Recycling Equipment

Topic: ROI/Residual Income

Characters: David Hendricks, the cost accountant for a small, closely held chemical manufacuring company
William Jones, the plant manager

The chemical company currently gets rid of waste solvents by paying a hazardous waste disposal company to dispose of them in a special landfill site. The board of directors asked William Jones to find ways to reduce the cost of disposing the solvents. Jones then requested that David Hendricks determine the cost and effectiveness of equipment for recycling the solvents.

David has learned that the equipment would considerably reduce the amount of solvent being discarded. When he consulted two industry sources for estimates of the cost savings to the company, he found that they disagreed considerably about expected future costs for the disposal of hazardous wastes. With the lower estimate of cost savings, purchase of the equipment would increase the company's net income but would decrease the return on investment because the recycling equipment is very expensive. David recalculated his analyses with the higher estimate of cost savings. With the greater cost savings, the recycling equipment would increase both net income and ROL.

David is uncertain which analysis to present to Mr. Jones. David is very concerned about the environment and believes that the company should make a commitment to recycling. He thinks that the second analysis, which shows an increase in ROI, is more realistic, but he realizes that his opinion may be biased. David knows that the company's return on investment affects the bonuses for company managers. The board of directors and stockholders are very interested in both net income and ROL David believes that if he presents both analyses to Mr. Jones, the plant manager will not support the project. If David gives Jones only the second analysis, the manager may recommend approval to the board of directors

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