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Managerial Accounting

Tenth Edition

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Managerial Accounting

Tenth Edition

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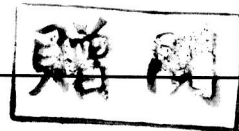
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Managerial Accounting

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TO THE STUDENT

A *Study Guide*, *Working Papers*, and *Student Solutions Manual* are available through your bookstore. The purpose of the *Study Guide* is to assist you in studying and reviewing the text material and provide you with a means of self-test by the study of the detailed outline and use of the true-false questions, multiple choice questions, matching and completion statements, and exercises included in the *Study Guide*. These may be used both in your initial study of the chapter material and in your subsequent review. The *Working Papers* have prepared forms and check figures for your problem assignments. The *Student Solutions Manual* has complete solutions for the even numbered problems, check figures for the odd numbered problems, and sample examinations with answers. If the *Study Guide*, *Working Papers*, or *Student Solutions Manual* are not in stock in your bookstore, ask the bookstore manager to order copies for you.

Preface

This edition was written as an integrated work in management accounting. Emphasis is placed upon those aspects of accounting with which all business majors should be familiar. If an overall theme were used to describe this text, it would focus on five key areas: cost accumulation and analysis, accounting aspects of planning, accounting aspects of control, accounting aspects of performance evaluation, and current relevant internal uses of managerial accounting information for many different management needs. These key areas were selected as the underlying theme for this text because we believe they best describe the "core" of management accounting theory and practice. We felt that if the core material were covered, the student would find the subject matter relevant in other business courses and, more importantly, in practice throughout his or her career.

This book may be used as a basic text for the student who has completed the first semester or quarter course in financial accounting at either the undergraduate or graduate level using its companion volume, Financial Accounting or any financial accounting text. The perspective is balanced and where optional treatments or approaches exist, these are identified and discussed.

Organization of the Text

Following each chapter are numerous questions, exercises, and problems. The majority of the problems adapted from the Certificate in Management Accounting Examination have been placed at the end of the problems. This permits the instructor to select assignments that range from easy-to-follow illustrative exercises and problems to difficult, thought-provoking problems that may be used for further class discussion.

The text is designed to provide an integrated approach to managerial accounting by using a building block approach, however, various chapters may be omitted or assigned out of sequence. Chapters I and 2 provide the necessary background, overview, and stimulus for the continued study of managerial accounting. After providing a foundation in managerial accounting, the emphasis of the course may focus on either a strictly managerial orientation or a systems/cost managerial accounting approach (or some combination of the two).

For example, an instructor who desired a strictly managerial orientation might assign Chapters 1 through 3 and 7 through 15, while a systems/cost/ managerial accounting orientation would include the entire text with the option of completing the course at any point after Chapter 13. In both sequences, Chapters 4 through 6, 14, 15, and 16 can be covered in any order that is desired. Chapter 13, Performance Reporting for Profit Centers and Investment Centers; Chapter 16, Financial Statement Analysis; Chapter 17, The Statement of Cash Flows are optional topics which may be included or omitted according to the preferences of the instructor. Some instructors begin their course with Chapter 16 and then move into Chapter 1.

Supplements for Students

A Study Guide to assist the student in studying and reviewing the text material (including self-testing by detailed outlines, true-false and multiple choice questions, matching and completion statements, and exercises), is also available as is a complete set of pre printed Working Papers (with check figures), a Student Solutions Manual, and alternative practice problems.

Acknowledgments

We have received invaluable assistance, ideas, comments, and constructive criticisms from both our students and our colleagues. A necessary ingredient in the writing of any textbook is the environment in which the effort took place. Our special thanks go to A. Benton Cocanougher—Texas A&M University, John M. Ivancevich—University of Houston, and William Staples—University of Houston—Clear Lake for their roles in providing this environment.

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August, 1994

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Learning Objectives

Chapter 1 introduces management accounting systems and managerial accounting. Studying this chapter should enable you to:

1. Understand the nature and purpose of both management information and management accounting systems.
2. Understand the objectives of management accounting.
3. Distinguish between financial and managerial accounting.
4. Understand the basic management structure and the role of decentralization.
5. Distinguish between line and staff functions.
6. Determine the general role of the controller in an organization.
7. Identify the various stages of planning.
8. Trace the information flows in a typical managerial accounting system.
9. Identify the basic uses of budgets and budgeting.
10. Identify the different cost classifications.
11. Distinguish between product costs and period costs, and explain the importance of this distinction in determining income.

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Managerial Accounting: An Introduction

INTRODUCTION

Managerial accounting is oriented towards providing quantitative financial information to managers for their use in planning, control, performance evaluation, and internal decision-making. The objective of this chapter is to provide an overview of the environment in which managers operate and to relate the role management and managerial accounting plays in that environment.

MANAGEMENT INFORMATION SYSTEMS

Organizations today are very complex systems. The components of the organization interact and change continuously. Managers of organizations must be able to coordinate and control these organizational components in order to operate efficiently and effectively.

To achieve their objectives, managers must develop a system for communicating information within the organization. This communication system is commonly referred to as a management information system. The function of a *management information system* is to collect, summarize, and communicate information needed by managers to facilitate internal decision-making and control. Managers must also provide information to external groups such as current and potential shareholders, creditors, and regulatory agencies. The management information system must also be capable of accommodating these users.

A management information system is composed of many subsystems. For instance, information might be collected to facilitate marketing decisions, other information might be needed for production scheduling decisions and different information might be needed for capital investment decisions. While some of the information required for each of these three decisions might be accounting data, information from other sources might also be required. An accounting information system is simply one segment or subsystem of the management information system. The function of the *accounting information system* is to collect and communicate *financial* information. The accounting information system is usually one of the largest and the most formal components of the total information system in an organization.

Two examples of management information systems used by well-known companies are summarized below.

The manager of a 7-Eleven outlet in Tokyo, Japan relies heavily on a computerized management information system to provide him with information about the purchasing habits of his customers and the items stocked in his store. This information shows what products are selling at various times of the day. This allows the manager to restock shelves with rice dishes that are popular with salarymen who shop between 7 and 9 p.m. and potato chip snacks that children buy on their way home from school.¹

Pizza Hut spent over \$20 million in 1993 to create electronic profiles of its customers. This system attempts to match the tastes of Pizza Hut's customers to the coupons sent to those customers. For example, individuals who normally ordered Neapolitan-style pizza received coupons for that type of pizza. Also, customers who had not ordered pizza for relatively long time periods received larger discounts than others. Pizza Hut has found that matching customers and their buying habits is more effective than sending uniform coupons to all of its customers.²

MANAGEMENT ACCOUNTING

Traditionally, the accounting information system has been thought of as consisting of two basic segments, financial accounting and management accounting. The basic difference between these two "types" of accounting lies in their user orientation. Utilizing this traditional breakdown, financial accounting is primarily concerned with users who are external to the firm and management accounting is concerned with internal users. However, it is perhaps more conceptually correct to define financial accounting as a subsystem of management accounting. This distinction may be seen by evaluating the definition of management accounting and the key terms found in that definition which was developed in Statements on Management Accounting, Statement Number 1A:³

¹ "Information Power," *Forbes* (June 21, 1993), 44.

² "How to Get Closer to Your Customers," *Business Week: Enterprise Edition* (1993), 44.

³ *Definition of Management Accounting, Statement Number 1A* (New York, National Association of Accountants, 1981), 4.