

SEGMENT REPORTING

Managers need more than a single, company-wide income statement; they need statements that focus on the various segments of a company.

DEFINITION OF A SEGMENT

A segment is any part or activity of an organization about which a manager seeks cost or revenue data. Examples of segments include: sales territories, products, divisions of a company, individual salespersons, individual customers, etc.

TRACEABLE AND COMMON COSTS

A cost is either traceable or common with respect to a particular segment.

Traceable costs arise because of the existence of the particular segment. Traceable costs would disappear if the segment itself disappeared.

Common costs support more than one business segment but are not traceable, in whole or in part, to any one of those segments.

SEGMENT REPORTING EXAMPLE**EXAMPLE:**

Mary Fischer, the owner of Mary's Market, would like information concerning the performance of the Market's two main segments—the meat and produce departments.

The following partial list of costs was provided to help identify fixed and variable and traceable and common costs:

	<i>Meat Department</i>	<i>Produce Department</i>
• Variable costs	<ul style="list-style-type: none"> • Wholesale cost of meats • Packaging materials 	<ul style="list-style-type: none"> • Wholesale cost of produce • Plastic bags and ties
• Traceable fixed costs	<ul style="list-style-type: none"> • Meat department manager's salary • Butchers' wages * • Meat department depreciation * • Rent on meat department spaces** 	<ul style="list-style-type: none"> • Produce department manager's salary • Workers' wages * • Produce department depreciation * • Rent on produce department spaces**
• Common fixed costs	<ul style="list-style-type: none"> • Rent on space occupied by general offices, checkout counters, etc. • General manager's salary • Accountant's salary • Checkout clerks' wages • Liability insurance premiums 	

* Depending on circumstances, all or part of the indicated costs could be variable.

** This assumes that the rent costs would be avoided if the department were eliminated.

SEGMENT REPORTING EXAMPLE

	<i>Total Company</i>	<i>Departments</i>	
		<i>Meats</i>	<i>Produce</i>
Sales	\$1,500,000	\$900,000	\$600,000
Variable expenses.....	<u>810,000</u>	<u>460,000</u>	<u>350,000</u>
Contribution margin.....	690,000	440,000	250,000
Traceable fixed expenses	<u>400,000</u>	<u>230,000</u>	<u>170,000</u> *
Department segment margin.....	290,000	<u>\$210,000</u>	<u>\$ 80,000</u>
Common fixed expenses not traceable to departments.....	<u>240,000</u>		
Net operating income	<u>\$ 50,000</u>		

		<i>Product Lines</i>	
		<i>Fresh Produce</i>	<i>Packaged Produce</i>
Sales	\$600,000	\$400,000	\$ 200,000
Variable expenses.....	<u>350,000</u>	<u>200,000</u>	<u>150,000</u>
Contribution margin.....	250,000	200,000	50,000
Traceable fixed expenses	<u>100,000</u>	<u>40,000</u>	<u>60,000</u>
Product line segment margin.....	150,000	<u>\$160,000</u>	<u>\$ (10,000)</u>
Common fixed expenses not traceable to product lines	<u>70,000</u>		
Department segment margin.....	<u>\$ 80,000</u>		

* The \$170,000 in traceable fixed expenses for the Produce Department changes to \$100,000 traceable and \$70,000 common expenses when the Produce Department is further segmented by product lines.

DANGERS IN ALLOCATING COMMON COSTS

Common costs should not be allocated among segments. If common costs are allocated, the results can be misleading.

EXAMPLE: Suppose the common costs of Mary’s Market were allocated on the basis of sales (a frequently used allocation basis).

	<i>Total</i>	<i>Product Lines</i>	
	<i>Company</i>	<i>Meats</i>	<i>Produce</i>
Sales	\$1,500,000	\$900,000	\$600,000
Variable costs	<u>810,000</u>	<u>460,000</u>	<u>350,000</u>
Contribution margin	690,000	440,000	250,000
Traceable fixed costs.....	<u>400,000</u>	<u>230,000</u>	<u>170,000</u>
Divisional segment margin.....	290,000	210,000	80,000
Allocated common fixed costs	<u>240,000</u>	<u>144,000</u>	<u>96,000</u>
Net operating income	<u>\$ 50,000</u>	<u>\$ 66,000</u>	<u>\$(16,000)</u>

If the Produce Department were closed down because of its apparent loss, the company would suffer an overall loss as shown below:

	<i>Total</i>	<i>Product Lines</i>	
	<i>Company</i>	<i>Meats</i>	<i>Produce</i>
Sales	\$900,000	\$900,000	—
Variable costs	<u>460,000</u>	<u>460,000</u>	—
Contribution margin	440,000	440,000	—
Traceable fixed costs.....	<u>230,000</u>	<u>230,000</u>	—
Divisional segment margin.....	210,000	210,000	—
Allocated common fixed costs	<u>240,000</u>	<u>240,000</u>	—
Net operating income	<u>\$(30,000)</u>	<u>\$(30,000)</u>	—