduct. The standards of ethical conduct for IMA members contain several responsibilities.

*Required:*

Enter the identifying letters in the blanks below to indicate the standard that best matches each description.

- A. Competence
- B. Confidentiality
- C. Integrity
- D. Objectivity
- E. Resolution of Ethical Conflict

1. \_\_\_\_\_ Disclose fully all relevant information that could reasonably be expected to influence an intended user's understanding of the reports, comments, and recommendations presented.
2. \_\_\_\_\_ Prepare complete and clear reports and recommendations after appropriate analyses of relevant and reliable information.
3. \_\_\_\_\_ Avoid actual or apparent conflicts of interest and advise all appropriate parties of any potential conflict.
4. \_\_\_\_\_ Refrain from disclosing confidential information acquired in the course of their work except when authorized, unless legally obligated to do so.
5. \_\_\_\_\_ Clarify relevant ethical issues by confidential discussion with an objective advisor to obtain a better understanding of possible courses of action.

**Problem Solutions**

1. Opportunity Costs (LO1)
  - a. The opportunity cost is \$1,200 – the value of the next best option.
  - b. Answers will vary. Examples of factors to consider include:
    - Distance to the jobs (the tutoring may not involve any travel costs if Jerry lives on campus).
    - Time commitments (the restaurant may require late evening or weekend schedules).
    - Quality of work (tutoring may be more personally fulfilling than the other jobs).
    - Costs of accepting job (the department store may require the purchase of appropriate clothing).
    - Benefits (department store may offer discounts on store merchandise; restaurant may provide free meals).
  
2. Individual Goals versus Organizational Goals (LO2)
  - a. Answers will vary. Examples of goals of Haven Home include:
    - To help homeless families and individuals become independent.
    - To provide life skills to homeless families and individuals.
    - To provide a place to reside for homeless families and individuals.
    - To provide a nurturing environment to homeless individuals and families.
    - To raise funds for operations.
    - To maintain a staff of volunteers and paid employees to meet the needs of occupants.
  - b. Answers will vary. Examples of goals of Corey include:
    - To provide a service to the community and individuals.
    - To nurture and support occupants.
    - To train occupants in life skills.
    - To follow the mission of the Haven Home.
    - To provide a positive environment for occupants.
    - To serve as a role model for occupants.
  - c. Answers will vary. Examples of policies Corey might implement include:
    - Require adult occupants to attend financial literacy training.
    - Require adult and teenager occupants to maintain a budget.
    - Provide children the opportunity to earn money from doing chores at the Haven House.
    - Require adult occupants to attend sessions on communication skills.
    - Develop a positive reward system for certain actions.
  
3. The Planning and Control Cycle (LO3)
  - a. Planning.
  - b. Implementing.
  - c. Evaluate.
  - d. Evaluate.
  - e. Revise.

## Accounting: Information for Decision Making

4. Characteristics of Financial and Managerial Accounting (LO4)
  - a. Managerial.
  - b. Managerial.
  - c. Financial.
  - d. Financial.
  - e. Financial.

5. Ethics and Decision Making (LO5)
  - a. B
  - b. A
  - c. A
  - d. B
  - e. A

6. Key Financial Players (Appendix A)
  - a. E
  - b. C
  - c. A
  - d. B
  - e. D

7. The IMA Code of Ethics (Appendix B)
  1. D
  2. A
  3. C
  4. B
  5. E

**END OF CHAPTER HOMEWORK CONTENT**

**Short Answer**

1. What are the four steps in decision making?
2. Why do individuals' goals differ?
3. What is the value of a decision option?
4. What is the opportunity cost of a decision option?
5. What is an organization? What is the key difference between decision making in organizations and decision making by individuals?
6. What three methods do organizations use to motivate employees to achieve firm goals?
7. What are planning decisions? What are control decisions?
8. What are the stages of the planning and control cycle?
9. What is the primary role of accounting?
10. Who are the primary users of financial accounting information? What types of decisions do these people make?
11. Who are the primary users of managerial accounting information? What types of decisions do these people make?
12. What are the key differences between financial and managerial accounting?
13. How does ethics fit into the Decision Framework?
14. What law prohibits managers in the United States from giving or taking bribes, even if it is the customary business practice in another country?
15. Who are the key financial players in organizations? What are their roles?
16. The code of ethical conduct prescribed for members of the Institute of Management Accountants divides expected behavior into four areas. What are these four areas?

