Chapter 18

Introduction to Managerial Accounting

## Chapter Overview

Chapter 18 introduces students to managerial accounting, as distinguished from financial accounting. Students learn about the information that managers—the decision-makers inside the business—must know and use in order to effectively plan and control the business.

The chapter then begins a discussion on today’s business environment. Recent trends include a shift toward a service economy, competing in the global marketplace, timed-based competition, advanced information systems, e-commerce, just-in-time management, and the total quality movement.

The chapter continues with a discussion of the professional ethical standards for management accountants and provides an ethical dilemma that can be used for discussion purposes. Service, merchandising, and manufacturing companies are discussed and an income statement example is provided for each. Cost classification issues are explained, such as product cost versus period costs and manufacturing overhead.

A summary exhibit provides product cost and period cost examples. The calculation of cost of goods manufactured is presented and a schedule example is provided. Exhibits help students visualize the flow of costs through a manufacturing company’s three inventory accounts.

The chapter concludes with a discussion on how to calculate cost per unit or cost per service for all three types of businesses. An end-of-chapter summary problem requires the student to calculate cost of goods sold and total period costs, and to prepare the income statement for a merchandising company. There are several short exercises for students to complete throughout the chapter.

**Learning Objectives**

1. Define managerial accounting and understand how it is used

2. Describe the difference between service, merchandising, and manufacturing companies

3. Classify costs for service, merchandising, and manufacturing companies

4. Prepare an income statement and schedule of costs of goods manufactured for a manufacturing company and calculate cost per item

5. Calculate cost per service for a service company and cost per item for a merchandising company

**Chapter 18: Teaching Outline**

1) Distinguish managerial accounting from financial accounting and the role of management accountability

a) Exhibit 18-1 Financial Accounting versus Managerial Accounting

2) Identify trends in today’s business environment

a) Shift Toward a Service Economy

b) Global Competition

c) Time-Based Competition

i. Advanced Information Systems…Enterprise Resource Planning (ERP)

ii. E-Commerce

iii. Just-in-Time Management (JIT)

d) Total Quality Management (TQM)

3) Apply ethical standards to decision making

a) Exhibit 18-3 IMA Statement of Ethical Professional Practice (excerpt)

4). Classify costs and prepare an income statement for a service company

a). Exhibit 18-4 Financial Statement Comparison, includes an Income Statement for a Service Company

5) Classify costs and prepare an income statement for a merchandising company

a) Exhibit 18-4 Financial Statement Comparison, includes an Income Statement for a Merchandising Company

6) Classify costs and prepare an income statement for a manufacturing company

a) Exhibit 18-4 Financial Statement Comparison, includes an Income Statement for a Manufacturing Company

b) Types of Costs

i. Direct Materials

ii. Direct Labor

iii. Manufacturing Overhead

c) Exhibit 18-5 Period and Product Costs for Smart Touch Learning (a manufacturing company)

d) Exhibit 18-6 Prime and Conversion Costs

7) Prepare a statement of cost of goods manufactured for a manufacturing company

a) Exhibit 18-7 Income Statement – Manufacturing Company

b) Exhibit 18-8 Manufacturing Company: Product Costs and Period Costs

c) Exhibit 18-9 Schedule of Costs of Good Manufactured

d) Exhibit 18-10 Flow of Costs Through Smart Touch Learning’s Inventory Accounts (a manufacturing company)

**Chapter 18: Summary Handout for Students**

1. Exhibit 18-1 Financial Accounting versus Managerial Accounting

2. Acting ethically is where integrity and credibility prevail; issues where professional judgments must be made arise often.

3. Service companies have only period costs.

* Period costs are incurred and expensed in the same accounting period.
* Unit cost per service = Total service costs/Total number of services provided

4. Merchandising companies have both product and period costs.

* Inventoriable product costs are held in inventory until sold.
* Beginning Inventory + Net Purchases + Freight In – Ending Inventory = Cost of Goods Sold
* Unit cost per item = Total cost of goods sold/Total number of items sold

5. Manufacturing companies maintain three kinds of inventory:

* Materials inventory
* Work in process inventory
* Finished goods inventory

6. Three components of manufacturing costs or inventoriable product costs are:

* Direct materials
* Direct labor
* Manufacturing overhead
  + - Indirect materials
    - Indirect labor
    - Other indirect costs

**Lecture Outline Tips: Key Topics**

When discussing financial and managerial accounting, it is common for students to prefer one over the other. It may be helpful to point this out to students, especially for accounting or business majors that may second guess their choice of major if they don’t like or excel in managerial accounting as they have in financial accounting. On the other hand, some students may prefer and excel in managerial accounting, which makes this a good time to point out the variety of career paths available in accounting.

When discussing the service economy and global competition, it may be interesting to take a survey of the types of jobs that students have and how many students know someone who had a job that was outsourced to another country. Ask students if the findings verify the textbook content.

Students will probably be able to relate to service and merchandising companies (think Walmart) better than manufacturing companies. Service and merchandising companies have already been discussed in the textbook. It may be helpful to ask students to provide examples of each type of company, especially merchandising and manufacturing, to assess their knowledge of the differences.

