

SOLUTIONS**Learning Goal 1****Multiple Choice**

1. b
2. d
3. a
4. b “Revenue” is a word that confuses many people. Usually they think revenue is the same thing as wealth (like cash, or some other valuable thing). Revenue is not a *thing*. Revenue is a measure of what customers paid for something the business sold. Revenue confirms the added value of what the business is offering.
5. d A business does not really know the total added value created by consuming resources until a sale is made. Making a sale does not mean there is a profit.
6. b Expenses are resources that are used up in operations and reduce wealth. Whether or not expenses will add value depends on how the resources are used.
7. c
8. c
9. a Notice that (d) is incorrect because a business can be adding value and still have a loss. This is because it is not adding *enough* value!
10. c Customers do not want cookie prices increased because of resources consumed by waste and loss.

SOLUTIONS

Learning Goal 1, continued

Reinforcement Problems

LG 1-1.

- a. A meal is created using various resources such as labor, food, and equipment. The meal provides valuable pleasure and energy to the customer, who pays for it.
- b. Information is made available that will inform people of the availability of new services and low-cost loans. People will want this information and want to borrow money, for which the bank will charge.
- c. The automobiles are made safer, which customers will perceive as adding to the total value of the automobile, making it more desirable. At a minimum, the cost of testing resources will be added to the price of the new car. The customer will probably pay it—and probably much more—very willingly.
- d. People are willing to pay more for better, safer surgery.

LG 1-2.

- a. Unless you think that people will like liver-flavored toothpaste (personally, I find it revolting), I would say that the total added value of the toothpaste is zero (unless it might be sold as a joke novelty) because I think no one will buy it at any price. So, the cost of the resources used to produce it will be lost, because thousands of tubes of the toothpaste will have to be disposed of, probably in a toxic-waste site.
- b. This is a difficult question, but typical of the uncertainty managers have to deal with. First, my feeling is that the exercise and child-care facilities will probably add more value than the value received from using four new trucks, depending upon how many other trucks are available and the need for the new ones. This is because healthy employees and employees with peace of mind will be far more careful and creative. They will produce and create quality things that ultimately increase the total added value (revenue). Second, cost of production will probably decline, employee turnover and training costs will be reduced, and company loyalty might be created. Thus, total expenses will also probably be reduced. This reduces the amount of resources used, even if total added value is not changed at all.

LG 1-3.

- a. This is a combination business. It is both a service (veterinary service) and a merchandising (pet-care products) business. However, it is primarily a service business.
- b. The clinic adds value primarily by providing veterinary medical care, which people need and are willing to pay for. Secondly, the clinic adds value by offering a selection of pet-care merchandise, which people also need and will pay for. Two new resources are being created: (1) veterinary medical services, and (2) pet-care merchandise selection.
- c. Total added value confirmed by the revenue was \$40,700 ($\$38,500 + \$2,200$). Based on the initial prices, the clinic apparently thought the merchandise had an added value of \$2,500, instead of \$2,200 it actually sold for.
- d. (1) Service resources consumed: $\$25,900$ ($\$21,200 + \$2,000 + \$450 + \$1,100 + \$400 + \750)
(2) Property resources consumed: $\$2,800$ ($\$2,000 + \800)
- e. The value chain includes consuming both services and property. Wages, rent, utilities, repairs, supplies, advertising, accounting and management, and cost of merchandise sold are the items that we know about. Total expenses in the value chain were \$28,700.

SOLUTIONS

Learning Goal 1, continued

LG 1-3, *continued*

- f. No. The repairs to the damaged equipment caused by poor training did not add value. Also, I have some doubts about the wages of the poorly trained employee adding much value in the future.
- g. The wealth of the business increased by \$12,000 during the month (\$40,700 – \$28,700). Because the business had this \$12,000 net income, I would say that last month was successful.

Note: Using the \$10,000 cash to purchase equipment does not diminish wealth; it simply changes form from cash into equipment. The merchandise, which is a resource purchased at some previous time, is now “consumed” because it was sold to customers.

LG 1-4.

- a. An account receivable is a legal right to collect money that the business owns as the result of making a sale. Even though you cannot touch it (like a desk or a computer) a legal right is property. Property that does not have physical substance, such as a legal right, is called “intangible property.” We discuss this more in Volume 2. Cash is not the same as accounts receivable. They are different kinds of property.
- b. This is a tricky question because it is not clear that any wealth (only services) is actually being received. However, each business is still accumulating wealth as a result of being in business! Example: suppose that Business A provides consulting service to Business B. Then Business B provides advertising service to Business A. Business B has now received consulting services without paying. Business A has now received advertising service without paying. Obtaining any valuable resource *without paying for it* (money saved) has exactly the same effect on total wealth as receiving the same amount of money from a sale.

Note: This concept assumes that the exchange of services is a genuine transaction in which each company is consuming resources as it provides real services—that no fraud or fake transactions are involved.