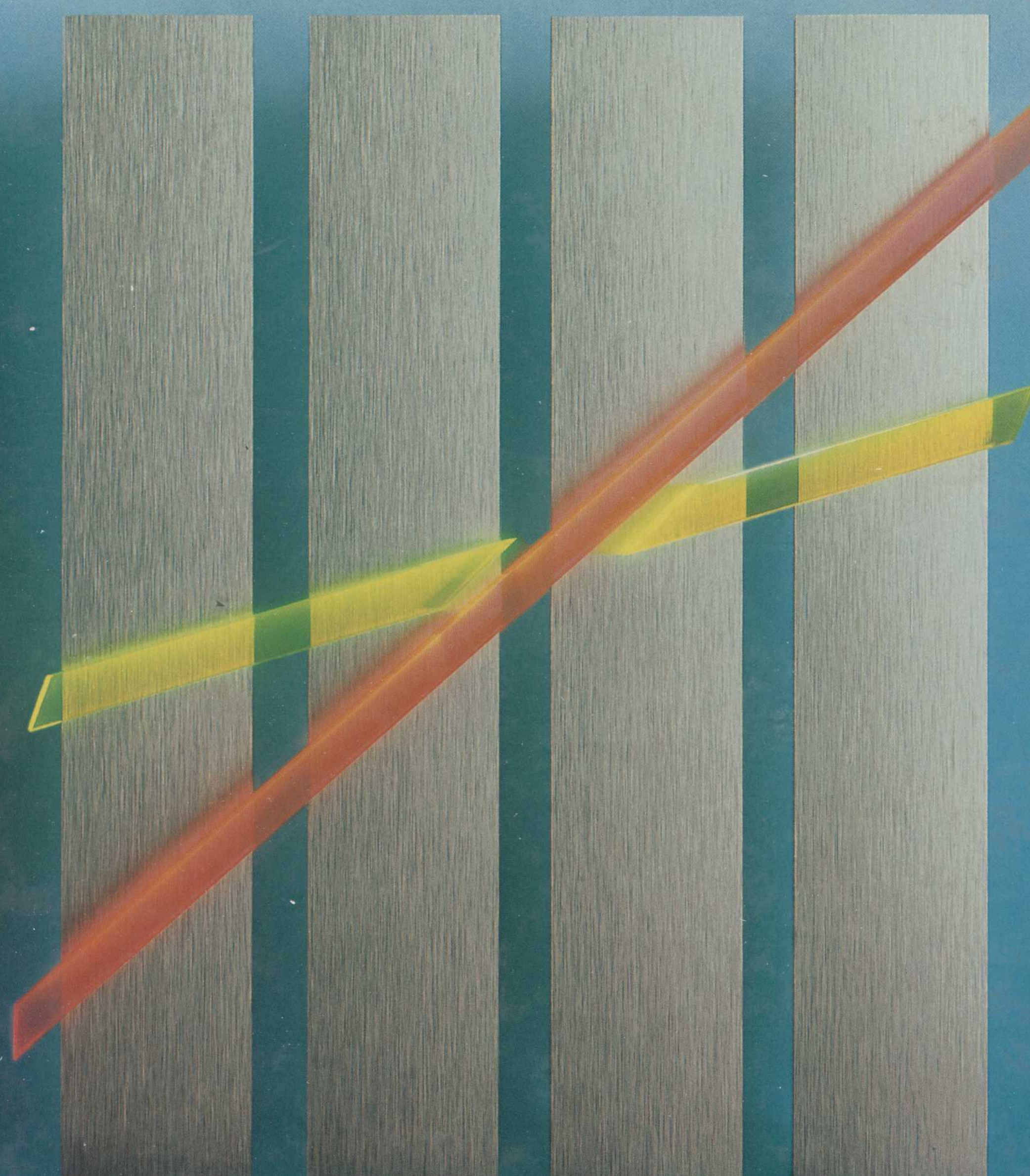
Sixth Edition

Managerial Accounting



Dominiak and Louderback

SIXTH EDITION

MANAGERIAL ACCOUNTING

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PREFACE

This book is designed for an introductory course in managerial accounting. Though we wrote the book with the undergraduate student in mind, we have had many reports of its successful use in both graduate and management development courses. One reason is that the wide variety of assignment material allows instructors to select assignments consistent with their students' backgrounds.

