# *Managerial Accounting for Business Leaders 1st edition Warren Solutions Manual*

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# CHAPTER 1
# INTRODUCTION TO MANAGERIAL ACCOUNTING

## DISCUSSION QUESTIONS

**1.** Managerial accounting is the process of developing information and management tools to achieve an organization's objectives. The management process is composed of four basic functions: strategic planning, measurement, evaluation, and control. Strategic planning is the process of developing long-term objectives. Measurement is the process of developing and agreeing upon performance metrics on how well the company is achieving its objectives. Evaluation is the process by which management monitors operations by comparing actual and expected results. Control is the process by which management takes actions to encourage specific behaviors or outcomes.

**2.** Financial accounting and managerial accounting are different in several ways. Financial accounting information is reported in statements that are useful to persons or groups outside of a company. These statements objectively report the results of operations for fixed periods of time and the financial condition of the business under generally accepted accounting principles. Managerial accounting information uses both subjective and objective information to meet the specific needs of management. This non-GAAP information can be reported periodically or as needed by management and can be reported for the entire entity or for segments of the organization. This information includes (i) historical data, which provide objective measures of past operations, and (ii) estimated data, which provide subjective estimates about future decisions.

**3.** **a.** Vertical units are structured as separate businesses within a company and normally develop and sell products directly to customers. Horizontal units are not responsible for developing and selling products, but provide services to other horizontal and vertical units within the company.
**b.** The accounting and legal departments are horizontal units within a company.
**c.** A consumer products division would be considered a vertical unit within a company.

**4.** Direct materials cost

**5.** Prime costs are the combination of direct materials and direct labor costs, while conversion costs are the combination of direct labor costs and manufacturing overhead costs.

**6.** Product costs are composed of three elements of manufacturing costs: direct materials cost, direct labor cost, and manufacturing overhead cost. These costs are treated as assets until the product is sold. Period costs consist of selling and administrative expenses that are used in generating revenue during the current period. They are recognized as expenses on the current period's income statement.

**7.** The three inventory accounts for a manufacturing business are as follows:
**a.** Finished goods inventory consists of completed (or finished) products that have not been sold.
**b.** Work in process inventory consists of the direct materials, direct labor, and manufacturing overhead costs for products that have entered the manufacturing process, but are not yet completed.
**c.** Materials inventory consists of the costs of the direct and indirect materials that have not entered the manufacturing process.

**8.** The cost of finished goods and the cost of work in process include the following:
**a.** Direct materials—the costs of materials that enter directly into the finished product.
**b.** Direct labor—the wages of factory workers who convert materials into a finished product.
**c.** Manufacturing overhead—the costs, other than direct materials and direct labor, that are incurred in the manufacturing process.


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## DISCUSSION QUESTIONS (Continued)

**9.** The manufacturing costs incurred during a period include direct materials used in production plus the direct labor and manufacturing overhead costs incurred during the period. The cost of goods manufactured for a period is computed by adjusting the manufacturing costs incurred during the period for the effects of beginning and ending work in process. Beginning work in process inventory is added and ending work in process is subtracted from the manufacturing costs incurred during a period to arrive at the cost of goods manufactured for the period.

**10.** A merchandising business purchases merchandise (products) in a finished state for resale to customers. The cost of product sold is called *cost of goods sold.* A manufacturer makes the product it sells using direct materials, direct labor, and manufacturing overhead, which make up the cost of goods manufactured included in the "Cost of goods sold" section of the income statement.



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## BASIC EXERCISES

**BE 1–1**

**Strategic planning (a)**
**Evaluation (c)**
**Control (b)**

**BE 1–2**

**a. Direct Materials**
**b. Direct Labor**
**c. Manufacturing Overhead**
**d. Manufacturing Overhead**

**BE 1–3**

**a. P**
**b. B**
**c. C**
**d. C**

**BE 1–4**

**a. Period cost**
**b. Product cost**
**c. Period cost**
**d. Product cost**

**BE 1–5**

| | | | |
|---|---|---|---|
| **a.** | **Work in process inventory, June 1** | | **$ 70,200** |
| | **Cost of direct materials used in production** | **$260,000** | |
| | **Direct labor** | **340,000** | |
| | **Manufacturing overhead** | **182,300** | |
| | **Total manufacturing costs incurred in June** | | **782,300** |
| | **Total manufacturing costs** | | **$852,500** |
| | **Work in process inventory, June 30** | | **(74,000)** |
| | **Cost of goods manufactured** | | **$778,500** |
| **b.** | **Finished goods inventory, June 1** | | **$ 33,300** |
| | **Cost of goods manufactured** | | **778,500** |
| | **Cost of finished goods available for sale** | | **$811,800** |
| | **Finished goods inventory, June 30** | | **(44,100)** |
| | **Cost of goods sold** | | **$767,700** |


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**BE 1–6**

**a.**

| Number of Guests | Nights per Visit | Guest Nights |
|---|---|---|
| 4,400 | 1 | 4,400 |
| 1,800 | 2 | 3,600 |
| 750 | 3 | 2,250 |
| 600 | 4 | 2,400 |
| 20 | 5 | 100 |
| | | 12,750 |

**b.** 15,000 available room nights (500 rooms × 30 nights in June)

**c.** $$\text{Occupancy Rate} = \frac{\text{Guest Nights}}{\text{Available Room Nights}}$$

$$\text{Occupancy Rate} = \frac{12{,}750}{15{,}000} = 85\%$$

**d.** The utilization (occupancy) rate has improved from 82% in the prior year to 85% in the current year.



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# EXERCISES

**Ex. 1–7**

a. Direct materials cost
b. Manufacturing overhead cost
c. Direct materials cost
d. Direct materials cost
e. Direct materials cost
f. Manufacturing overhead cost
g. Direct materials cost
h. Manufacturing overhead cost
i. Direct labor cost

**Ex. 1–8**

a. Manufacturing overhead cost
b. Direct materials cost
c. Manufacturing overhead cost
d. Manufacturing overhead cost
e. Direct materials cost
f. Manufacturing overhead cost
g. Direct materials cost
h. Manufacturing overhead cost
i. Direct materials cost
j. Direct labor cost

**Ex. 1–9**

b, e, g, h

**Ex. 1–10**

a. Period cost
b. Period cost
c. Product cost
d. Product cost
e. Product cost
f. Period cost
g. Product cost
h. Period cost
i. Product cost
j. Period cost
k. Period cost
l. Product cost
m. Product cost
n. Period cost
o. Period cost
p. Product cost
q. Product cost

**Ex. 1–11**

a. cost object
b. product
c. conversion
d. operational planning
e. cost
f. work in process inventory
g. decreases

**Ex. 1-12**

a. electricity used to run assembly line
b. prime
c. strategic
d. period
e. evaluation
f. indirect
g. product


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**Ex. 1–13**

| | | | |
|---|---|---|---|
| a. | indirect | g. | indirect |
| b. | direct | h. | indirect |
| c. | indirect | i. | indirect |
| d. | indirect | j. | indirect |
| e. | direct | k. | indirect |
| f. | indirect | l. | direct |

**Ex. 1–14**

**a. The errors in the manufacturing cost report are as follows:**

1. **The maintenance salaries of $84,400 and indirect materials of $56,200 should be included as manufacturing overhead.**

2. **The manufacturing overhead incorrectly includes the following items: sales salaries of $348,750, promotional expenses of $315,000, corporate office insurance and property taxes of $219,400, and corporate office depreciation of $90,000. These items should not be included as manufacturing overhead.**

**b. The corrected report is as follows:**

| Marching Ants Inc.<br>Manufacturing Costs<br>For the Quarter Ended June 30 | | |
|---|---|---|
| Cost of direct materials used in production | | $ 551,300 |
| Direct labor | | 478,100 |
| Manufacturing overhead: | | |
| Maintenance salaries | $ 84,400 | |
| Indirect materials | 56,200 | |
| Supervisor salaries | 517,500 | |
| Heat, light, and power | 140,650 | |
| Insurance and property taxes—plant | 151,900 | |
| Depreciation—plant and equipment | 123,750 | |
| Total manufacturing overhead | | 1,074,400 |
| Total | | $2,103,800 |



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**Ex. 1–15**

**a.**

| Sorensen Manufacturing Company<br>Income Statement<br>For the Month Ended January 31 | | |
|---|---|---|
| Revenues | | $1,200,000 |
| Cost of goods sold | | (675,000) |
| Gross profit | | $ 525,000 |
| Operating expenses: | | |
| Selling expenses | $215,000 | |
| Administrative expenses | 125,000 | |
| Total operating expenses | | (340,000) |
| Net income | | $ 185,000 |

**b.** Inventory balances on January 31:

| | |
|---|---|
| Materials ($250,000 – $180,000) | $70,000 |
| Work in Process ($180,000 + $450,000 + $180,000 – $760,000) | $50,000 |
| Finished Goods ($760,000 – $675,000) | $85,000 |

