Potential costs and benefits to henley manufacturing

Finance

Accounting Requirement A Potential Costs and benefits to Henley Manufacturing In most cases, when a firm decides to announce its financial statements information to the shareholders during annual meetings, there are costs and benefits involved. In most scenarios, shareholders are interested in such information as it helps them in evaluating their ongoing investment decisions in a firm (Kimmel, Weygandt & Kieso, 2011). In this case of Henley Manufacturing, by announcing its sales and earnings goals at the shareholders' meeting, it is likely to undergo the following in terms of costs and benefits. Costs for disclosure: An announcement of sales increase by 15% and net income by 20% to the shareholders may be deemed by them as a source for pay increase demand by the managers and other employees. As such, the shareholders may resort to hiring new managers to replace current ones should they demand for huge pay rise. In this case, the announcement would serve as a cost to both the shareholders who will incur costs recruiting new managers and employees, as well as to the managers and employees as they will likely lose their jobs if they persist on pay rise. Second, such disclosure will imply the organization incurring information costs such as those of obtaining, gathering collating, maintaining, summarizing, and communicating the data on the financial statements effectively to the intended external users such as shareholders. Other costs under this category would be cost of auditing the reports before announcement, the cost to accounting staff tasked with maintaining the firm's financial statements, as well as the cost of printing the same and mailing to all the shareholders before the annual meeting day (Kimmel, Weygandt & Kieso, 2011). Third, there may be costs of competitive disadvantage as rival firms may use the same information in ways that may be detrimental to the company. Examples of information that may be leaked are the advertising strategies, pricing strategies and new products and markets development plans. Fourth, such an announcement will lead to incurring of litigation costs. These are costs that may arise in defending the company from actions that may be brought forth in the annual meeting by the shareholders or creditor lawsuits. Example of such costs may be payments to lawyers (direct costs) to defend the company from such suits, and production time lost by managers and other employees while preparing the reports. Fifth, the company may incur political costs that may arise by the government regulators and politicians advancing their own interests and proposing new taxes to the company due to the presumed ‘ forecasted excessive profitability’. Benefits: In most cases, companies are known to compete for corporate control of the market. This entails activities such as mergers and acquisitions. An announcement of forecasted increased sales and earnings growth would enable the company make informed decisions on its acquisition decisions of rival firms. Second, should Henley Manufacturing be a target for a friendly merger or offer for tender, enclosing such sales and growth details would be beneficial to them as it would imply that they have the incentives hence, raise their bid price on the same. Third, should Henley Manufacturing be a target for a hostile merger or acquisition, disclosing such information to the shareholders will greatly offer the firm’s managers incentives to show that the company is deemed for growth in future: hence, best if left in the hands of the current team of management and not merged with another firm. Fourth, disclosing such information would benefit the firm in the manner that it would shield it from future pressure from government agencies that may mandate them to disclose the same or more detailed information in future (Kimmel, Weygandt & Kieso, 2011). Consequently, announcing such sales and earnings information to the shareholders and other external parties allows for timely disclosures than if postponed or ignored up to when critically needed. Finally, the release of the same also helps the management in deciding on how best the facts contained therein will be interpreted in future financial years. 2. Recommendation to the CEO In line to the above costs and benefits for the disclosure, my recommendation to the CEO would be not to disclose or announce neither the sales goals nor the earnings goals to the shareholders. Based on the discussion presented above on the costs and benefits, it is pretty obvious that the costs are likely to outweigh the benefits of disclosure. Furthermore, the only tangible benefit from the same would be planned mergers or acquisitions, of which the company has none at the moment. Consequently, the company's history has been that of non-disclosure of the same and still it has managed to field positive results. It is unlikely that any disclosure will positively impact on the growth prospects of the firm. For instance, if the CEO discloses the sales and earnings growth rate goals, and then the projections become unattainable, the resultant effect may be for the company's prices to drop, offering of easy credit terms, and overspending in advertisement costs so as to attain the much anticipated growth goals. One way to avoid this disappointment would be to make less specific goals. 3. Change of my recommendation In all likelihood, should the projections have been for three years and not one, my recommendation to the CEO would change. This would be based on the fact that the CEO should recognize that greater consideration should be given to the matter since, the horizon of planning has been increased from one year to three years. In such long durations, it becomes more difficult for a firm to have accurate forecasts hence, the need for greater consideration. For instance, the attainment of the sales and earnings growth rate goals over the next three years would largely depend on factors such as industry-wide and market-wide competitive conditions. As such, my recommendations would automatically change. Requirement B The nature of cases as presented are now quite varied. A recommendation for disclosure would be largely based on the expectations of the person attending the annual meeting. For instance, cash flow forecasts and profitability forecasts would be of much interest to the financial analysts and investors more than any aspects of the financial statements. Therefore, it would be quite reasonable to recommend the same to the CEO. Consequently, I would reasonably recommend to the CEO the disclosure of the following goals subject to the costs and benefits as I had earlier on discussed: an annual earnings growth of 20%, an annual sales growth of 15%, a return on net tangible assets of 16%, the common equity return of 20% and the minimum profit margin of 5%. Presenting these growth goals would be quite essential for the shareholders and other stakeholders in the annual meeting (Kimmel, Weygandt & Kieso, 2011).

Reference Kimmel, P. D., Weygandt, J. J., & Kieso, D. E. (2011). Financial accounting: Tools for business decision making. Hoboken, N. J: John Wiley.