### Solutions to Short Answer

1. (LO1) Step 1: Specify the decision problem, including the decision maker's goals.  
Step 2: Identify options.  
Step 3: Measure benefits (advantages) and costs (disadvantages) to determine the value (benefits reaped less costs incurred) of each option.  
Step 4: Make the decision, choosing the option with the highest value.
2. (LO1) Because people place different emphasis on factors such as money, risk, and leisure.
3. (LO1) The benefits of an option less its costs. Because value is the contribution of an option to the decision maker's goals, we measure value relative to the status quo, which is not doing anything at all.
4. (LO-1) The value of the next best option.
5. (LO-2) An organization is a group of individuals engaged in a collectively beneficial mission. The key difference between individual and organizational decision making relates to goals – organizational goals rarely coincide with the goals of all individual participants.
6. (LO-2) (1) Policies and procedures; (2) Monitoring; (3) Incentive schemes and performance evaluation.
7. (LO-3) Planning decisions relate to choices about acquiring and using resources to deliver products and services to customers. Control decisions relate to motivating, monitoring, and evaluating performance.
8. (LO-3) Plan, Implement, Evaluate, Revise (PIER Cycle).
9. (LO-4) To help measure the costs and benefits of decision options.
10. (LO-4) Persons outside the firm. These individuals make decisions about buying and selling stock, lending money, dividends, and taxes.
11. (LO-4) Persons inside the firm. These individuals make decisions about which products and services to offer, the prices of products and services, what equipment to purchase, who to hire and how to pay them.
12. (LO-4) The primary users (external vs. internal), governing principles, the unit of analysis, emphasis, periodicity, and types of data considered.
13. (LO-5) Ethics relate to every step of the decision framework. Ethics can shape our goals, the options we consider, how we measure costs and benefits, and the ultimate decision we make.
14. (LO-5) The Foreign Corrupt Practices Act of 1977.



## **Accounting: Information for Decision Making**

- 15 (APP-A) The key financial players include the CEO, CFO, controller, treasurer, and chief internal auditor. The roles of each player are described in detail in the appendix.
- 16 (APP-B) (1) Competence, (2) Confidentiality, (3) Integrity, and (4) Objectivity.

### Short Essay

1. You are about to graduate from college, and you have been fortunate to receive three job offers. How will you make your decision? Briefly discuss your goals and how you would rank your options.
2. Enlarging the number of options available can never reduce opportunity cost. Is this true?
3. Jessica Wilde works for a leading consulting company. She wishes to leave her job and pursue a full-time MBA program. What is Jessica's opportunity cost of joining an MBA program?
4. List three sources for differences in individuals' goals. Discuss one business that relies on variations in individuals tastes for risk.
5. What do you believe are the organizational goals of a nonprofit hospital, a university, and an honor society?
6. Why do organizations pay commissions to salespeople? What are the advantages and disadvantages of paying sales commissions from an organization's point of view?
7. Special Forces such as the Navy SEALs and the Army Rangers represent group settings in which there is almost perfect alignment between team and individual goals, and where individuals often put team goals ahead of their personal well being. What unique features give rise to the difference between these organizations and the "typical" profit-making organization?
8. Referring to an experience that we are sometimes forced to endure, we often find ourselves saying things like, "That wasn't too bad." What is the implicit plan in this statement? What is the control aspect? What implications does the assessment have for subsequent plans?
9. Control can apply to situations in which you are assessing a process ("Did I get 30 miles to the gallon?") and to situations in which you are evaluating another's performance ("Don't slouch!"). How does the introduction of another person change the nature of the control problem?
10. Some argue that accounting systems only measure costs and not opportunity costs. Do you agree?
11. Would firms engage auditors to certify their financial statements even if they are not required to do so? (*Hint*: Think about the credibility of unaudited statements). Also discuss why reputation is an auditor's primary asset.
12. Suppose that you are a journalist who has obtained a video copy of a particularly violent crime. You know that a broadcast would likely cause some emotional harm to the victim's family. However, you also know that airing the tape will increase your TV station's viewership significantly. Should you air the tape, even if there are no legal restrictions against doing so?