**Ex. 1–16**

| Diesel Additives Company<br>Balance Sheet<br>August 31 | | |
|---|---|---|
| Current assets: | | |
| Cash | | $167,500 |
| Accounts receivable | | 348,200 |
| Inventories: | | |
| Materials | $26,800 | |
| Work in process | 61,100 | |
| Finished goods | 89,400 | |
| Total inventories | | 177,300 |
| Supplies | | 13,800 |
| Prepaid insurance | | 9,000 |
| Total current assets | | $715,800 |



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**Ex. 1–17**

| | | |
|---|---|---|
| Materials inventory, September 1 | | $ 235,200 |
| Materials purchased during September | | 815,900 |
| Cost of materials available for use | | $1,051,100 |
| Materials inventory, September 30 | | (203,000) |
| Cost of direct materials used in production | | $ 848,100 |

**Ex. 1–18**

a. $352,410 ($19,660 + $332,750)
b. $328,910 ($352,410 – $23,500)
c. $474,120 ($515,770 – $41,650)
d. $461,770 ($515,770 – $54,000)
e. $165,000 ($1,240,000 – $1,075,000)
f. $172,000 ($1,240,000 – $1,068,000)

**Ex. 1–19**

| | | |
|---|---|---|
| Work in process inventory, January 1 | | $ 430,400 |
| Manufacturing costs incurred during January: | | |
| Cost of direct materials used in production | $1,287,200 | |
| Direct labor | 1,720,500 | |
| Manufacturing overhead | 3,600,700 | |
| Total manufacturing costs incurred | | 6,608,400 |
| Total manufacturing costs | | $7,038,800 |
| Work in process inventory, January 31 | | (391,200) |
| Cost of goods manufactured | | $6,647,600 |

**Ex. 1–20**

a. $942,500 ($116,600 + $825,900)
b. $812,500 ($942,500 – $130,000)
c. $501,120 ($540,000 – $38,880)
d. $470,000 ($540,000 – $70,000)
e. $920,000 ($1,100,000 – $180,000)
f. $155,000 ($1,100,000 – $945,000)


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**Ex. 1–21**

**a.**

| Firetree Manufacturing Company<br>Statement of Cost of Goods Manufactured<br>For the Month Ended March 31 | | | |
|---|---|---|---|
| Work in process inventory, March 1 | | | $ 428,700 |
| Direct materials: | | | |
| Materials inventory, March 1 | $ 240,000 | | |
| Purchases | 2,673,500 | | |
| Cost of materials available for use | $2,913,500 | | |
| Materials inventory, March 31 | (195,200) | | |
| Cost of direct materials used in production | | $2,718,300 | |
| Direct labor | | 3,200,000 | |
| Manufacturing overhead: | | | |
| Indirect labor | $ 320,000 | | |
| Machinery depreciation | 213,000 | | |
| Heat, light, and power | 174,000 | | |
| Supplies | 36,100 | | |
| Property taxes | 30,000 | | |
| Miscellaneous costs | 48,200 | | |
| Total manufacturing overhead | | 821,300 | |
| Total manufacturing costs incurred in March | | | 6,739,600 |
| Total manufacturing costs | | | $7,168,300 |
| Work in process inventory, March 31 | | | (510,400) |
| Cost of goods manufactured | | | $6,657,900 |

**b.**

| | |
|---|---|
| Finished goods inventory, March 1 | $ 582,100 |
| Cost of goods manufactured | 6,657,900 |
| Cost of finished goods available for sale | $7,240,000 |
| Finished goods inventory, March 31 | (614,400) |
| Cost of goods sold | $6,625,600 |



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**Ex. 1–22**

| | | | |
|---|---|---|---|
| a. | Finished goods inventory, January 1 | | $ 880,000 |
| | Cost of goods manufactured | | 4,490,000 |
| | Cost of finished goods available for sale | | $5,370,000 |
| | Finished goods inventory, January 31 | | (775,000) |
| | Cost of goods sold | | $4,595,000 |
| b. | Sales | | $ 6,600,000 |
| | Cost of goods sold | | (4,595,000) |
| | Gross profit | | $ 2,005,000 |
| c. | Gross profit | | $2,005,000 |
| | Operating expenses: | | |
| | Selling expenses | $530,000 | |
| | Administrative expenses | 340,000 | |
| | Total operating expenses | | (870,000) |
| | Net income | | $1,135,000 |

**Ex. 1–23**

| | | | |
|---|---|---|---|
| a. | Sales | | $ 792,000 |
| | Less gross profit | | (462,000) |
| | Cost of goods sold | | $ 330,000 |
| b. | Cost of goods manufactured | | $ 396,000 |
| | Less cost of goods sold | | (330,000) |
| | Finished goods inventory | | $ 66,000 |
| c. | Purchased materials | | $244,200 |
| | Less materials inventory | | (33,000) |
| | Direct materials cost | | $211,200 |
| d. | Total manufacturing costs | | $ 455,400 |
| | Less: Direct materials | $211,200 | |
| | Manufacturing overhead costs (indirect labor and factory depreciation)* | 198,000 | (409,200) |
| | Direct labor cost | | $ 46,200 |

* $171,600 + $26,400

| | | | |
|---|---|---|---|
| e. | Total manufacturing costs | | $ 455,400 |
| | Less cost of goods manufactured | | (396,000) |
| | Work in process inventory | | $ 59,400 |



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# PROBLEMS

## Prob. 1–24A

| Cost | Product Costs | | | Period Costs | |
|---|---|---|---|---|---|
| | Direct Materials Cost | Direct Labor Cost | Manufacturing Overhead Cost | Selling Expense | Administrative Expense |
| a. | | | | | X |
| b. | | | | X | |
| c. | X | | | | |
| d. | X | | | | |
| e. | | | X | | |
| f. | | | | X | |
| g. | | | | | X |
| h. | | | X | | |
| i. | | | X | | |
| j. | | | X | | |
| k. | X | | | | |
| l. | X | | | | |
| m. | X | | | | |
| n. | | | X | | |
| o. | X | | | | |
| p. | | | X | | |
| q. | | | X | | |
| r. | X | | | | |
| s. | | | X | | |
| t. | | | | X | |
| u. | | | X | | |
| v. | | | | | X |
| w. | | | X | | |
| x. | | | | X | |
| y. | | X | | | |
| z. | | | X | | |



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**Prob. 1–24B**

| Cost | Product Costs | | | Period Costs | |
|---|---|---|---|---|---|
| | Direct Materials Cost | Direct Labor Cost | Manufacturing Overhead Cost | Selling Expense | Administrative Expense |
| a. | | | | | X |
| b. | | | X | | |
| c. | | | | X | |
| d. | | | | X | |
| e. | X | | | | |
| f. | | | X | | |
| g. | | | X* | | |
| h. | | | X | | |
| i. | | | X | | |
| j. | X | | | | |
| k. | | X | | | |
| l. | | | X | | |
| m. | | | X | | |
| n. | | | X | | |
| o. | | X | | | |
| p. | X | | | | |
| q. | | | X | | |
| r. | | | X | | |
| s. | | | X | | |
| t. | | | X | | |
| u. | | | | X | |
| v. | X | | | | |
| w. | X | | | | |
| x. | | | X | | |
| y. | | | | | X |
| z. | X | | | | |

* Item g might also be classified as direct materials cost if the cost is significant since it can be directly traced to the end product.



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**Prob. 1–25A**

| Cost | Product Costs | | | Period Costs | |
|---|---|---|---|---|---|
| | Direct Materials Cost | Direct Labor Cost | Manufacturing Overhead Cost | Selling Expense | Administrative Expense |
| a. | | | X | | |
| b. | X | | | | |
| c. | X | | | | |
| d. | | | X | | |
| e. | | | | X | |
| f. | | | | X | |
| g. | | | X | | |
| h. | | | | | X |
| i. | | | X | | |
| j. | | | X | | |
| k. | | | X | | |
| l. | | | | | X |
| m. | | | | | X |
| n. | | | X | | |
| o. | | | X | | |
| p. | | | | | X |
| q. | | | X | | |
| r. | | | X | | |
| s. | | | X | | |
| t. | | | X | | |
| u. | | | | | X |
| v. | | | | X | |
| w. | | X | | | |
| x. | | | X | | |



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**Prob. 1–25B**

| Cost | Product Costs | | | Period Costs | |
|---|---|---|---|---|---|
| | Direct Materials Cost | Direct Labor Cost | Manufacturing Overhead Cost | Selling Expense | Administrative Expense |
| a. | | | | X | |
| b. | | | | | X |
| c. | X | | | | |
| d. | | | X | | |
| e. | | | | X | |
| f. | | | X | | |
| g. | | | X | | |
| h. | | X* | | | |
| i. | | | X | | |
| j. | X | | | | |
| k. | | | X | | |
| l. | X | | | | |
| m. | | | X | | |
| n. | X | | | | |
| o. | | | | | X |
| p. | | | X | | |
| q. | | | X | | |
| r. | | | | X | |
| s. | X | | | | |
| t. | | | | X | |
| u. | X | | | | |
| v. | | X | | | |
| w. | | | | | X |
| x. | | | | X | |

* Health insurance premiums are employment benefits for direct labor and are included as part of the direct labor cost.



