EXERCISE 1-1 (10 minutes)


EXERCISE 1-2 (20 minutes)

1. Planned gross profit for 19x9 = 10,000 units x $5 = $50,000
2. Actual gross profit for 19x9 = 10,000 units x $2 = $20,000
3. The actual gross profit is lower by $30,000 than the planned gross profit for two major reasons:
   a. Planned sales were $150,000 (10,000 units x $15) whereas actual sales were only $130,000 (10,000 units x $13). The difference of $2 in selling price per unit lowered both sales and gross profit by $20,000.
   b. Planned cost of production was $100,000 (10,000 units x $10) whereas actual cost of production was $110,000. The difference of $1 in cost of production per unit increased cost of production and lowered gross profit by $10,000.
4. Management would have more control over the second reason in (3) above and may be able to take actions to correct the situation because it involves cost of production. Cost of production may be controlled through the implementation of cost systems and procedures that help management control all elements of cost of production. On the other hand, management most probably has little control over the selling price per unit because, in competitive markets the selling price is determined by the laws of supply and demand and is not based on the cost of production of any particular company. Thus, every company would have to accept the market price or assume the risk of making lower sales or no sales at all.
PROBLEM 1-4 (10 minutes)

In discussing the ethical implications in this case, it is logical to consider short-term profit maximization versus long-term profit satisfaction. When managers disregard the ethics, and choose to make decisions that would maximize short-term profits, long-term repercussions may be serious. Local governments may investigate possible tax evasion. The company may get bad publicity in the host country, which may lead to the company's expulsion from the country. Internally, tax savings-driven policies would interfere with proper performance evaluation of managers. In the long run, ethical behavior of managers may help the company earn satisfactory profits in a stable environment for a long period of time.