Manufacturers have three inventory accounts—raw materials (RM), work-in-process (WIP), and finished goods (FG). All three are assets on the balance sheet. Inventory is removed from finished goods when sold. The inventory accounts record product costs as they are added in the production process—direct materials, direct labor, and manufacturing overhead.

Point out the distinction between direct and indirect manufacturing costs. Direct costs are added to WIP, whereas indirect costs are added to manufacturing overhead and applied to WIP using a predetermined overhead rate. Therefore, when materials are used, you must know if it is indirect or direct. When labor is incurred, you must know whether it is direct or indirect. The recording of labor in an asset account (WIP) may need additional explanation. Students may want to expense labor because it was expensed in previous chapters. Remind students that manufacturing companies add all product costs to inventory and they are expensed (costs of goods sold) when inventory is sold.

Overhead includes all manufacturing costs other than direct materials and direct labor. Therefore, students must know if a cost is manufacturing or non-manufacturing. For example, “depreciation” will no longer suffice. Is it manufacturing or non-manufacturing? As discussed for labor above, students may want to expense all indirect costs such as depreciation, insurance, etc. because they were expensed in previous chapters. Remind students that manufacturing companies add all product costs to inventory and they are expensed (costs of goods sold) when inventory is sold.

# **Chapter 18 Assignment Grid**

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Learning Objective** | **Short Exercises**  ***Easy*** | **Exercises**  ***Moderate*** | **Problems (Group A) *Difficult*** | **Problems (Group B)**  ***Difficult*** |
| 1 | 1, 2, 3, 4 | 14, 15, 16 | 26 | 34 |
| 2 | 5, 6 | 17, 18, 19 | 28, 29, 30, 31, 32 | 36, 37, 38, 39, 40 |
| 3 | 7, 8, 9 | 20 | 27 | 35 |
| 4 | 10, 11, 12 | 21, 22, 23 | 28, 31, 32, 33 | 36, 39, 40, 41 |
| 5 | 13 | 24, 25 | 28, 29, 30 | 36, 37, 38 |

**Other End of Chapter Materials:**

|  |
| --- |
| Continuing Problem P18-42 |
| Decision Case 18-1 |
| Decision Case 18-2 |
| Ethical Issue 18-1 |
| Fraud Case 18-1 |
| Team Project 18-1 |
| Communication Activity 18-1 |

***Answer Key to Chapter 18 Quiz:***

|  |  |
| --- | --- |
| 1. A  2. B  3. D  4. C  5. D | 6. C  7. C  8. B  9. B  10. D |

Name Date Section

**CHAPTER 18**

**TEN-MINUTE QUIZ**

***Circle the letter of the best response.***

1. Which is *not* a characteristic of managerial accounting information?

A. Emphasizes the external financial statements

B. Provides detailed information about individual parts of the company

C. Emphasizes relevance

D. Focuses on the future

2. World-class businesses use which of these systems to integrate all of a company’s worldwide functions, departments, and data into a single system?

A. Cost standards

B. Enterprise resource planning

C. Just-in-time management

D. All of the above

3. Today’s business environment is characterized by

A. global competition.

B. time-based competition.

C. a shift toward a service economy.

D. Items A, B, and C are correct.

4. Which of the following accounts does a manufacturing company have that a service company does *not* have?

A. Advertising expense

B. Salary payable

C. Cost of goods sold

D. Retained earnings

5. In computing cost of goods sold, which of the following is the manufacturer’s equivalent to the merchandiser’s purchases and freight-in?

A. Total manufacturing costs to account for

B. Direct materials used

C. Total manufacturing costs incurred during the period

D. Cost of goods manufactured

6. Which of the following is a direct cost of manufacturing a sport boat?

A. Salary of engineer who rearranges plant layout

B. Depreciation on plant and equipment

C. Cost of boat engine

D. Cost of customer hotline

7. Which of the following is *not* part of manufacturing overhead for producing a computer?

A. Manufacturing plant property taxes

B. Manufacturing plant utilities

C. Depreciation on delivery trucks

D. Insurance on plant and equipment

*Questions 8 and 9 use the data that follow. Suppose a bakery reports this information:*

|  |  |  |
| --- | --- | --- |
| Beginning materials inventory | $ | 8,000 |
| Ending materials inventory |  | 7,000 |
| Beginning work in process inventory |  | 4,000 |
| Ending work in process inventory |  | 3,000 |
| Beginning finished goods inventory |  | 3,000 |
| Ending finished goods inventory |  | 5,000 |
| Direct labor |  | 30,000 |
| Purchases of direct materials |  | 95,000 |
| Manufacturing overhead |  | 21,000 |

8. What is the cost of direct materials used?

A. $95,000

B. $96,000

C. $103,000

D. $94,000

9. What is the cost of goods manufactured?

A. $146,000

B. $148,000

C. $144,000

D. $147,000

10. A management accountant who avoids conflicts of interest meets the ethical standard of

A. confidentiality.

B. competence.

C. credibility.

D. integrity.