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**Prob. 1–26A**

1. **The most logical definition for the final cost object would be the patient. The reason is that the cost can be accumulated at the patient level for billing and insurance reimbursement purposes.**

2.

| Cost | Direct | Indirect |
|---|---|---|
| a. | | X |
| b. | X | |
| c. | X | |
| d. | | X |
| e. | | X |
| f. | X | |
| g. | | X |
| h. | | X |
| i. | X | |
| j. | | X |
| k. | | X |
| l. | X | |
| m. | | X |
| n. | X | |
| o. | | X |
| p. | X | |
| q. | | X |
| r. | | X |
| s. | | X |
| t. | | X |
| u. | | X |


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**Prob. 1–26B**

1. **The most logical definition for the final cost object would be a hotel guest. Guests consume services such as a meal, a night's stay in a hotel room, room service, a telephone call, etc.**

2.

| Cost | Direct | Indirect |
|---|---|---|
| a. | | X |
| b. | | X |
| c. | | X |
| d. | X | |
| e. | X | |
| f. | X | |
| g. | | X |
| h. | | X |
| i. | X | |
| j. | | X |
| k. | X | |
| l. | | X |
| m. | | X |
| n. | X | |
| o. | | X |
| p. | | X |
| q. | X | |
| r. | | X |
| s. | X | |
| t. | | X |
| u. | | X |
| v. | X | |
| w. | | X |



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**Prob. 1–27A**

**1. Rainier Company**

| | | |
|---|---|---|
| **a.** | **$111,500** | **($950,000 + $100,000 – $938,500)** |
| **b.** | **$5,598,500** | **($938,500 + $2,860,000 + $1,800,000)** |
| **c.** | **$5,616,500** | **($5,598,500 + $400,000 – $382,000)** |
| **d.** | **$5,635,000** | **($615,000 + $5,616,500 – $596,500)** |
| **e.** | **$3,585,000** | **($9,220,000 – $5,635,000)** |
| **f.** | **$2,585,000** | **($3,585,000 – $1,000,000)** |

**Yakima Company**

| | | |
|---|---|---|
| **a.** | **$708,200** | **($48,200 + $710,000 – $50,000)** |
| **b.** | **$1,330,000** | **($2,484,200 – $708,200 – $446,000)** |
| **c.** | **$169,100** | **($2,660,600 – $2,491,500)** |
| **d.** | **$211,500** | **($2,491,500 + $190,000 – $2,470,000)** |
| **e.** | **$2,080,000** | **($4,550,000 – $2,470,000)** |
| **f.** | **$580,000** | **($2,080,000 – $1,500,000)** |

**2.**

**Yakima Company**
**Statement of Cost of Goods Manufactured**
**For the Month Ended May 31**

| | | | |
|---|---|---|---|
| Work in process inventory, May 1 | | | $ 176,400 |
| Direct materials: | | | |
| Materials inventory, May 1 | $ 48,200 | | |
| Purchases | 710,000 | | |
| Cost of materials available for use | $758,200 | | |
| Materials inventory, May 31 | (50,000) | | |
| Cost of direct materials used | | $ 708,200 | |
| Direct labor | | 1,330,000 | |
| Manufacturing overhead | | 446,000 | |
| Total manufacturing costs incurred in May | | | 2,484,200 |
| Total manufacturing costs | | | $2,660,600 |
| Work in process inventory, May 31 | | | (169,100) |
| Cost of goods manufactured | | | $2,491,500 |



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**Prob. 1–27A (Concluded)**

**3.**

| Yakima Company<br>Income Statement<br>For the Month Ended May 31 | | |
|---|---|---|
| Sales | | $ 4,550,000 |
| Cost of goods sold: | | |
| Finished goods inventory, May 1 | $ 190,000 | |
| Cost of goods manufactured | 2,491,500 | |
| Cost of finished goods available for sale | $2,681,500 | |
| Finished goods inventory, May 31 | (211,500) | |
| Cost of goods sold | | (2,470,000) |
| Gross profit | | $ 2,080,000 |
| Operating expenses | | (580,000) |
| Net income | | $ 1,500,000 |



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**Prob. 1–27B**

**1. On Company**

**a. $30,800 ($282,800 + $65,800 – $317,800)**
**b. $854,000 ($317,800 + $387,800 + $148,400)**
**c. $800,800 ($854,000 + $119,000 – $172,200)**
**d. $827,400 ($224,000 + $800,800 – $197,400)**
**e. $299,600 ($1,127,000 – $827,400)**
**f. $182,000 ($299,600 – $117,600)**

**Off Company**

**a. $581,560 ($685,720* + $91,140 – $195,300)**
**b. $685,720 ($1,519,000 – $256,060 – $577,220)**
**c. $195,300 ($1,727,320 – $1,532,020)**
**d. $256,060 ($1,532,020 + $269,080 – $1,545,040)**
**e. $399,280 ($1,944,320 – $1,545,040)**
**f. $234,360 ($399,280 – $164,920)**

*** *Note:* The student must calculate part (b) prior to calculating part (a) since the solution to part (b) is needed as an input to part (a).**

**2.**

| On Company<br>Statement of Cost of Goods Manufactured<br>For the Month Ended December 31 | | | |
|---|---|---|---|
| Work in process inventory, December 1 | | | $ 119,000 |
| Direct materials: | | | |
| Materials inventory, December 1 | $ 65,800 | | |
| Purchases | 282,800 | | |
| Cost of materials available for use | $348,600 | | |
| Materials inventory, December 31 | (30,800) | | |
| Cost of direct materials used in production | | $317,800 | |
| Direct labor | | 387,800 | |
| Manufacturing overhead | | 148,400 | |
| Total manufacturing costs incurred in December | | | 854,000 |
| Total manufacturing costs | | | $ 973,000 |
| Work in process inventory, December 31 | | | (172,200) |
| Cost of goods manufactured | | | $ 800,800 |


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**Prob. 1–27B (Concluded)**

**3.**

| On Company<br>Income Statement<br>For the Month Ended December 31 | | |
|---|---|---|
| Sales | | $1,127,000 |
| Cost of goods sold: | | |
| Finished goods inventory, December 1 | $ 224,000 | |
| Cost of goods manufactured | 800,800 | |
| Cost of finished goods available for sale | $1,024,800 | |
| Finished goods inventory, December 31 | (197,400) | |
| Cost of goods sold | | (827,400) |
| Gross profit | | $ 299,600 |
| Operating expenses | | (117,600) |
| Net income | | $ 182,000 |



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**Prob. 1–28A**

**1.**

| Robstown Corporation<br>Statement of Cost of Goods Manufactured<br>For the Year Ended December 31, 20Y8 | | | |
|---|---|---|---|
| Work in process inventory, January 1, 20Y8 | | | $ 63,900 |
| Direct materials: | | | |
| Materials inventory, January 1, 20Y8 | $ 44,250 | | |
| Purchases | 556,600 | | |
| Cost of materials available for use | $600,850 | | |
| Materials inventory, December 31, 20Y8 | (31,700) | | |
| Cost of direct materials used in production | | $ 569,150 | |
| Direct labor | | 1,100,000 | |
| Manufacturing overhead: | | | |
| Indirect labor | $115,000 | | |
| Depreciation expense—factory equipment | 80,000 | | |
| Heat, light, and power—factory | 53,300 | | |
| Property taxes—factory | 40,000 | | |
| Rent expense—factory | 27,000 | | |
| Supplies—factory | 9,500 | | |
| Miscellaneous costs—factory | 11,400 | | |
| Total manufacturing overhead | | 336,200 | |
| Total manufacturing costs incurred in 20Y8 | | | 2,005,350 |
| Total manufacturing costs | | | $2,069,250 |
| Work in process inventory, December 31, 20Y8 | | | (80,000) |
| Cost of goods manufactured | | | $1,989,250 |



