
ACCOUNTING

TEXT AND CASES

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Graduate School of
Business Administration
Harvard University

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Case material of the Harvard Graduate School of Business Administration is made possible by the cooperation of business firms who may wish to remain anonymous by having names, quantities, and other identifying details disguised while basic relationships are maintained. Cases are prepared as the basis for class discussion rather than to illustrate either effective or ineffective handling of administrative situations.

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ACCOUNTING
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Preface

An accounting text can be written with an emphasis on either of two viewpoints: (1) what the user of accounting information needs to know about accounting or (2) what the preparer of accounting reports needs to know about accounting. This book has as its focus the user of accounting information. Of course, such a person needs to know enough about the preparation of accounting reports to be an intelligent user of them, and this text includes the technical material needed for this purpose. The text is aimed primarily, however, at the person who wants to understand accounting so that he or she can be a knowledgeable user of accounting information.

The focus of the book makes it particularly appropriate for required “core” courses in accounting, where many of the students in the course are not planning to take further elective accounting courses. First, we believe that if a core course stresses the more analytical uses of accounting information by managers and outside analysts rather than the procedural details that the practicing accountant needs to know, then those students who do not take further accounting courses will be left with a positive view of the importance of accounting, rather than with the negative “bean counter” stereotype. Second, we feel that a user orientation in the core course is actually likely to generate a greater number of accounting majors from the class than if the course is oriented more toward the person who has already decided to major in accounting. Similarly, in our experience, the required accounting module in a

management development program will generate little participant interest unless the module is oriented toward the nonaccountant user of accounting information. In sum, we think the book conveys the fact that accounting is *interesting* and *fun*, not dull and tedious.

More specifically, this book is used in at least the following four ways:

1. An introductory course where most (if not all) of the students have no prior training in accounting. In many schools, this introduction comprises two separate courses, one dealing with financial accounting and the other with management accounting. Many schools use this book for both such courses, whereas some use it only for financial accounting (Chapter 1 and Chapters 2–14) or for management accounting (Chapter 1 and Chapters 15–27). This book is used in such introductory courses at both the upper undergraduate level and in graduate programs. In addition to its widespread use in schools of business and management, it is also used in introductory accounting courses in some law schools, education schools, and schools of public health.

2. An elective course that builds on a required introductory course in accounting—particularly where the introductory course has more of a procedural orientation, whereas the elective is intended to be more conceptual, analytical, and user-oriented.

3. The accounting module in a management development program, where the participants represent a variety of functional and technical backgrounds.

4. As a nontechnical accounting reference book for nonaccountants in business and other organizations.

Although designed for beginning students, the book does not contain enough “pencil-pushing” material to meet the needs of many instructors of beginning courses. Such instructors may wish to use the companion volume, *Accounting Principles Workbook*,¹ which, in addition to key terms and discussion questions, has much problem material (10–15 problems per chapter), a short practice set, and some cases that are not in this volume.

Many instructors also assign or recommend the programmed text, *Essentials of Accounting*,² either as preliminary to study of the subject (it is often sent in advance to participants in MBA and management development programs) or as a review device. This book is a self-study introductory treatment of financial accounting, geared to Part 1 of this text.

¹James S. Reece and Robert N. Anthony, *Accounting Principles Workbook*, 6th ed. (Homewood, Ill.: Richard D. Irwin, 1983).

²Robert N. Anthony, *Essentials of Accounting*, 3d ed. (Reading, Mass.: Addison-Wesley, 1983).

The Cases

As in previous editions, the cases have been selected because of their interest and educational value as a basis for class discussion. They are not necessarily intended to illustrate either correct or incorrect handling of management problems. Skill in the management use of accounting information can be acquired, we believe, only through experience. Thinking about a case, and discussing it in the classroom and in informal discussion groups, can help to provide such experience. In preparing to discuss a case in class, the student is required to *do something*—to analyze a problem, to weigh various factors involved in it, to make some calculations, to take a position, and so on. In class, the student is required to explain his or her point of view, to defend it, to understand and appraise the arguments of colleagues, and to decide what arguments are the strongest. Practice in doing these things helps to increase skill and understanding; in fact, many educators believe that the really important parts of a subject can be learned only by experience of some sort, as opposed to merely hearing or reading about them. Thus, although the case material comprises less than half the pages in this book, the discussion of these cases is by far the more important part of the educational process.

The Seventh Edition has a total of 121 cases, 10 more than the previous edition. Many of the cases are new, and the great majority of the cases that were carried over from the Sixth Edition have been updated (in some instances, with a change in case name).