### Solutions to Short Essay

1. (LO-1) Your ultimate goal could be to earn as much as you can before you retire, say, 40 years after you graduate. With this goal in mind, you have to plan a career path and evaluate the three job offers to see which of these jobs will take you on that path. Besides pay, factors such as the reputation of the organization, the quality of on-the-job training you will get, opportunities to climb the organizational ladder are very important from a career perspective. If all three job offers are equally attractive in terms of the career you have chosen for yourself, then short-term goals and desires will dictate which job offer you should accept. All else equal, you will naturally want to accept the job offer that pays you the most, or you may be willing to accept slightly lower pay to live in a city that you like, or work for an organization with better reputation, and so on.
2. (LO-1) Yes, this statement is true. Opportunity cost is the value of the next best option. As more options become available, it is possible that a new option may be more attractive than the current best option, in which case the new option becomes the best option, and the current best option becomes the next best option. In this case, the opportunity cost *increases* but it can never decrease as long as all the current options are also available to choose from.
3. (LO-1) Let us say that the full-time MBA program takes two years to complete. The opportunity cost of pursuing the program is the income she will be losing over this period by quitting her existing job, the experience she will lose from not being on the job for two years, and any promotions she may be foregoing.
4. (LO-1) Differences in individual goals can arise from:
  - Differences in preferences: Some individuals place a greater weight on maximizing wealth, others place a greater weight on being the best in what they do (the two are not always perfectly correlated)
  - Attitudes toward risk: Some have a greater tolerance for risk than others
  - Differences in ethical thresholds: What is perfectly acceptable ethical behavior for some may not be acceptable to others.
5. (LO-2) The goal of a nonprofit hospital is to provide adequate healthcare to the community it serves at low cost, without a profit motive. The goal of a university is to meet the educational needs of the community/country and to promote knowledge and discovery. Many universities also attract students from other states/countries as part of an outreach effort to promote diversity and learning. State universities are mostly government funded and do not have an explicit profit motive, but most private universities do. The goal of an honor society in a university is to promote academic excellence, cultural diversity, and leadership.
6. (LO-2) Sales commissions are a way to motivate sales personnel to strive hard to sell more. The more they are able to sell, the more money they get. The advantage of course is that revenues and profits increase for the organization. The disadvantage is that commissions often make the sales people follow aggressive tactics with potential buyers (you may have experienced this behavior in auto dealerships, department stores, furniture stores, and consumer electronics stores). Such behavior may turn away customers in the long run. Commissions also promote cut-throat competition among sales personnel in vying for customers, which can prove counter-productive.