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**Prob. 1–28A (Concluded)**

**2.**

| Robstown Corporation<br>Income Statement<br>For the Year Ended December 31, 20Y8 | | | |
|---|---|---|---|
| Sales | | | $ 3,850,000 |
| Cost of goods sold: | | | |
| Finished goods inventory, January 1, 20Y8 | | $ 101,200 | |
| Cost of goods manufactured | | 1,989,250 | |
| Cost of finished goods available for sale | | $2,090,450 | |
| Finished goods inventory, | | | |
| December 31, 20Y8 | | (99,800) | |
| Cost of goods sold | | | (1,990,650) |
| Gross profit | | | $ 1,859,350 |
| Operating expenses: | | | |
| Administrative expenses: | | | |
| Office salaries expense | $318,000 | | |
| Depreciation expense—office | | | |
| equipment | 30,000 | | |
| Property taxes—office building | 25,000 | $ 373,000 | |
| Selling expenses: | | | |
| Advertising expense | $400,000 | | |
| Sales salaries expense | 200,000 | 600,000 | |
| Total operating expenses | | | (973,000) |
| Net income | | | $ 886,350 |



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**Prob. 1–28B**

**1.**

| Shanika Company<br>Statement of Cost of Goods Manufactured<br>For the Year Ended December 31, 20Y6 | | | |
|---|---|---|---|
| Work in process inventory, January 1, 20Y6 | | | $109,200 |
| Direct materials: | | | |
| Materials inventory, January 1, 20Y6 | $ 77,350 | | |
| Purchases | 123,500 | | |
| Cost of materials available for use | $200,850 | | |
| Materials inventory, December 31, 20Y6 | (95,550) | | |
| Cost of direct materials used in production | | $105,300 | |
| Direct labor | | 186,550 | |
| Manufacturing overhead: | | | |
| Indirect labor | $ 23,660 | | |
| Depreciation expense—factory equipment | 14,560 | | |
| Heat, light, and power—factory | 5,850 | | |
| Property taxes—factory | 4,095 | | |
| Rent expense—factory | 6,825 | | |
| Supplies—factory | 3,250 | | |
| Miscellaneous costs—factory | 4,420 | | |
| Total manufacturing overhead | | 62,660 | |
| Total manufacturing costs incurred in 20Y6 | | | 354,510 |
| Total manufacturing costs | | | $463,710 |
| Work in process inventory, December 31, 20Y6 | | | (96,200) |
| Cost of goods manufactured | | | $367,510 |



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**Prob. 1–28B (Concluded)**

**2.**

| Shanika Company<br>Income Statement<br>For the Year Ended December 31, 20Y6 | | | |
|---|---|---|---|
| Sales | | | $ 864,500 |
| Cost of goods sold: | | | |
| Finished goods inventory, January 1, 20Y6 | | $ 113,750 | |
| Cost of goods manufactured | | 367,510 | |
| Cost of finished goods available for sale | | $ 481,260 | |
| Finished goods inventory, | | | |
| December 31, 20Y6 | | (100,100) | |
| Cost of goods sold | | | (381,160) |
| Gross profit | | | $ 483,340 |
| Operating expenses: | | | |
| Administrative expenses: | | | |
| Office salaries expense | $ 77,350 | | |
| Depreciation expense—office equipment | 22,750 | | |
| Property taxes—headquarters building | 13,650 | $ 113,750 | |
| Selling expenses: | | | |
| Advertising expense | $ 68,250 | | |
| Sales salaries expense | 136,500 | 204,750 | |
| Total operating expenses | | | (318,500) |
| Net income | | | $ 164,840 |



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## MAKE A DECISION

**MAD 1–29**

**a. Comfort Plus:**

| Number of Guests | | Nights per Visit | | Guest Nights |
|---|---|---|---|---|
| 3,680 | × | 1 | = | 3,680 |
| 1,100 | × | 2 | = | 2,200 |
| 500 | × | 3 | = | 1,500 |
| Total guest nights | | | | 7,380 |

**Connors:**

| Number of Guests | | Nights per Visit | | Guest Nights |
|---|---|---|---|---|
| 4,390 | × | 1 | = | 4,390 |
| 700 | × | 2 | = | 1,400 |
| 800 | × | 3 | = | 2,400 |
| Total guest nights | | | | 8,190 |

**b. Comfort Plus: 300 rooms × 30 days = 9,000 available room nights for April**
**Connors: 350 rooms × 30 days = 10,500 available room nights for April**

**c.** $$\text{Occupancy Rate} = \frac{\text{Guest Nights}}{\text{Available Room Nights}}$$

$$\text{Comfort Plus: } \frac{7{,}380}{9{,}000} = 82\%$$

$$\text{Connors: } \frac{8{,}190}{10{,}500} = 78\%$$

**d. Comfort Plus has the better occupancy rate at 82% of capacity, compared to Connors' occupancy rate of 78%.**

**MAD 1–30**

**a. The occupancy change is unfavorable for Hilton Hotels. Occupancy for Hilton decreased from 75.7% to 40.3%, or a 35.4 percentage point decrease over the year.**

**b. The occupancy change is unfavorable for Marriott International. Occupancy for Marriott decreased from 73.7% to 31.4%, or a 42.3 percentage point decrease over the year.**

**c. Hilton Hotels has a better occupancy rate than Marriott International for the two years provided. This can be perceived both by the occupancy percentage comparisons for each year (75.7% vs. 73.7% in 2019 and 40.3% vs. 31.4% in 2020) and by the slightly smaller decrease in occupancy for the year (35.4 percentage points for Hilton vs. 42.3 percentage points for Marriott).**


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**MAD 1–30 (Concluded)**

**d. An important question beyond occupancy is the price at which the rooms are sold. Price will influence occupancy. For example, it is possible to increase occupancy by reducing price. However, a reduced price may reduce revenue by more than the revenue increase achieved by increased occupancy. Thus, hotels also need to monitor the average daily price for which room nights are sold.**

***Note:*** **In this case, Hilton Hotels had an average room price of $114.03 in 2020 (down from $144.79 in 2019), while Marriott had an average room price of $151.51 in 2020 (down from $182.60 in 2019). Thus, while both hotels saw a decrease in price, and while Marriott had a lower occupancy rate, Marriott made more revenue per room night in 2020 than did Hilton. Thus, Marriott's overall performance appears more favorable than what could be determined by just the occupancy data.**

**Further, understanding the long-term impact of pandemic-related demand at Hilton and Marriott is important. For example, it is important to investigate how travel was affected in the areas served by Hilton and Marriott, and how sanitation changes at these hotels could influence future demand.**

**MAD 1–31**

**a.**

| | Number of Guests | | Average Length of Visit (in Nights) | | Guest Nights (Number of Guests × Average Length of Visit) |
|---|---|---|---|---|---|
| Sunrise Suites | 183,600 | × | 1.5 | = | 275,400 |
| Nationwide Inns | 228,000 | × | 1.2 | = | 273,600 |

**b.**

| | Number of Hotels | | Average Number of Rooms per Hotel | | Days in June | | Room Nights for June |
|---|---|---|---|---|---|---|---|
| Sunrise Suites | 120 | × | 90 | × | 30 | = | 324,000 |
| Nationwide Inns | 150 | × | 76 | × | 30 | = | 342,000 |

**c.** $$\text{Occupancy Rate} = \frac{\text{Guest Nights}}{\text{Available Room Nights}}$$

$$\text{Sunrise Suites: } \frac{275{,}400}{324{,}000} = 85\%$$

$$\text{Nationwide Inns: } \frac{273{,}600}{342{,}000} = 80\%$$

**d. Sunrise Suites had the better occupancy rate during June, with 85% compared to Nationwide Inns' occupancy rate of 80%. Additional analyses should evaluate the average price per room, since price can influence the occupancy rate and there can be a trade-off between average room price and occupancy.**



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**MAD 1–32**

**a.**

| | April | May | June |
|---|---|---|---|
| Admitted patients | 1,440 | 1,860 | 2,250 |
| Average length of stay per patient | × 4.0 | × 3.5 | × 3.0 |
| In-patient days | 5,760 | 6,510 | 6,750 |

**b.** Available beds:

| | Private | Semi-Private | Total |
|---|---|---|---|
| Number of rooms | 100 | 100 | |
| Beds per room | × 1 | × 2 | |
| Total bed capacity | 100 | 200 | 300 |

Available bed days:

| | April | May | June |
|---|---|---|---|
| Bed capacity | 300 | 300 | 300 |
| Days per month | × 30 | × 31 | × 30 |
| Available bed days | 9,000 | 9,300 | 9,000 |

**c.** Occupancy rate:

| | April | May | June |
|---|---|---|---|
| In-patient days [from (a)] | 5,760 | 6,510 | 6,750 |
| Available bed days [from (b)] | ÷ 9,000 | ÷ 9,300 | ÷ 9,000 |
| Occupancy rate | 64% | 70% | 75% |

**d.** The occupancy rate increased from April to May and again from May to June. This suggests the hospital bed capacity is being utilized more efficiently over time. A closer examination of the data reveals that the average length of stay is declining, while the number of admissions is increasing. The average length of stay may be declining due to greater efficiency in delivering health care, assuming no change in treatment mix is being provided over the three months. This potential improvement provides greater capacity to accept new patients, as can be perceived from the three-month data. Thus, the reduced length of stay and greater occupancy are both contributing to the hospital's ability to serve more patients per month.



