

The background is a dark green color. A large, abstract graphic is composed of a grid of parallel lines. The lines are colored in a gradient from yellow on the left to green on the right. The grid is not perfectly rectangular; it has a jagged, stepped appearance on the right side, suggesting a bar chart or a data visualization. The lines are spaced evenly and create a sense of depth and movement.

# MANAGEMENT ACCOUNTING

*Planning and Control*

*Wolk/Gerber/Porter*

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# Management Accounting

Planning and Control

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# Preface


**W**hile there are many management accounting books that are on the market, it is our belief that a particular niche has not as yet been filled. Our specific objectives in writing this book have been threefold:

1. To present the role of management accounting in the organization and the relatively complex and sophisticated concepts of management accounting in an understandable and down-to-earth manner with numerous illustrations;
2. To have an excellent group of questions, exercises, and problems, including the most varied and challenging selection of problems on the market from CMA and CPA examinations;
3. To present the elements of cost accounting, which form an important part of the underlying structure of management accounting, in a manner that will allow this subject matter to be appropriately integrated with the material of management accounting proper.

In terms of the third objective, the cost accounting chapters appear fairly early in the text (Chapters 6–10). We realize, of course, that many instructors will prefer to cover this material later in the course. Therefore, several alternative chapter sequences are suggested in the Instructor's Manual.

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## Teaching Aids

The Instructor's Manual also contains important information relative to the ancillaries accompanying this text. Included among the ancillary materials are templates utilizing Lotus 1-2-3 (series 3.0) spreadsheets that can be used for solving problems in many chapters throughout the book. These problems are designated in the text with the following symbol: 

Other ancillaries accompanying this book, in addition to the Instructor's Manual and the template for solving problems with Lotus 1-2-3, are:

Solutions Manual

Student Study Guide

Test Bank

Transparencies for all exercises and problems as well as selected key exhibits in the text

Check Figures

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## The User

There are two primary audiences for whom this book is intended. The first group is comprised primarily of sophomores in undergraduate programs in business administration and economics. The business administration students consist of both nonaccounting majors and accounting majors, although the former generally predominate in terms of sheer numbers. Typically, these students take a course in management accounting in the second semester of the sophomore year after a three-hour course in financial accounting. The second group consists of students in "generalist" types of MBA programs. One MBA approach often consists of a single required accounting course. The prerequisite is often six hours of accounting with the bulk of that generally being financial accounting. A second variation in MBA programs is a two-sequence accounting requirement with the second course being one devoted to management accounting. There is certainly much diversity within each of these two groups, not to mention differences between them. Nevertheless, we believe that both of these audiences of primarily nonaccounting majors can be well served by this book. The text itself has been made extremely flexible by the use of several appendixes containing more advanced material that can be included or excluded at the instructor's behest based upon student needs and abilities. Suffice it to say that whether sophomore or MBA, the student should gain a very significant understanding and appreciation of the importance of management accounting and its role and place in the organization of the enterprise.

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## Acknowledgments

We have found that many debts are accumulated along the way to completing an enterprise of this sort. Our reviewers provided many excellent insights and useful suggestions for both the book and the ancillaries. The reviewers and their present affiliations included Jack Bailes, Oregon State Univer-

sity; Jim Brown, University of Nebraska-Lincoln; Frank Daroca, Loyola Marymount University; Laverne Gebhard, University of Wisconsin-Milwaukee; Bob Koehler, The Pennsylvania State University; Linda Marquis, Northern Kentucky University; Diane Pattison, University of San Diego; Lynn Rans, California State University of Los Angeles; William Ryan, California State Polytechnic University at Pomona; and Jack Truitt, Washington State University. Special thanks go to Donna Ulmer of Southern Illinois University-Edwardsville for her work on the student study guide and Mick Watterson of Drake University for developing the templates.

We would also like to thank the many individuals at PWS-Kent Publishing Company for their work in helping to bring this project to its fruition, in particular Jack McHugh, Pam Rockwell, and Marcia Cole. We found them to be very knowledgeable professionals as well as fun to work with.

Our typists, Sue Hart and Ginger Wheeler deserve a very special commendation. They did an outstanding job of turning our often illegible pages into finished manuscript form. In addition, they showed a surprising mastery of high-tech accoutrements such as word processing programs and laser printers, which are absolutely indispensable to book writing in the age of the computer.

We would also like to thank the American Institute of Certified Public Accountants for its generosity in allowing us to use questions and problems from the CPA examinations. Permission has also been received from the Institute of Certified Management Accountants of the National Association of Accountants to use questions from past CMA examinations. In addition, special thanks go to The Quaker Oats Company and Meredith Corporation. Quaker Oats kindly allowed us to use their annual report, and Meredith provided us with several of their organization charts.

Finally, we dedicate this book to our wives: Barbara, Muriel, and Melissa. Without their patience and encouragement this project would have been more difficult to complete.

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CHAPTER **1**

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# **An Introduction to Management Accounting**

## **Learning Objectives**

After reading this chapter you should be able to:

1. Understand what management accounting involves.
2. Know how management accounting differs from financial accounting.
3. Understand the relationship between management accounting and cost accounting.
4. Understand what the planning process is.
5. Comprehend the types of decisions that comprise short-run planning.
6. Be aware of long-run planning issues.
7. Understand what control is and how it ties together with the planning function.

**O**rganizations need information to make decisions. One very important source of information for management is its accounting system. The information provided to management from its accounting system, as well as additional related analyses, forms the subject matter of management accounting.

It is probably obvious that information is needed by management in order to facilitate decision making. Without appropriate information, we cannot expect correct decisions to be made. Decision making is actually part of the broader managerial function of planning. Management accounting also facilitates the function of control (comparing actual results against plan). Both of these functions and how they relate to management accounting will be discussed shortly.

In order to put management accounting into perspective, let us first see—in very simple terms—how an accounting system works. A simple portrayal of an accounting system is shown in Exhibit 1–1.

To summarize Exhibit 1–1, we can say that an accounting system captures data, represented by the transactions of a firm, and converts the raw data into useful types of information. Among the useful reports prepared by the firm's accounting system are the three types of financial statements that you are familiar with: the balance sheet (also called the statement of financial position), the income statement, and the statement of changes in financial position (formerly called the funds flow statement). However, not all the information coming from the enterprise's accounting system falls under the scope of managerial accounting. Much of it goes to users outside the particular entity.

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## Financial Accounting and Management Accounting

**Financial accounting** is concerned with information provided by a firm's accounting system for users external to the firm. Some examples of financial accounting information include the following:

Financial statements to prospective lenders such as banks or other financial institutions;

Tax returns provided to the Internal Revenue Service (IRS) or state taxation agencies;

Filings with the Securities and Exchange Commission (SEC), a regulatory agency of the United States government, for firms whose securities are traded on stock exchanges such as the New York Stock Exchange or the American Stock Exchange;

Annual reports for stockholders of enterprises whose securities are publicly owned; registered for trading (buying and selling) on security exchanges.