## Accounting: Information for Decision Making

7. (LO-2) In wars and in combat situations, individuals have to depend on each other for survival. Working well in groups becomes a matter of life and death. So there is a natural alignment between team and individual goals. In a typical profit-making organization, the “free-rider” problem is more difficult to eliminate, because there is a natural incentive for each individual to contribute minimally to team goals and yet try to reap the full benefit. You may see this behavior when you work on group assignments for your class. Some individuals take responsibility and put in the effort needed, while others – realizing that the work is going to get done – do not contribute as much, and devote their time to other “productive” activities. The incentives are similar in profit-making organizations.
8. (LO-3) When we say “that wasn’t too bad,” we are essentially comparing what happened with what we expected would happen. That is, our expectations were not met. Most of us plan ahead, and things don’t always go the way we plan, for reasons beyond our control. In such instances, we adjust our expectations and then evaluate what actually happened. For example, let us say you set out on a drive to Chicago from Houston and you plan to cover the distance in 12 hours. But along the way, you run into unexpected rough weather, and it takes you 18 hours to reach Chicago. Given the driving conditions that you had to endure, you say to yourself “that wasn’t too bad!”
9. (LO-3) Yes, it does! There is a control problem in both scenarios. But in the first scenario the control problem is not related to divergence in goals, which is the case when you have to evaluate another individual’s performance. A process can go out of control for reasons beyond your control, and all you can do is to fine tune the process. Feedback on how the process is going helps in this respect. In the second case, you have to control another individual’s actions through monitoring or by providing appropriate incentives.
10. (LO-4) Yes, in general, this is true. Most accounting systems are designed to measure historical performance. However, the purpose of a management accounting system is to help decision making by providing reasonable estimates of opportunity costs. To the extent that trends in historical cost patterns can help in estimating future costs (or opportunity costs), even traditional financial accounting systems do help.
11. (LO-4) One could argue effectively that firms, interested in surviving in a competitive marketplace, would want to do so. By engaging auditors even if not required to do so, firms are signaling to investors that they have nothing to hide and that they are good firms to invest in. Take another example, in this increasing global product markets, many companies seek third-party quality assurance (such as ISO 9000) to convey to all the markets around the world that their products are of high quality. Note that such third-party certifications are not required by governments.
12. (LO-5) This is a tough question. You face a difficult trade-off involving a troubling ethical dilemma. Many TV channels, especially family-oriented channels, would opt to not show the tape because it might hurt their viewership in the long-run, let alone cause emotional harm in the short run. Such channels do not face much of a trade-off. On the other hand, other TV stations, in particular cable channels, might well allow their profit motive to dictate their decision.

**Exercises**

1. Toys Ahoy! has 1,000 action figures in inventory that cost \$6.25 per unit to produce. Due to changing consumer preferences, the sales department is having great difficulty selling the action figures, and Toys Ahoy! must choose between two options. *Option 1*—scrap (dispose of) the action figures at a total cost of \$1,000 (for landfill fees); *Option 2*—rework all of the action figures, at a total cost of \$1,200 in labor and materials, and sell them to a local toy store for a total of \$750.

*Required:*

- a. What is the value of scrapping the action figures?
  - b. What is the value of reworking the action figures and selling them to the toy store?
  - c. Is the fact that Toys Ahoy! spent \$6.25 to produce each action figure relevant to your value computations?
- 
2. Jon Tyler is a handyman who does odd jobs such as painting, fixing leaky faucets, installing ceiling fans, and minor electrical work. Jill Safford recently contracted with Jon to paint the outside of her home, and chose a unique color that few persons would consider. The day before he planned to paint, Jon purchased an initial batch of 20 gallons of the paint. The local hardware store, which mixed the paint to order, charged Jon \$325; the store also noted its policy of “no refunds or exchanges on custom colors.” Unfortunately, Jon threw his back out that evening. By the time he recovered a month later, Jill had sold her home.

*Required:*

- a. What is Jon’s opportunity cost of using the paint for a new job?
- b. Suppose Jon decides to throw the paint out because no one else wants the color that Jill had picked out. As a hazardous substance, paint has to be properly disposed. The landfill will charge Jon \$40 to dispose of the paint (\$2 per can). In light of this new information, what is Jon’s opportunity cost of using the paint for a new job?
- c. Suppose Jill had paid a nonrefundable advance of \$350 to Jon. How, if at all, does this information affect Jon’s opportunity cost of using the paint for another job?

## Accounting: Information for Decision Making

3. Consider a professional sports team such as the Miami Heat, the Chicago Cubs, or the Colorado Avalanche. The team comprises many individuals, each of whom is a gifted athlete and is well paid. As a multimillion dollar business, the team also has several layers of management staff in addition to the usual complement of coaches and trainers. Professional sports teams are often owned by partnerships and corporations, with a wealthy individual having controlling interest.

*Required:*

a. What are the goals of a team's owners? Do these goals mesh with the goals of the coaching staff and the individual players?

b. What methods do owners use to align the goals of individual players with the goals of the team?

4. Many firms in the retail industry use "mystery shoppers" to evaluate the quality of their stores and employees. In addition, audit staff for fast-food restaurants such as McDonald's and Burger King use extensive checklists to evaluate the degree to which their franchisees are complying with company policies. On these unannounced audits, representatives of the company may check the freshness of the food, the average wait time for the drive through, and the cleanliness of the facilities.