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**MAD 1–33**

**a. Available seat capacity for each flight number for June:**

| | |
|---|---|
| Number of seats per flight | 180 |
| Number of flights in June (one per day) | × 30 |
| Total seat capacity per flight number (June) | 5,400 |

**b.**

| Flight Number | Number of Seats Sold | Available Seat Capacity [from (a)] | Passenger Load* |
|---|---|---|---|
| 57 | 5,130 | 5,400 | 95% |
| 85 | 2,592 | 5,400 | 48% |
| 94 | 2,376 | 5,400 | 44% |

*** Number of seats sold ÷ Available seat capacity**

**c. The passenger load information indicates that Flight 57 flies very near to capacity, but Flights 85 and 94 fly at less than half of capacity. This suggests the management of Eastern Skies is offering too much capacity for the morning flights to Chicago. One solution would be to use smaller aircraft for Flights 85 and 94 so as to better match capacity with demand. Alternatively, Eastern could consolidate the two flights into one flight that could depart at some time between the two original times, such as 10:45 AM. Passengers could then migrate to the new flight, resulting in a better utilization of the remaining flight.**



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## TAKE IT FURTHER

**TIF 1–34**

**Brian has behaved unethically and violated several of the IMA's principles of ethical conduct. By determining the price of the lumber that he is buying, Brian has created a conflict-of-interest situation that violates the principle of objectivity. For professionals to be objective, they must make decisions that are not influenced by their personal feelings or result in personal gains. Since Brian is in a position to directly influence the price that he will pay for the lumber, he cannot be objective. Thus, although it is appropriate for Brian to take advantage of Avett's policy of allowing employees to purchase materials at cost, he should have had someone else (such as his supervisor) determine the amount that he owed for the lumber. Clearly, selecting the lowest price has opened the door for criticism.**

**TIF 1–35**

**Answers may vary slightly by restaurant chosen. A suggested answer for a pizza restaurant follows:**

| Cost | Direct Materials | Direct Labor | Overhead | Selling Expenses |
|---|---|---|---|---|
| Ingredients | X | | | |
| Cook wages | | X | | |
| Manager salary | | | X | |
| Depreciation on equipment and fixtures | | | X | |
| Coupon costs | | | | X |
| Advertising | | | | X |
| To-go boxes | X | | | |
| Disposable plates, utensils, cups | X | | | |
| Nondisposable plates, utensils, cups | | | X | |
| Repair costs | | | X | |
| Property taxes | | | X | |
| Store depreciation | | | X | |
| Cashier salary | | | X | |
| Beverages | X | | | |
| Building heat and A/C | | | X | |
| Salad ingredients | X | | | |
| Delivery person wages | | X | | |
| Power costs for ovens | | | X | |

**In service businesses, the distinction between direct labor and overhead will not always be clear.**



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**TIF 1–36**

**Memo**

**To:** **Todd Johnson**

**From:** **A+ Student**

**Re:** **Financial vs. Managerial Accounting Information**

**The objectives of financial and managerial accounting are quite different, and your statement does not fully consider these differences. In one sense, your statement may be appropriate at high levels in the organization. For example, it is appropriate to evaluate a division manager who is responsible for the overall performance of a division using the same financial performance measures that shareholders use to evaluate the company. However, these measures are not appropriate for evaluating managerial decision-making below the division level. At these levels, summary financial performance measures do not provide the relevant information needed to direct and control the company's operations. Operational performance measures need to focus on measuring cost, quality, delivery time, equipment availability, inventory levels, scrap, waste, and efficiency. This list is much broader and more detailed than the financial statement numbers provided to the stockholders.**

**The stockholders' interest in profit is related to increasing shareholder value. Managers must increase long-term shareholder value by engaging in strategies that enhance people, product, and processes in the delivery of value to customers. These strategies can be measured by both financial and nonfinancial means. Therefore, managerial accounting information needs a much broader set of objective and subjective measures used internally in the organization to guide strategy and operations.**



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**TIF 1–37**

**a. The vice president of the Information Systems Division can use managerial accounting information in a number of ways. For example, the vice president might use these data to determine resources that will be needed based on a projection of the amount and type of work required for the next period. Managerial accounting information would also be used to determine whether the bank should lease additional processing capacity or purchase a new central processing unit. In addition, managerial accounting information could be used to achieve better control over information systems activities by evaluating the costs of ongoing operations, based on the demand for information services.**

**b. The hospital administrator can use managerial accounting information in a number of ways. One way is for cost planning and control. The administrator could use managerial information to keep costs commensurate with services provided and to plan for staffing and nursing levels. This information can be used to determine the cost of various services and, thereby, in making decisions with respect to the amount of service that is appropriate in each case. The administrator can also use managerial accounting information to determine whether the hospital's costs are being covered by fixed payments from Medicare, Medicaid, or insurance. If not, the administrator needs to know the source of the cost overruns. Does the hospital allow too many procedures? Require longer bed days? Have resources that are underutilized (e.g., a cancer wing with three patients)?**

**c. The CEO of the food company will use managerial accounting information to support the control of the three divisions. Each of the three divisions will be subject to a number of financial goals. The CEO also needs to support strategic decision-making. In this regard, the CEO needs managerial accounting information on the profitability of various product families, profitability of different regions, and profitability of various customer segments. This information can guide the CEO in allocating future effort and resources.**

**d. The copy shop manager needs fairly simple managerial accounting information. At the most basic level, the copy shop manager needs to know the costs of performing various copy tasks, such as one-sided copy, two-sided copy, collating, and binding. These activities will have some direct costs, such as paper, and some indirect costs, such as copy machine time. The manager will need to estimate the impact of both of these costs in order to price the various copy jobs to the public. Managerial accounting information will include the cost details necessary to price the various copy shop services at a level needed to cover equipment costs, lease expenses, and profit.**



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**TIF 1–38**

**a. The High Times manager will use managerial accounting information to accumulate the costs associated with different menu items. The costs, direct and indirect, will help in determining the pricing strategy.**

**b. The plant manager is going to use cost information on scrap and rework to identify the amount of waste occurring in the plant. This measure of waste is fairly common in fabrication-type facilities. The measures can guide the plant manager to locations or products where significant waste is occurring. The plant manager can use the scrap and rework measures to guide operational improvement toward the location that is experiencing the greatest level of scrap or rework. The measures can also monitor improvement in rework and control the number of network hours charged by floor personnel.**

**c. The cost of ending inventory must be determined as financial statements are prepared. The division controller will likely require inventory valuation at the close of every month in order to have a good understanding of the month-by-month earnings of the division. The division controller will provide the ending inventory information by using managerial accounting information in determining the cost of products. To determine the appropriate cost, the product cost is multiplied by the units left in inventory.**

**d. The Maintenance Department manager needs to be able to plan the resources used by his department. The planning process involves identifying the required resources to fulfill the department's objective(s). For example, the Maintenance Department manager may know the repair histories of various machines. These histories can be used to forecast the repairs anticipated during the next year. The manager may also know that a new process will be brought online during the next year. New processes are frequently troublesome, so the manager will need to budget additional resources to accommodate introduction of the new technology.**



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**TIF 1–39**

**1. Obie's bill has a number of points that should be considered. Some of the points, with the appropriate argument, are identified below.**

- **The trip back to the shop resulted in an $80 labor charge. Obie should argue that the whole hour should not be billed. The hour is the result of stocking out of a circuit board on the truck. The circuit board should have been with the repair person. There was a board for the previous customer. However, since only one was stocked, the repair person had to go back to the shop. The trip back to the shop was nonproductive time that should not have been charged directly to Obie but should be part of Geek Gang's overhead cost to all customers. In other words, Obie should not be responsible for this mistake.**
- **The overtime premium should not have been charged to Obie. What if Obie was the first appointment in the morning? If he was, there would be no overtime premium. It's only random misfortune that Obie was the last client of the day and therefore received the overtime premium. Add to this the fact that the overtime would not have been necessary without the trip back to the shop, and the conclusion is that Obie should not be charged directly for overtime. The overtime premium should be part of Geek Gang's overhead charged to all clients equally. Obie should be charged the overtime only if the decision for overtime was caused by or required by Obie.**

**Thus, the labor portion of the bill should only be $70 + $60 + $60 = $190.**

**There are other parts of the bill that should not be in dispute.**

- **The materials storage and handling charge is a normal charge of maintaining a parts inventory for the benefit of clients that need parts.**
- **The fringe benefits and overhead added to the hourly rate are both reasonable. The fringe benefit attaches directly to the direct labor. Fringe benefits are just another form of compensation. The overhead must be covered by all customers. Therefore, including overhead in the hourly rate is the most logical method of covering these costs.**
- **The additional charge for the first hour is also reasonable. The first hour charge covers the costs of transit, which are directly attributable to making a home visit. Obie requires a home visit, so Obie should be responsible for the costs of making the visit. If Obie brought the computer to the shop, this cost would not be incurred.**


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**TIF 1–39 (Concluded)**

| 2. Cost | Direct Materials | Direct Labor | Overhead |
|---|---|---|---|
| Circuit board | X | | |
| Storage and handling | | | X |
| Straight-time labor | | X | |
| Fringe benefits* | | X | |
| Overhead | | | X |
| Vehicle depreciation and fuel | | | X |
| Overtime premium | | | X |

* Could be considered overhead.