The book emphasizes the *uses* of managerial accounting information. It is therefore appropriate not only for accounting majors but also for nonaccounting business majors (in marketing, management, finance, etc.), and majors in nonbusiness areas such as engineering, mathematics, and the physical sciences. Our desire to reach a broad audience is consistent with enrollment trends in managerial accounting courses.

We make few assumptions about the reader's background knowledge. We assume a reader has had one or two terms of financial accounting or a working exposure to basic financial statements. But from a limited accounting background we expect only that a reader has some understanding of the most basic principles on which financial statements are based. The journal-entry/T-account framework appears only in Chapter 15 and is not, with the exception of that chapter, critical to understanding the concepts being presented.

Most discussions in the book focus on the functions of management: planning, decision making, controlling, and performance evaluation. This emphasis is apparent even in the chapters on product costing (Chapters 13–15), a topic that accounting textbooks seldom discuss with the nonaccountant in mind. Thus, those chapters approach product costing from the standpoint of analyzing results under different costing systems, rather than concentrating on cost-accumulation procedures or the accounting problems related to those procedures.

Our objectives in this edition remain essentially the same as those for the first five editions:

1. To present clearly and understandably the most important conceptual and practical aspects of managerial accounting;
2. To order the material in a way that allows the reader to build from elementary concepts to more complex topics and thus to integrate and expand early understanding;

3. To show students some of the interrelationships between managerial accounting and several other courses required in a normal business curriculum;
4. To show the reader, through discussion, illustration, and assignment material, what seems to us the almost infinite number of applications of managerial accounting principles to decision making in economic entities of all types (including personal decisions);
5. To encourage the reader to recognize that *people,* not entities, make decisions and are responsible for the results of those decisions.

We use several means to achieve these objectives. First, we use examples and illustrations liberally. Sometimes we introduce an important concept by means of an example; sometimes we try to give meaning to a rather abstract concept by immediately concentrating on an illustration. Second, we proceed through the text (and its increasingly complex concepts) in a building-block fashion. Thus, we begin with the principles of cost behavior and volume-cost-profit analysis, which underlie virtually all of managerial accounting, and use this basis to approach the more complex problems encountered in decision making, comprehensive budgeting, responsibility accounting, and product costing. A reader will see the continued reliance on previously developed concepts by the regularity of references to earlier chapters. Our frequent text references to the concepts, research, and practices of other business disciplines are intended both to encourage further study and to remind the reader that decision making requires an integration of knowledge from many areas.

The applicability of managerial accounting concepts to a wide variety of economic entities is most obvious in sections of the text that specifically refer to nonbusiness situations. But both the examples used in other parts of the text and the decision situations posed in assignment material also reflect our efforts to demonstrate the opportunities for using managerial accounting concepts in a nonbusiness context.

We regularly draw attention to the qualitative and difficult-to-quantify aspects of a topic. As part of the qualitative considerations, we discuss behavioral problems and point out the implications of such problems. We raise these qualitative issues to emphasize that decisions are made by individuals with beliefs and feelings. From the attention given to these issues, we also expect readers to recognize that accounting data provide relevant information but do not dictate courses of action.

Throughout the book we emphasize that decisions are made on the basis of estimates and that some factors important to a decision are difficult to quantify. Our intentions are to underscore (1) the presence of the manager's constant companion, uncertainty, and (2) the importance of recognizing all the available alternatives and all the factors relevant to each alternative. Both the text and many of the problems—especially those appearing relatively late in the assignment material—emphasize that a major problem in managing any enterprise is determining the right questions to ask and, concomitantly, what kinds of information to seek. In our opinion, students should learn that real-world problems do not present themselves in the form of schedules to be filled in and manipulated. Indeed, sometimes a manager's most difficult task is to discern, from the mass of economic activity taking place all around, exactly what the problem is that requires investigation and resolution.

PLAN OF THE BOOK

We organized this book to emphasize the fundamental importance of cost behavior patterns to all aspects of managerial decision making. After an introductory chapter, Part One, Volume-Cost-Profit Analysis and Decision Making, consists of four chapters that are intended to help the student develop a clear and firm grasp of the basic implications and applications of this fundamental issue. These chapters introduce different types of cost behavior, the reasons for such behavior, a tool for using information about behavior (volume-cost-profit analysis), and the basic analytical approaches used for making short-term decisions.