*Required:*

Why do companies invest resources in such monitoring programs? Why is it not enough to instruct employees to follow prescribed company policies?

5. Dr. Sam "Smiley" Shapiro, DDS, has just graduated from a prestigious dental school in the Western United States. He has asked for your assistance in classifying the following actions/decisions within the context of the planning and control cycle: Plan, Implement, Evaluate, and Revise.

**Item #      Description**

- 1 Whether to hire two or three dental hygienists? Dr. Shapiro has narrowed his choices to two or three hygienists based on expected patient volume.
- 2 Prepare a staffing schedule so that at least one hygienist is available during all times the office is open.
- 3 Track the number of patients seen by each hygienist per week.
- 4 Reevaluate the adequacy of current staffing levels.

*Required:*

Classify each decision according to its stage in the planning and control cycle. Provide a brief rationale for each classification.

## Accounting: Information for Decision Making

6. After years of working for others, Gina Matheson has decided to open her own florist shop. Over time, Gina has gained considerable experience in the nuances of selling flowers and flower arrangements in the retail market. She also has developed good contacts with flower wholesalers. She currently is contemplating the pricing of bouquets for Mother's Day. This is an important decision because, as per the Society of American Florists, sales on this day account for 15 to 20% of the annual sales of flowers in the United States. (The other critical sales day is Valentine's Day, which falls on February 14).

*Required:*

Identify at least one decision/action for each of the four stages of the planning and control cycle: Plan, Implement, Evaluate, and Revise.

7. "I was trained as an engineer, I work as an engineer, and I intend to retire as an engineer. Why on earth would I want to learn accounting? Linda Payton, a senior production engineer at a Fortune 500 firm, clearly is unhappy that her boss asked her to attend a one-week seminar on managerial accounting before taking on her new position. Linda's new duties deal with managing tools. She has overall authority for when to replace tools, whether to buy them or make them, and what quantities to purchase or produce.

*Required:*

The following list presents five decisions that Linda might face in her job. How can managerial accounting information help with these decisions? For each decision, list at least one information item that Linda might use and whether the item is financial or nonfinancial in nature.

1. Whether actual costs are in line with expectations?
  2. Whether to make a tool in-house or buy it from a supplier?
  3. How many tools to purchase for making 100,000 units of a product?
  4. What is the right inventory level for a given tool?
  5. Whether to make a new tool or to refurbish an existing tool?
8. You have spent the last two days in San Diego, California, on company business. You flew in on Wednesday morning and took the red-eye flight out on Thursday evening. During this trip, you stayed with your friend, Darren. As Darren lives in the suburbs, you rented a car and paid \$80 for the rental and gas. Finally, as a courtesy, you treated Darren and his wife to dinner on Wednesday night (cost: \$90). You also spent \$45 toward other meals, even though you had breakfast with Darren on Thursday. Usually, your firm puts up its employees in a downtown hotel. The average cost for San Diego is \$140 per night (this is the discounted corporate rate). The firm also pays a per-diem meal allowance of \$50 (no receipt required). However, if you were with clients, the firm would reimburse the actual cost for the meal (receipt required).

*Required:*

Prepare an expense report for your trip (excluding airfare). Assume that if you stayed at the hotel, no car would have been needed as you can walk from the hotel to your firm's office.

Solutions to Exercises

1. (LO-1)
  - a. The value associated with scrapping the action figures is the cost associated with disposing of them. Because scrapping the action figures will cost \$1,000, the value of this option is **(\$1,000)**.
  - b. Reworking the action figures will cost Toys Ahoy! \$1,200, but selling them to the toy store will bring in \$750 in revenues. Thus, the value of reworking the action figures and selling them to the toy store is  $\$750 - \$1,200 = \mathbf{\$450}$ .  
Unfortunately, the value of both options is negative. However, relative to scrapping the toys, reworking them increase's Toys Ahoy!'s profit by  $\$450 - (\$1,000) = \$550$ . **Thus, reworking the action figures is the preferred option.**
  - c. Intuitively, the fact that Toys Ahoy! spent \$6.25 to produce each action figure is **not relevant to the decision** at hand because Toys Ahoy! has already incurred the expenditure – it is a sunk cost. *That is, this cost does not change relative to the status quo.* As discussed in more detail in Chapter 2, value is forward looking and involves measuring future sacrifices and future benefits.
  