**TIF 1–40**

1. If the hourly professional rate is set based, in part, on the desire to cover indirect costs, the rate will be higher than if it is only based on the direct costs of professionals. However, Larson & Company needs to set its rates high enough to cover all of its costs and generate a profit.
2. If some clients use more supplies than others, the current billing system will not accurately reflect the fact that these clients are slightly more costly for Larson & Company to serve. However, given the overall cost of providing CPA services to clients, costs relating to office supplies, even for clients who require an above-average level of supplies, are insignificant.
3. While employees at Larson & Company could exert the effort necessary to directly trace the costs of office supplies to each client, the cost of doing so would outweigh the benefit. In addition, even clients who use very few supplies would likely be turned off by being "nickeled and dimed" with charges for print jobs, faxes, and other office supply costs. In the end, just because a cost can be directly traced to a cost object, that doesn't mean a cost should be directly traced to a cost object.



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**TIF 1–41**

**Excel**

**Cost Classifications**

| Row Labels | Sum of Charge Amount |
|---|---|
| **Period Cost** | **$1,047,203.00** |
| **Administrative Expenses** | **$1,021,968.00** |
| Administrative Wages | $225,945.00 |
| External Auditor Fees | $42,256.00 |
| Management Salaries | $753,767.00 |
| **Selling Expenses** | **$25,235.00** |
| Advertising | $25,235.00 |
| **Product Cost** | **$5,510,935.00** |
| **Direct Labor Costs** | **$1,685,285.00** |
| Manufacturing Employee Wages | $1,685,285.00 |
| **Direct Materials Cost** | **$2,107,857.00** |
| Freight | $102,577.00 |
| Raw Materials, Steel | $1,452,127.00 |
| Raw Materials, Vinyl Compound | $553,153.00 |
| **Manufacturing Overhead Costs** | **$1,717,793.00** |
| Electricity | $671,121.00 |
| Factory Equipment Depreciation | $357,125.00 |
| Packaging Materials | $449,915.00 |
| Warehouse Lease | $239,632.00 |
| **Grand Total** | **$6,558,138.00** |

**Tableau**

**Cost Classifications**

| Product | Costs | Charge Type | |
|---|---|---|---|
| Period Costs | Administrative Expenses | Administrative Wages | $ 225,945.00 |
| | | External Auditor Fees | 42,256.00 |
| | | Management Salaries | 753,767.00 |
| | | Total | $1,021,968.00 |
| | Selling Expenses | Advertising | $ 25,235.00 |
| | | Total | $ 25,235.00 |
| | Total | | $1,047,203.00 |
| Product Costs | Direct Labor Costs | Manufacturing Employees | $1,685,285.00 |
| | | Total | $1,685,285.00 |
| | Direct Materials Costs | Freight | $ 102,577.00 |
| | | Raw Materials, Steel | 1,452,127.00 |
| | | Raw Materials, Vinyl | 553,153.00 |
| | | Total | $2,107,857.00 |
| | Manufacturing Overhead Costs | Electricity | $ 671,121.00 |
| | | Factory Equipment | 357,125.00 |
| | | Packaging Materials | 449,915.00 |
| | | Warehouse Lease | 239,632.00 |
| | | Total | $1,717,793.00 |
| | Total | | $5,510,935.00 |



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# CERTIFIED MANAGEMENT ACCOUNTANT (CMA®) EXAMINATION QUESTIONS (ADAPTED)

**CMA 1–42**

**b. Sales commissions on cars would be part of the selling expense for the car dealership, not a manufacturing cost. Options (a) and (d) are direct material costs, while option (c) would be charged to manufacturing overhead.**

**CMA 1–43**

**c. Plunkett's product costs are $656,100, and the period costs are $493,000, as follows:**

| | Product Costs |
|---|---|
| Direct materials | $ 56,000 |
| Direct labor | 179,100 |
| Overhead | 421,000 |
| Total | $656,100 |

| | Period Costs |
|---|---|
| Selling expenses | $235,900 |
| Administrative expenses | 229,400 |
| Fire loss | 27,700 |
| Total | $493,000 |

**CMA 1–44**

**c. Prime costs of $150,000 are the combination of direct material costs of $100,000 and direct labor costs of $50,000. Conversion costs of $130,000 are the combination of direct labor costs of $50,000 and overhead costs of $80,000.**

**CMA 1–45**

**c. Manufacturing overhead includes those items that cannot be directly traced to any one particular product and/or is an insignificant part of the total cost. In this case, the wood screws and glue used in the production of school desks and chairs would most likely be classified as manufacturing overhead.**



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# Instructor Manual

Warren/Jones/Tayler, Managerial Accounting for Business Leaders, 2026, 9798214042169; Chapter 1, Introduction to Managerial Accounting

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## Purpose and Perspective of the Chapter

The purpose of Chapter 1 is to introduce students to managerial accounting and how it differs from financial accounting. Managerial accounting provides information to internal users. Managers use this information to plan, measure, evaluate, and control the performance of the business. Managerial accounting information includes historical data to evaluate performance and estimated data to assist in making future decisions. Financial accounting is reported at fixed intervals and provides information to assist external users in making decisions. These external users include shareholders, creditors, government agencies, and the general public.

Students will also learn how managerial accounting relates to manufacturing and service businesses. Within manufacturing, costs can be divided into three categories: direct materials, direct labor, and manufacturing overhead. Direct costs can be directly connected to a specific cost object, while indirect costs are those that cannot be traced conveniently to a cost object. Costs other than direct materials and direct labor that are incurred in the manufacturing process are classified as manufacturing overhead cost. Costs can be divided into product and period costs. Product costs consist of manufacturing costs, direct materials, direct labor, and manufacturing overhead. Period costs are selling and administrative costs.

Financial statements for manufacturing entities are somewhat more complex than for merchandising or service businesses. For example, manufacturers have three inventory accounts on their balance sheets for raw materials, work in process, and finished goods. These inventories are reported, along with the costs of production, in a cost of goods manufactured statement. This information is used to determine the cost of goods sold on the income statement.

Finally, service businesses look at utilization rates to measure the use of fixed assets in serving customers. Examples are provided of service industries and businesses, and differences are explained between the use of managerial accounting in manufacturing and service entities.

## Chapter Objectives

The following objectives are addressed in this chapter:

Obj. 1 Describe how managerial accounting supports the management process, its differences with financial accounting, and its place within the organization.

Obj. 2 Describe the nature of manufacturing operations, including different types and classifications of costs.

Obj. 3 Describe financial statements for a manufacturing business, including the balance sheet, statement of cost of goods manufactured, and income statement.

Obj. 4 Compute utilization rates in evaluating the performance of service companies.

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## Complete List of Chapter Activities and Assessments

The following table organizes activities and assessments by objective, so that you can see how all this content relates to objectives and make decisions about which content you would like to emphasize in your class based on your objectives. For additional guidance, refer to the Teaching Online Guide.

| Chapter Objective | Activity/Assessment | Source (i.e., PPT slide, Workbook) |
|---|---|---|
| Obj. 1 | Discussion Activity 1 | PPT Slides 11–12 |
| Obj. 2 | Knowledge Check Activity 1 | PPT Slides 20–21 |
| Obj. 2 | Knowledge Check Activity 2 | PPT Slides 25–26 |
| Obj. 3 | Knowledge Check Activity 3 | PPT Slides 34–35 |
| Obj. 4 | Discussion Activity 2 | PPT Slides 40–41 |

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## Key Terms

**Chief accounting officer (CAO):** A vice president of accounting who reports to the CFO and oversees technical accounting, accounting policy, credit, collections, tax, treasury, and internal audit functions.

**Chief executive officer (CEO):** The highest-ranking person in a company.

**Chief financial officer (CFO):** An executive vice president responsible for overseeing the financial activities of an entire company.

**Control:** The process by which management takes actions to encourage specific behaviors or outcomes.

**Controller:** The manager of the accounting function of a vertical (business unit).

**Conversion costs:** The combination of direct labor and manufacturing overhead costs.

**Cost:** A sacrifice made to obtain some benefit.

**Cost object:** A product, sales territory, department, or activity to which costs are assigned, depending on the decision-making needs of management.

**Cost of goods manufactured:** The total cost of making and finishing a product.

**Cost of goods sold:** The cost of merchandise sold recognized as an expense; the cost of finished goods available for sale minus the ending finished goods inventory.