Occasionally a student or instructor questions our use of small business settings for many of the cases. Such cases often avoid certain complexities at a point when the student is not yet prepared to deal with them. We also were interested to note a recent study which reported that small businesses (those employing fewer than 500 people): (1) represent 99.8 percent of all U.S. businesses, (2) produce 38 percent of the nation's GNP, (3) employ 47 percent of the nongovernment labor force, (4) contribute two out of three new jobs, and (5) produce twice as many innovations per employee as larger firms. We therefore feel that exposure to some small-business cases is beneficial to students, many of whom will eventually work in such firms or work with them as auditors or consultants.

Changes in the Seventh Edition

Developments in accounting, particularly financial accounting, have continued to be rapid in the last four years. These have resulted in many changes in the text and an overall expansion of Part 1, Financial Accounting. (Part 1 reflects FASB pronouncements through January 1983, as well as the 1981 and 1982 tax acts.) We have also modified Part 2, with particular emphasis on improving the sequencing of topics and reorganizing the longer chapters of the previous edition into shorter ones. The net result is that this edition totals 27 chapters—one introductory

and 13 each on financial reporting and management accounting—compared with the 23 chapters of the previous edition.

More specifically, some of the management accounting overview has been moved forward to Chapter 1, so that this chapter is more introductory to the entire book rather than just to Part 1. Chapters 2–7 reflect evolutionary and updating changes, including introduction of the debit-credit matrix in Chapter 4's discussion of computer-based recordkeeping systems; however, the basic thrust of these chapters remains the same. The former chapter, Other Expenses and Net Income, has been reorganized into two chapters: Chapter 8, Liabilities and Interest Expense, has expanded coverage of leases and contains an appendix explaining the concept of present value and its role in liability accounting; Chapter 9, Other Expenses, Net Income, and Owners' Equity, completes the more detailed discussion of the income and balance sheet. The funds flow chapter now follows, expanded to include the net monetary asset concept of funds and new materials (including ratios) on how to analyze funds flow statement information. After the Acquisitions and Consolidated Statements chapter, a new Chapter 12, Accounting and Changing Prices, deals with inflation accounting concepts, FASB-33 requirements, and foreign currency transaction and translation problems. The final two chapters of Part 1 have been modified slightly, including a brief discussion of the role of the efficient markets hypothesis in choosing among accounting principle alternatives. In these later chapters of Part 1, where students can cope better with the complexities of the statements of real companies, we have made greater use of materials taken from actual company annual reports, as opposed to hypothetical financial statement data.

Part 2, on management accounting, begins with Chapter 15's expanded description of the contrast between financial reporting and management accounting. All discussion of cost behavior, formerly split between two chapters, is now consolidated in Chapter 16, prior to any detailed discussion of full costs, differential costs, or responsibility costs. The previous edition's two long chapters on costing concepts and systems have been rearranged into three shorter chapters (17–19), the first of which emphasizes the uses made of full cost information in various kinds of organizations. Discussion of production cost variances (Chapter 20) still immediately follows the standard costing chapter, because most instructors seem to prefer this sequence; however, Chapter 20 can also be taught as a responsibility accounting chapter, just prior to Chapter 26, Analyzing and Reporting Performance. The consolidation of cost behavior materials in Chapter 16 also enabled us to present differential accounting concepts and techniques in two chapters (rather than three): Chapter 21 looks at short-run decisions, and Chapter 22 at longer-run (capital budgeting) decisions. The previous edition's lengthy chapter on responsibility accounting has been divided into two chapters, one

dealing with the management control structure (23) and the other with management control processes (24). The previous edition's final two chapters on programming, budgeting, and the reporting and analysis of performance have been retained with no substantial changes but are now followed by a new concluding chapter called Management Accounting System Design, which summarizes the concepts discussed in Part 2 of the book.

Acknowledgments

We are grateful to the many people who have made suggestions for improving this book. Included among those people are our colleagues at Harvard Business School and the Graduate School of Business Administration at The University of Michigan, particularly Robert H. Colson (Michigan). We also appreciate the comments of Brandt R. Allen, University of Virginia; Eduardo Ballarin, IESE (Barcelona); Bernard L. Beatty, Wake Forest University; F. Virgil Boyd, Loyola University of Chicago; David M. Buehlmann, University of Nebraska at Omaha; John C. Dawson, Grinnell College; Jesse F. Dillard, The Ohio State University; H. Peter Holzer and Rene P. Manes, University of Illinois at Urbana-Champaign; Wiley S. Mitchell, The University of Kansas; Frank Rose, Stanford University; William J. Ruckstuhl, The American College; and Donald R. Simons, Boston University.

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Robert N. Anthony
James S. Reece

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The 121 cases included in this book are listed below in alphabetical order, together with their authors' names. Cases with no author's name shown were written by, or under the supervision of, Robert N. Anthony or James S. Reece. Unless otherwise indicated, the copyright on all cases is held by Osceola Institute. No case herein may be reproduced in any form or by any means without the permission of the copyright holder.

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