Part Two, Budgeting, treats operating, financial, and capital budgeting in four chapters. Chapter 6 concentrates on operating budgets, building on the material in Part One and introducing, on a more formal basis, behavioral considerations. Chapter 7 deals with financial budgeting, including cash budgets and pro forma balance sheets, and considers the special problems of budgeting for not-for-profit entities. Chapter 8 introduces capital budgeting; it considers income taxes, but deals only with relatively straightforward decisions involving acquiring new assets. Chapter 9 addresses more complex decisions, such as those involving the replacement of assets, and a few aspects of the Accelerated Cost Recovery System. Understanding Chapters 8 and 9 requires understanding the concepts of present value analysis. An Appendix offers a basic discussion and illustrations of present value analysis, with the emphasis on understanding relationships, and without mathematical development of present value factors.

Part Three integrates the topics of control and performance evaluation. Chapter 10 introduces responsibility accounting, alternative organizational structures, and cost allocation, emphasizing the behavioral aspects of these topics. Chapter 11 treats divisional performance evaluation—again, emphasizing behavioral issues. Chapter 12 discusses standard variable costs and variance analysis to evaluate cost centers.

Part Four consists of three chapters on product costing. These chapters emphasize the uses of product-cost information and analysis of reports prepared under different product-costing methods. Chapter 13 introduces the general ideas of cost flows, absorption costing, and predetermined overhead rates; both actual and normal costing are illustrated in a job-order context. Building on the standard cost concepts of Chapter 12 and absorption costing ideas of Chapter 13, Chapter 14 develops the idea of a standard fixed cost per unit and contrasts absorption and variable costing. Chapter 15 completes the product-costing coverage by introducing the special problems of a process-costing situation and illustrating the flows of costs through accounts. (An Appendix to Chapter 15 illustrates the first-in-first-out cost-flow assumption under process costing.)

NEW FEATURES

1. The most comprehensive change reflected in this edition is the integration of the terminology and techniques of the just-in-time philosophy and the new manufacturing environment. These ideas are incorporated throughout the book consistent with its overall plan, so that almost every chapter in Parts One through Four is affected. Some of the more extensive changes are:
   a. Chapter 1 introduces and contrasts the conventional and advanced environments.
   b. Chapters 2 and 3 use the new terminology in an expanded discussion of the importance of identifying the activity driving a cost.
   c. Chapters 4 and 10 give added attention to the importance of the traceability of costs. The discussion of allocated costs in Chapter 10 has been revised and expanded.
   d. The chapters on budgeting (Chapters 6 through 9) consider the effects of the new environment on inventory policies.
   e. The discussions of absorption costing and overhead application in Chapters 13 and 14 reinforce the importance of identifying cost drivers and illustrate the use of multiple bases for applying overhead.
   f. Chapter 15 includes an illustration of backflush costing as an example of the impact of a JIT environment on the cost accounting cycle.

   The assignment material in various chapters has been revised or expanded to reflect the integration described above. In addition, we have incorporated in the text the reported experiences of some companies that have adopted advanced manufacturing techniques.
2. We simplified and refined the discussion in Chapter 3 on the relationships between cost classification schemes and managerial actions.
3. The Appendix to Chapter 10 now includes the reciprocal method, as well as the step-down method, of allocating costs of service departments.
4. To reflect the increasing interest in a global perspective on business, Chapter 11 includes a section on the problems of performance evaluation and transfer prices in multinational companies.
5. Chapter 17 conforms with the pronouncement of the Financial Accounting Standards Board (Statement Number 95) on the cash flow statement.
6. About one-third of the assignment material is new or revised, and the total number of assignment items is slightly higher than in the fifth edition. Revisions and additions appear, for the most part, among exercises and the earlier problems.

ASSIGNMENT MATERIAL

One of the strongest features of this book is the assignment material, because of its integration with the text, its volume, and its variety with respect to degree of difficulty and economic entities. Users of previous editions have told us that these factors make it possible to teach this course, and the individual topics therein, at various levels of difficulty. Users cite the same factors as facilitating successful offerings of the course to students with widely different backgrounds and in a variety of time frames. (Comments in the Instructor's Manual aid in judicious choice of assignment items to accommodate different objectives.)

End-of-chapter material includes questions for discussion, exercises, problems, and cases. There are no review questions that can be answered by referring to a sentence or two in the chapter. Discussion questions are designed to increase students' understanding of concepts, and many have no clearly correct answers. Exercises are usually short and cover basic applications of one or two key concepts. Problems tend to be longer than exercises, and are more challenging, sometimes contain irrelevant information, and often ask the student to state reservations about whatever solutions are proposed. Both exercises and problems are generally arranged in order of increasing difficulty.