2. (LO-1)
  - a. The opportunity cost of any option is the value of the next-best option. Assume Jon could use the same color paint for another job. What's Jon's next-best option? The problem makes it clear that the paint is "unique" and has few, if any, alternative uses. Given this, Jon's opportunity cost of using the paint for another job is **\$0**. This estimate assumes that there is no cost to storing the paint.
  - b. Jon's next-best option is to dispose of the paint at a cost of \$40. Jon can avoid this cost by using the paint for another job. Thus, the opportunity cost of using the paint for another job is **(\$40)**. Jon should therefore be willing to pay someone up to \$40 to let him use the paint in their job!
  - c. The fact that Jon received a non-refundable advance of \$350 does not change the opportunity cost in any way. The revenue and the cash costs are past events and are sunk. Both value and opportunity cost are forward looking – **because this amount does not change relative to the status quo, the \$350 is not relevant to the decision at hand.**



3. (LO-2)
- a. The owners likely have multiple goals. Making a profit is important, as is winning games and championships. Some owners probably enjoy the prestige and glamour associated with owning a professional team. Other owners wish to give back to the community by funding appropriate recreational outlets. Each person in the coaching staff ultimately worries about his or her own career. Surely, the coaching staff enjoys what they do and being associating with “winners.” However, some part of their concern about the team’s success stems from its effect on their personal career prospects. Coaches are not as worried as owners about the team’s overall profitability or other monetary issues. Players have potentially conflicting goals. On the one hand, they wish to do what is best for the team. However, they also recognize that they have only a few years in their careers and that their earnings during this period must sustain them through their lives. Thus, players bargain aggressively with owners, sometimes putting team profitability in jeopardy. Such actions may also create animosity among players and affect the team’s effectiveness. For instance, a player may “hold out” (i.e., not report to training camps) for more compensation. Players are also known to engage in acts that increase their visibility and stature at the team’s expense. Who among us does not know a “hot-dogging” athlete?
  - b. Teams can and do use a number of systems to align players’ incentives with team incentives. Clauses giving incentive pay for reaching different levels of the playoffs and reaching milestones in performance (e.g., batting averages, rushing yards) are common. Contracts also usually specify parameters for physical fitness, as well as norms for expected behavior. Contracts often allow teams to ‘fire’ players if they engage in behavior that damages a team’s reputation. Designing and implementing contract-based and formal control measures is difficult in this setting as team performance depends on many factors. It is often difficult to specify what players should do or to measure their contribution to the team’s success. Teams therefore rely a great deal on intangibles such as “leadership” and “culture” when motivating players to do the right thing. Coaches sometimes discipline players by benching them for games or denying players time on the field/court. They also rely on the players’ ego and the value players attach to their reputation to keep players in check.
4. (LO-2) Organizations invest in monitoring programs because the organization’s goals may not always coincide with the goals of individual employees. When owners and other stakeholders delegate decision making, they run the risk that employees will make decisions that may not be in the organization’s best interests. For example, employees may pad expense accounts, take excessive breaks or time off, or even steal from the company. Monitoring can help by either penalizing undesired behavior or rewarding desired behavior. For example, mystery shopper programs help assess the quality of store operations and make sure that employees are following company policies. For example, a Burger King franchisee may substitute lower quality ketchup or other condiments, or not keep the facilities up to the standards consistent with the franchisor’s corporate image. Audit visits and other mechanisms serve to deter such behavior – in extreme instances, the franchisee could lose its license. Just telling someone to follow the rules is not enough. Enforcement or follow-up is necessary. Without enforcement, employees might simply agree to the rules but then ignore them and do whatever they want. Incentive schemes such as bonus pay and stock options also help align individual goals with organizational goals.

5. The following table provides the required classifications, including comments pertaining to the rationale underlying each classification.