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**Data analytics:** The science of analyzing large amounts of raw data, sometimes called "big data," to discover patterns, identify anomalies, or gain other useful insights for decision-making.

**Direct costs:** Costs that are identified with and traced to a cost object.

**Direct labor cost:** The wages of factory workers who are directly involved in converting materials into a finished product.

**Direct materials cost:** The cost of materials that are an integral part of the finished product.

**Evaluation:** The management process by which management monitors operations by comparing actual and expected results.

**Factory burden:** Costs, other than direct materials and direct labor costs, that are incurred in the manufacturing process. Also called *manufacturing overhead cost*, *factory overhead*, or simply *overhead*.

**Factory overhead:** Costs, other than direct materials and direct labor costs, that are incurred in the manufacturing process. Also called *manufacturing overhead cost*, *factory burden*, or simply *overhead*.

**Financial accounting:** The branch of accounting that is concerned with recording transactions using generally accepted accounting principles (GAAP) for a business or other economic unit and with a periodic preparation of various statements from such records.

**Finished goods inventory:** The direct materials costs, direct labor costs, and manufacturing overhead costs of finished products that have not been sold.

**Horizontals:** Departments within a company that do not develop products but provide services to the various verticals and other horizontals.

**Indirect costs:** Costs that are not identified with or traced to a cost object.

**Indirect labor:** Labor costs that are not directly traced to the finished product; any labor needed to make a product that is not directly traced to the product.

**Indirect materials:** Materials costs that are not directly traced to the finished product; any materials needed to make a product that are not directly traced to the product.

**Management accounting:** The branch of accounting that uses both historical and estimated data in providing information that management uses in conducting daily operations, in planning future operations, and in developing overall business strategies. Also called *managerial accounting*.

**Management by exception:** The philosophy of focusing evaluation on "unexpected" good or bad performance.

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**Management process:** The four basic management functions of (1) strategic planning, (2) measurement, (3) evaluation, and (4) control.

**Managerial accounting:** The branch of accounting that uses both historical and estimated data in providing information that management uses in conducting daily operations, in planning future operations, and in developing overall business strategies. Also called *management accounting*.

**Manufacturing overhead cost:** Costs, other than direct materials and direct labor costs, that are incurred in the manufacturing process. Also called *factory overhead*, *factory burden*, or simply *overhead*.

**Materials inventory:** The cost of materials that have not yet entered into the manufacturing process.

**Measurement:** The management process where managers develop and agree upon performance metrics on how well the company is achieving its objectives.

**Operational planning:** Developing short-term actions for managing the day-to-day operations of a company.

**Overhead:** Costs, other than direct materials and direct labor costs, that are incurred in the manufacturing process. Also called *manufacturing overhead cost*, *factory overhead*, or *factory burden*.

**Period costs:** Selling and administrative expenses incurred in marketing the product, delivering the product, or managing the company and not directly related to manufacturing the product.

**Prime costs:** The combination of direct materials and direct labor costs.

**Product costs:** The three components of manufacturing cost: direct materials, direct labor, and manufacturing overhead costs.

**Statement of cost of goods manufactured:** A statement prepared by manufacturing companies that summarizes the cost of goods manufactured during the period.

**Strategic planning:** Developing long-term actions to achieve a company's objectives.

**Utilization rate:** A measure of the use of a fixed asset in serving customers relative to the asset's capacity.

**Verticals:** Business units often structured as separate businesses within a parent company that develop products sold directly to consumers.

**Work in process inventory:** The direct materials costs, the direct labor costs, and the applied manufacturing overhead costs that have entered into the manufacturing process but are associated with products that have not been finished.

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## CHAPTER OUTLINE

The following outline organizes activities (including any existing discussion questions in PowerPoints or other supplements) and assessments by chapter (and therefore by topic), so that you can see how all the content relates to the topics covered in the text.

I. Managerial Accounting (1-1, PPT Slides 3–12, BUSPROG: Analytic, AICPA: FN-Measurement)

a. Managerial accounting, sometimes called management accounting, is the process of developing information and management tools to achieve an organization's objectives.
b. The management process is composed of the following four basic functions:
   - Strategic planning
   - Measurement
   - Evaluation
   - Control
c. Strategic planning is where the management process begins to develop long-term objectives and normally involves a time horizon of five to ten years.
d. Operational planning develops short-term actions for managing the day-to-day operations of the company.
e. Measurement is the process where managers develop and agree upon performance metrics on how well the company is achieving its objectives.
f. Evaluation is the process by which management monitors operations by comparing actual and expected results.
g. Control is the process by which management takes actions to encourage specific behaviors or outcomes.
h. Exhibit 1 (PPT Slide 5) provides the managerial accounting schema that describes the primary roles of managerial accounting.
i. Considerations and choices in developing costing information include:
   i. What cost system to use to record and report the cost of a product
   ii. How to allocate overhead costs, such as equipment depreciation, to products
   iii. How to allocate support department costs, such as factory janitorial costs, to products
   iv. How to allocate joint manufacturing costs to products
   v. How to report fixed production costs, such as factory supervisory salaries
   vi. How to determine and report variances (differences) between actual and planned costs
j. Managerial accounting develops a variety of tools for management to use in analyzing information and making decisions, including:
   - Cost-volume-profit analysis for determining the sales necessary to break even or earn a target profit

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- Budgeting for resource planning
- Decentralization for assessing operations that are centralized or distributed throughout the company
- Differential analysis for comparing the profitability of various options
- Capital investment analysis for use in deciding among long-term assets to purchase

k. Exhibit 2 (PPT Slide 8) shows the differences between financial accounting and managerial accounting.

l. Most large companies are organized in terms of "verticals" and "horizontals."

i. Verticals are sometimes referred to as business units, since they are often structured as separate businesses within the parent company. Verticals develop products that are sold directly to customers.

ii. Horizontals are departments within the company that are not responsible for developing products. Horizontals provide services to the various verticals and other horizontals.

m. Exhibit 3 (PPT Slide 10) shows a partial organization chart for McAfee.

n. **Discussion Activity 1:** *What do you think of the role of managerial accounting in manufacturing and service industries? In groups of three to four students, select an industry, such as airlines, telecommunications, health care, smartphone manufacturers, pharmaceuticals, among others. Discuss how using managerial accounting techniques can directly benefit the specific industry chosen. Select a spokesperson from your group to share your findings with the class.* (PPT Slides 11–12)

- No matter the industry chosen, the managerial accounting toolbox can be very helpful in decision-making. For example, airlines want to know how many passengers are needed for individual flights to be profitable, and they often cancel or add flights based on these analyses. In a manufacturing environment, factories will adjust their production based on the budgeted sales and the break-even sales required to cover their costs.
- With all the needs of businesses in various industries, there will be a robust discussion of how managerial accounting can help with significant management decisions.

II. Manufacturing Operations (1-2, PPT Slides 13–26, BUSPROG: Analytic, AICPA: FN-Measurement)

a. The operations of a business can be classified as service, merchandising, or manufacturing. Most of the managerial accounting concepts that apply to manufacturing businesses also apply to service and merchandising businesses.

b. As a basis for illustration of manufacturing operations, a guitar manufacturer, Legend Guitars, is used in this chapter.

c. Exhibit 4 (PPT Slide 13) illustrates the guitar-making operations of Legend Guitars.

d. A cost is a sacrifice made to obtain some benefit and, in managerial accounting, costs are often assigned to a cost object.

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e. A cost object can be anything to which costs are assigned and will vary depending upon the decision-making needs of management.
f. Direct costs are identified with and can be traced to a cost object.
g. Indirect costs are not identified with or traced to a cost object.
h. Exhibit 5 (PPT Slide 14) shows the direct costs at Legend Guitars, and Exhibit 6 (PPT Slide 14) shows Legend Guitars' indirect costs.
i. Exhibit 7 (PPT Slide 15) shows how costs are classified as direct and indirect at Legend Guitars.
j. Exhibit 8 (PPT Slide 16) shows the three manufacturing costs of Legend Guitars: direct materials, direct labor, and manufacturing overhead.
k. Manufactured products begin with raw materials that are converted into finished products.
l. To be classified as a direct materials cost, the cost must be both of the following:
    - An integral part of the finished product
    - A significant portion of the total cost of the product
m. Examples of direct materials costs include the following:
    - The cost of the wood used in producing a guitar
    - The cost of electronic components for a television
    - Silicon wafers for microcomputer chips
    - Tires for an automobile
n. Most manufacturing processes use employees to convert materials into finished products.
o. The cost of employee wages that is an integral part of the finished product is classified as direct labor cost.
p. A direct labor cost must meet both of the following criteria:
    - An integral part of the finished product
    - A significant portion of the total cost of the product
q. Examples of direct labor costs include the following:
    - The wages of employees who cut guitars out of raw lumber and assemble them
    - Mechanics' wages for repairing an automobile
    - Assemblers' wages for assembling a laptop computer
r. Costs other than direct materials and direct labor that are incurred in the manufacturing process are combined and classified as manufacturing overhead cost (sometimes called factory burden or factory overhead).
s. All manufacturing overhead costs are indirect costs of the product.
t. Some manufacturing overhead costs include the following:
    - Heating and lighting the factory
    - Repairing and maintaining factory equipment
    - Property taxes on factory buildings and land
    - Insurance on factory buildings
    - Depreciation of factory plant and equipment
u. **Knowledge Check Activity 1:** *For a manufacturer, which of the following would be considered a manufacturing overhead cost?* (PPT Slides 20–21)
    - The answer is electricity costs in a furniture manufacturing facility.