Cases normally contain less information than is needed to develop a single solution, our intention being to emphasize this inconvenient characteristic of real-life situations. For most cases, the student must propose an analytical approach appropriate to the available, relevant information. Cases, and the later problems, require the student to determine what principles are relevant and how those principles apply in a given situation. That is, these assignments are designed to encourage the student to think, since a manager must do so.

ALTERNATIVE CHAPTER SEQUENCING

The text contains more material than is needed for a one-term course, and we expect most users to omit one or more chapters. Several users have found alternative sequencing to be practical. We recommend, however, that whatever chapters are used be covered in the order presented. The text does offer considerable flexibility in the order of coverage.

Chapters in Part Four are the most likely candidates for omission or alternative sequencing. Chapters 17 and 18, on cash flows and financial analysis, are primarily for students whose financial accounting backgrounds did not include these topics. These chapters contain only a few, noncritical references to earlier chapters. Accordingly, either one or both of these chapters can be taken up at any time or omitted entirely.

Chapter 16, which discusses several quantitative methods of analysis, can be covered separately at any time after Chapter 12. Or, individual segments of that chapter can be assigned in conjunction with earlier chapters. The section on statistical decision theory has illustrations that use materials from Chapters 6, 8, and 12. The illustrations, while concentrating on applying the quantitative methods, draw on topics discussed in these earlier chapters. [The concept of expected value can be introduced as early as Chapter 5.] The section on inventory control models is particularly relevant to Chapter 6, which covers production and purchases budgets. The linear programming section extends the material in Chapter 5 on alternative uses of limited resources. Similarly, the section on learning curves can supplement the discussion in Chapter 3 on cost prediction methods.

Instructors desiring an earlier and greater emphasis on product costing can move to Chapters 12 through 15 after Chapter 5. Moving to Chapter 12 after Chapter 4 (or even after Chapter 3) is possible if additional time is given to the early discussion of indirect/common costs. (Note that giving early emphasis to product costing requires incorporating Chapter 12 in the coverage of that topic rather than as part of the study of responsibility accounting, because some understanding of standard costs is assumed in Chapters 14 and 15.) Some users increase the time available to cover product costing by omitting Chapters 10 and 11. Alternatively, some users omit all product-costing material, or omit all or parts of Chapter 14 and 15.

Chapter 4 can be omitted without loss of continuity. It is also possible to omit one or both chapters on capital budgeting (Chapters 8 and 9) without serious loss of continuity, and some users have taken these options.

The Appendix dealing with present values was designed to be used with Chapters 8 and 9 on capital budgeting. It assumes no previous exposure to the general idea of the time value of money, but those who have had such exposure are likely to find this material useful for review.

SUPPLEMENTARY MATERIAL

An **Instructor's Manual** contains suggested time allocations for alternative course lengths and chapter sequencing, additional comments on assignment materials, and further descriptions of teaching supplements such as Lotus templates. For each chapter, it provides a brief statement of the topical coverage, suggestions of assignment items for coverage of basic concepts, and a brief commentary about concepts or approaches that students find difficult to understand.

The **Test Bank** contains true-false and multiple-choice questions, and short problems. A Computerized Test Bank is also available on 3½-inch and 5¼-inch PC disks.

The **Solutions Manual** contains solutions for all assignment material and suggested times for completing assignments. It also provides notes to the instructor regarding class use of the material. These notes offer (1) alternative approaches for arriving at solutions; (2) suggestions for eliciting class discussion; and (3) suggestions for expanding individual assignments to cover new issues, pursuing existing issues in more depth, or highlighting relationships between managerial accounting concepts and concepts studied in other business disciplines.

A list of ***check figures*** for at least some parts of virtually every exercise, problem, and case is available in quantity from the publisher. In addition, ***transparencies*** are available upon adoption for all solutions and some text illustrations. There is also a set of Lotus 1-2-3® templates for various assignments.

The **Study Guide** is designed to help students obtain full value from the study of this text. This supplement, which offers key statements to use as guides in reading the chapters, includes not only objective questions but also a variety of short and medium-length problems (solutions included) to test understanding. The final section of the Guide for each chapter identifies those concepts, practices, or approaches that cause the most difficulty or greatest misunderstanding for students.

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Geraldine F. Dominiak
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BRIEF CONTENTS

CONTENTS