<b>Action/Decision</b>	<b>Stage</b>	<b>Rationale</b>
Whether to hire two or three dental hygienists? Dr. Shapiro has narrowed his choices to two or three hygienists based on expected patient volume.	<b><u>Plan</u></b>	This decision relates to the choice of a resource level. Hiring more staff provides greater capacity, allowing Dr. Shapiro to serve more patients, but also commits Dr. Shapiro to greater costs.
Prepare a staffing schedule so that at least one hygienist is available during all times the office is open.	<b><u>Implement</u></b>	This action relates to implementing the choice. The associated decision (we could view each possible schedule as a decision option) relates to how resources, in this case hygienists, will be used to deliver services.
Track the number of patients seen by each hygienist per week.	<b><u>Evaluate</u></b>	This on-going control process helps Dr. Shapiro figure out the efficiency and effectiveness with which he is using costly resources. Moreover, because Dr. Shapiro sees each patient during each visit, he also can personally track the quality of work done by each of his hygienists.
Re-evaluate the adequacy of current staffing levels.	<b><u>Revise</u></b>	Over several weeks or months, Dr. Shapiro will get a sense of whether his hygienists are fully utilized. He will also determine whether additional hygienists need to be hired or which, if any, of his hygienists need to be let go.

This problem illustrates the classical loop between planning and control. We typically begin with a plan that is based on a set of assumptions (in this case, expected patient volume). These assumptions are our beliefs about the unknown future. We then implement our choices. As time passes, we obtain new information about the actual outcomes (in this case, actual patient volume and the quality of work done by each hygienist). On an on-going basis, this new information will cause us to adjust how we implement our plans (e.g., change the schedule for the next week). Over a period, we will accumulate enough information to revise our original set of assumptions, which might cause us to revisit the decision. The overall point is that there is a natural cycle of doing something based on a set of assumptions, comparing actual outcomes with expectations, and then revising our assumptions. In many instances, the broad loop relating to a decision contains smaller loops within it. For instance, we can think of creating each week's schedule as forming a separate planning and control cycle.

6. (LO-3)

The following table lists the four stages of the planning and control cycle and the associated decisions/actions. There are many possible decisions for each category.

<b>Stage</b>	<b>Action/Decision</b>
Plan	One possible decision is whether to price at the same levels as last year or to raise prices by, for example, 10% to account for the higher cost of flowers this year. Other decisions include whether to hire additional help or how much money to spend on advertising.
Implement	Based on the chosen price level, order and stock enough bouquets to meet the expected demand. (Notice that we could view this as a decision in itself, viewing each volume of order as an option.)
Evaluate	Compare actual sales to budgeted sales. Identify reasons for any deviations. (Again, we could view this as a decision by framing each possible reason for a deviation as a possible option. We then choose among possible explanations.)
Revise	Gina would use data on actual sales, her prices versus the prices of other florists, and national trends to revise her expectations about future sales. This revised belief will be a key input into her pricing decision for next Mother's day.

As we see, Gina begins with a plan that is based on a set of assumptions (in this case, how much demand she might expect for any given price). These assumptions are her beliefs about the unknown future. She then implements her choices (e.g., post prices, order flowers). As Mother's day nears, pre-orders and information about other florists' prices might give Gina an impetus to revise her prices. That is, she obtains new information on an ongoing basis, which in turn causes her to adjust her implementation (e.g., revise prices, run more ads). Over a period, she will accumulate enough information to revise her original set of assumptions, which might cause her to improve the next pricing decision.

The overall point is that there is a natural cycle of doing something based on a set of assumptions, comparing actual outcomes with expectations, and then revising our assumptions. In many instances, the broad loop relating to a decision contains smaller loops within it. For instance, we can think of offering a discount at day's end as forming a separate planning and control cycle within the overall cycle that we discussed above.

## Accounting: Information for Decision Making

7. (LO-4) As shown below, Linda may be surprised to find managerial accounting information invaluable in her new position. As a manager, Linda decides how best to use the organizational resources entrusted to her, and she will find both financial and non-financial information from her company's managerial accounting system to be helpful for making these decisions.