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- Costs other than direct materials cost and direct labor that are incurred in the manufacturing process, such as electricity costs, are considered manufacturing overhead costs.

v. Exhibit 9 (PPT Slide 22) illustrates the prime costs and conversion costs at Legend Guitars.
w. Exhibit 10 (PPT Slide 23) shows examples of product costs and period costs at Legend Guitars.
x. Exhibit 11 (PPT Slide 24) shows a flowchart of product costs, period costs, and financial statements.
y. **Knowledge Check Activity 2:** *Which of the following would be considered a period cost?* (PPT Slides 25–26)
   - The answer is sales manager's salary.
   - Any cost that is incurred in the factory or manufacturing process is a product cost. The sales manager's salary would be an administrative cost, which is considered a period cost.

III. Financial Statements for a Manufacturing Business (1-3, PPT Slides 27–35, BUSPROG: Analytic, AICPA: FN-Measurement)

a. The statement of stockholders' equity and statement of cash flows for a manufacturing business are similar to those for service and merchandising businesses.
b. However, the balance sheet and income statement for a manufacturing business are more complex.
c. This is because a manufacturer makes the products that it sells and, thus, must record and report product costs.
d. The reporting of product costs primarily affects the balance sheet and the income statement.
e. A manufacturing business reports three types of inventory on its balance sheet as follows:
   i. Materials inventory (sometimes called raw materials inventory) consists of the costs of the direct and indirect materials that have not yet entered the manufacturing process.
   ii. Work in process inventory consists of the direct materials, direct labor, and manufacturing overhead costs for products that have entered the manufacturing process but are not yet completed (in process).
   iii. Finished goods inventory consists of completed (or finished) products that have not been sold.
f. Exhibit 12 (PPT Slide 29) shows a balance sheet presentation of inventory in merchandising and manufacturing companies.
g. Exhibit 13 (PPT Slide 30) shows income statements for merchandising and manufacturing businesses.
h. A merchandising business determines its cost of goods sold by first adding its net purchases for the period to its beginning inventory.
i. This determines inventory available for sale during the period. The ending inventory is then subtracted to determine the cost of goods sold.
j. A manufacturing business makes the products it sells using direct materials, direct labor, and manufacturing overhead.

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- A manufacturing business must determine its cost of goods manufactured during the period.
- The cost of goods manufactured is determined by preparing a statement of cost of goods manufactured.

k. Exhibit 14 (PPT Slide 32) shows a manufacturing company's income statement with a statement of cost of goods manufactured.

l. Exhibit 15 (PPT Slide 33) illustrates the flow of manufacturing costs.

m. **Knowledge Check Activity 3:** *Which of the following is calculated for both a manufacturer and a merchandising business?* (PPT Slides 34–35)

- The answer is cost of goods sold.
- Both a manufacturer and a merchandising business would need to calculate their cost of goods sold to report on the income statement. Only a manufacturer would need to calculate the ending balances of raw materials and work in process inventories, as well as create a statement of cost of goods manufactured.

IV. Analysis for Decision-Making: Utilization Rates (1-4, PPT Slides 36–41, BUSPROG: Analytic, AICPA: FN-Measurement)

a. A utilization rate measures the use of a fixed asset in serving customers relative to the asset's capacity.

b. A higher utilization rate is considered favorable, while a lower utilization rate is considered unfavorable.

c. Different service industries will have different names and computations used for measuring utilization rates.

d. In the hotel industry, for example, utilization is measured by the occupancy rate, which is computed as:

- Occupancy Rate = Guest Nights/Available Room Nights
- Guest Nights = Number of Guests × Number of Nights per Visit (per time period)
- Available Room Nights = Number of Available Rooms × Number of Nights per Time Period

e. Exhibit 16 (PPT Slide 37) lists examples of service industries, services, and companies.

f. Exhibit 17 (PPT Slides 38–39) lists managerial accounting differences between manufacturing and service companies.

g. **Discussion Activity 2:** *Service businesses often have a unique item that can be used as a utilization rate, such as the example of guest nights in the hotel industry. In groups of three to four students, think about service businesses and what they may use for a possible utilization rate. Consider transportation, shipping, banking, and repair service industries, among others. Share your findings with your class.* (PPT Slides 40–41)

- Students likely found many examples in service businesses and possible utilizations rates. For example, companies such as FedEx and UPS may use a rate per mile on their delivery truck and airplanes. Auto repair facilities may use specific machinery that reflects the costs associated with services, such as a machine used for front-end alignments.
- Businesses continue to rely on fixed assets and technological advancements to lower costs and provide services.

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## Additional Discussion Questions

The following are discussion questions that do not appear in the text, PPTs, or courseware – they are for you to use as you wish. You can assign these questions several ways: in a discussion forum in your LMS; as whole-class discussions in person; or as a partner or group activity in class.

1. Discussion: Managerial Accounting Tools (Managerial Accounting, 1-1, PPT Slide 7) Duration 10 minutes.
    a. What are some of the more popular managerial accounting tools, and how do they help management in decision-making?
        i. Answer: One of the more popular managerial accounting tools is cost-volume-profit analysis, which is also known as break-even. It is important for both manufacturers and service businesses to know how many products or services they must sell to cover their costs. Once that amount is determined, they know they will be attaining profit. Without knowing the break-even point, businesses are not able to ascertain when they will be profitable. Another popular tool is budgeting. In addition to planning for revenues, control of expenses is a very important part of managing a business. Budgets provide a roadmap of likely scenarios that can be used to communicate a company's goals throughout an organization. They can also be used to determine why the goals were not met. A budget provides a "blueprint" of goals for a company to attain, and it is more likely to be successful if it is carefully planned by multiple levels of management and employee input.
2. Discussion: Difference Between Direct and Indirect Costs (Manufacturing Operations, 1-2, PPT Slide 14) Duration 10 minutes.
    a. What is the difference between direct and indirect costs, and why are they kept separate?
        i. Answer: Direct costs can be traced to a specific object or task. For example, when manufacturing products, a part that is identifiable, such as a tire on an automobile, is easily traced to each car that is produced. These costs can be tracked with a specific quantity known for each product. Essentially, direct costs are easier to "see" and know the specific costs per item produced. Indirect costs are much more challenging to identify per product. Items such as factory rent, indirect labor from factory supervisors, or depreciation on machinery cannot easily be traced to each individual product made. For example, heating or cooling a production facility will depend on outdoor temperature changes, thus energy costs cannot be easily traced to individual products. Likewise, the production supervisors' salaries will remain the same regardless of how many products were actually made within a specific time

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period. Of course, indirect costs must be tracked as well, to determine the overall cost of goods manufactured.

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## ADDITIONAL RESOURCES

The following are activities and assignments developed by Cengage but not included in the text, PPTs, or courseware – they are for you to use if you wish.

1. **Writing Exercise:** *Violating GAAP* (Analytic, Critical Thinking, 1-1, PPT Slides 4–8) Duration 15 minutes.
    a. Instruct students to write an answer to the following question: Why is it permissible to violate generally accepted accounting principles (GAAP) when preparing reports used strictly by company management?
        i. Answer: Since these reports are for internal use only, they do not provide any influence to investors about decisions to invest in the company. These reports are for management to aid in the decision-making process. It should be clear to all users that these reports may not follow GAAP.
2. **Internet Activity:** *Becoming a Certified Management Accountant* (Analytic, Critical Thinking, 1-1, PPT Slides 3–12) Duration 15 minutes.
    a. Go online to the Institute of Certified Management Accountants' website: imanet.org. Click on Certifications and then the CMA Overview. In groups of 3–4 students, look at the data listed on the webpage, including exam content, exam pass rates, qualifications to take the exam, and any other valuable information that you can share with the class. Would you consider pursuing this certification? If so, state your reasons.
        i. Answer: Students will find various statistics and other information on the webpage, including pass rates, specific topic areas tested on the exam, the number of CMAs worldwide, and perhaps some videos of success stories for CMA certification holders. Encourage students to consider this specialty area in accounting, especially if they prefer a corporate environment or have entrepreneurial aspirations.

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