Decision	Information Items	Are information items financial/non-financial in nature?
Whether actual costs are in line with expectations?	Budgeted costs	Budgeted and actual cost data are financial in nature.  Linda may use non-financial data such as the volume of production to adjust her estimates of expected costs. The more units produced, the greater the expected cost as the company will be using more materials and labor. Linda also may rely on non-financial data such as absenteeism rates and whether her company was starting a new product to figure out the source of the cost differences.
	Actual costs	
	Actual volume of production	
Whether to make a tool in-house or buy it from a supplier?	Price charged by the supplier	The supplier's price and internal cost data are financial.  Non-financial data include supplier quality and reliability, as well as the reliability and quality of the tools if they were manufactured by Linda's firm.
	Cost to make the tool internally	
	Supplier quality and reliability	
How many tools to purchase for making 100,000 units of a product?	Rate of wear	Use data, such as rate of wear, are non-financial. Cost data, which would be used to determine the amount of safety stock, are in financial terms.
	Expected cost of tool	
	Expected loss if tool not available	

## Accounting: Information for Decision Making

What is the right inventory level for a given tool?	Expected rate of use, variance in use rates across time periods (e.g., Linda's firm may have seasonal production cycles)  Cost of tool, cost of capital, other storage costs	Data concerning use patterns, including rate of wear and variance in use rates, are non-financial. Data about cost estimates, including storage costs and capital costs, are expressed in financial terms.
Whether to make a new tool or to refurbish an existing tool?	Cost to make the new tool  Cost to refurbish existing tool  Expected lives of the two tools  Quality of the tools	Again, the cost data are in financial terms whereas data pertaining to quality and expected lives are non-financial in nature.

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8. Let us begin by computing the expected cost if you had stayed at a hotel:

Cost of hotel for one night	\$140.00
Per-diem meal allowance	<u>\$100.00</u>
Total	<u><b>\$240.00</b></u>

Next, let us compute your *actual expenses*:

Cost of car rental	\$80.00
Cost of dinner Wednesday	\$90.00
Cost of other meals	<u>\$45.00</u>
Total cost	<u><b>\$215.00</b></u>

**At least five views exist regarding the appropriate expense report:**

- You could turn in a report for \$240, arguing that the firm would have spent this amount for the trip. Any cost savings stemming from your actions should belong to you.
- You have saved the firm some money by staying with Darren rather than in a hotel. Thus, you should turn in a report for \$215, justifying the dinner with Darren and the car rental as offsetting hotel costs.
- At another extreme, some would argue for a report of \$45 only, being the actual meal cost. Under this view, the car rental and the dinner are personal expenses and non-reimbursable. Further, you should only claim the lower of actual expenses or the per-diem allowance.
- You could claim the \$100 as the per-diem allowance for two days. After all, company policy allows you to claim \$50 per day for meals, no matter what you actually spend.
- A final view, which is perhaps what many of us would do, is to claim the car rental and the per-diem for two days ( $\$180 = \$80 + 2 \text{ days} \times \$50 \text{ per day}$ ), reasoning that the car rental is a reasonable off-set to the cost of the hotel.

There is no clear answer, and different people would reasonably claim different amounts. Deciding the reasonableness of travel expenses can be difficult. For instance, some might argue that the cost savings are fictitious. You might have been more productive if you had stayed in a hotel and had a restful night. Partying with friends might adversely affect your work quality the next day. In addition, perhaps you would have dined with clients or engaged in other beneficial activities (e.g., having dinner with colleagues to continue the meeting). These opportunities might have been missed because of your desire to have dinner with Darren. On the other hand, some might argue that the company is imposing costs by having you travel and spend time away from your family. Allowing you to spend time with friends and sightsee is one way to compensate for these non-pecuniary costs.

Many firms avoid these problems by formulating explicit policies. For instance, they might reimburse you \$100 per day as a flat fee if you do not stay at a hotel.

This exercise nicely illustrates that, just like beauty “lies in the eyes of the beholder,” there often is no bright line test for what is ethical or unethical. We can see this confusion in advice columns such as “Ask the Ethicist” that appear in the *New York Times Magazine*.