

Accounting:

Text and Cases

Twelfth Edition

Robert N. Anthony

*Ross G. Walker Professor Emeritus
Graduate School of Business Administration
Harvard University*

David F. Hawkins

*Lovett-Learned Professor of Business
Administration
Graduate School of Business Administration
Harvard University*

Kenneth A. Merchant

*Deloitte & Touche LLP Chair of Accountancy
Leventhal School of Accounting
University of Southern California*



Boston Burr Ridge, IL Dubuque, IA Madison, WI New York San Francisco St. Louis
Bangkok Bogotá Caracas Kuala Lumpur Lisbon London Madrid Mexico City
Milan Montreal New Delhi Santiago Seoul Singapore Sydney Taipei Toronto

Contents

PART 1

FINANCIAL ACCOUNTING 1

Chapter 1

The Nature and Purpose of Accounting 2

- The Need for Information 2
 - Operating Information 3*
 - Financial Accounting Information 4*
 - Management Accounting Information 4*
 - Tax Accounting Information 5*
 - Definition of Accounting 6*
- The Profession of Accounting 6
- Our Approach to Accounting 6
 - Preconceptions about Accounting 7*
 - Plan of the Book 7*
- The Financial Accounting Framework 8
 - Accounting as a Language 8*
 - Nature of Principles 9*
 - Criteria 9*
 - Source of Accounting Principles 10*
- Financial Statements 12
 - The Balance Sheet 13*
 - The Income Statement 15*
 - "Package" of Financial Reports 16*
 - Financial Statement Objectives 16*
 - Sarbanes-Oxley Act 18*
 - Income Tax Reporting 18*
- Summary 18
- Problems 19
- Cases 21
 - Case 1-1: Ribbons an' Bows, Inc. 21*
 - Case 1-2: Kim Fuller 22*
 - Case 1-3: Baron Coburg 23*

Chapter 2

Basic Accounting Concepts: The Balance Sheet 25

- Basic Concepts 25
 - The Money Measurement Concept 26*
 - The Entity Concept 27*
 - The Going-Concern Concept 27*
 - The Cost Concept 28*
 - The Dual-Aspect Concept 31*

The Balance Sheet 32

- An Overall View 33*
- Account Categories 34*
- Assets 35*
- Liabilities 37*
- Owners' Equity 38*

Ratios 41

- Current Ratio 41*

Balance Sheet Changes 41

- Original Capital Contribution 41*
- Bank Loan 42*
- Purchase of Merchandise 42*
- Sale of Merchandise 42*

Concluding Comment 43

Summary 43

Problems 43

Cases 46

- Case 2-1: Maynard Company (A) 46*
- Case 2-2: Music Mart, Inc. 47*
- Case 2-3: Lone Pine Cafe (A) 47*

Chapter 3

Basic Accounting Concepts: The Income Statement 49

The Nature of Income 49

Basic Concepts 50

- The Accounting Period Concept 50*
- The Conservatism Concept 53*
- The Realization Concept 55*
- The Matching Concept 56*

Recognition of Expenses 57

- Terminology 57*
- Criteria for Expense Recognition 57*
- Expenses and Expenditures 58*
- Dividends 60*
- Summary of Expense Measurement 61*

Gains and Losses 62

- The Consistency Concept 62*
- The Materiality Concept 62*

The Income Statement 63

- Revenues 65*
- Cost of Sales 65*
- Gross Margin 66*
- Expenses 66*

<i>Net Income</i>	66
<i>Statement of Retained Earnings</i>	66
<i>Relation between Balance Sheet and Income Statement</i>	67
<i>Income Statement Percentages</i>	67
Other Concepts of Income	67
<i>Accrual versus Cash-Basis Accounting</i>	67
<i>Income Tax Accounting</i>	68
<i>Economic Income</i>	69
<i>Pro Forma Earnings</i>	69
Accounting and Changing Prices	69
<i>Nature of the Problem</i>	70
<i>Proposed Solutions</i>	70
Summary	71
Problems	72
Cases	74
<i>Case 3-1: Maynard Company (B)</i>	74
<i>Case 3-2: Lone Pine Cafe (B)</i>	75
<i>Case 3-3: Dispensers of California, Inc.</i>	75
<i>Case 3-4: Pinetree Motel</i>	76
<i>Case 3-5: National Association of Accountants</i>	78
Chapter 4	
Accounting Records and Systems	81
Recordkeeping Fundamentals	81
<i>The Account</i>	82
<i>Permanent Accounts and Temporary Accounts</i>	82
<i>The Ledger</i>	83
<i>The Chart of Accounts</i>	83
<i>Debit and Credit</i>	83
The Accounting Process	85
Transaction Analysis	86
<i>Example: Campus Pizzeria, Inc.</i>	86
<i>Balancing Accounts</i>	89
<i>The Trial Balance</i>	90
The Adjusting and Closing Process	91
<i>Adjusting Entries</i>	91
<i>Closing Entries</i>	94
<i>Statement Preparation</i>	96
<i>The Journal</i>	96
Accounting Systems	98
<i>Internal Accounting Controls</i>	98
Computer-Based Accounting Systems	99
<i>What a Computer-Based System Does</i>	99
<i>Modules</i>	100
<i>Problems with Computer Systems</i>	100
Summary	101
Appendix: Additional Accounting Cycle Procedures	101
Problems	103
Cases	105
<i>Case 4-1: PC Depot</i>	105
<i>Case 4-2: Save-Mart</i>	106
<i>Case 4-3: Copies Express</i>	107
<i>Case 4-4: Waltham Oil and Lube Center, Inc.</i>	108
Chapter 5	
Revenue and Monetary Assets	110
Timing of Revenue Recognition	110
<i>Basic Recognition Criteria</i>	110
<i>SEC Response</i>	111
<i>Delivery Method</i>	113
<i>Percentage-of-Completion Method</i>	114
<i>Production Method</i>	115
<i>Installment Method</i>	115
Amount of Revenue Recognized	116
<i>Bad Debts</i>	117
<i>Sales Discounts</i>	119
<i>Credit Card Sales</i>	120
<i>Sales Returns and Allowances</i>	121
<i>Revenue Adjustment versus Expense</i>	121
<i>Warranty Costs</i>	122
<i>Interest Revenue</i>	123
Monetary Assets	125
<i>Difference in Reporting Monetary and Nonmonetary Assets</i>	125
<i>Cash</i>	125
<i>Receivables</i>	125
<i>Marketable Securities</i>	125
Analysis of Monetary Assets	126
<i>Current Ratio</i>	126
<i>Acid-Test Ratio</i>	127
<i>Days' Cash</i>	128
<i>Days' Receivables</i>	128
Summary	129
Problems	129
Cases	132
<i>Case 5-1: Stern Corporation (A)</i>	132
<i>Case 5-2: Grennell Farm</i>	132
<i>Case 5-3: Joan Holtz (A)</i>	135
<i>Case 5-4: Bausch & Lomb, Inc. (A)</i>	137
<i>Case 5-5: Boston Automation Systems, Inc.</i>	143

Chapter 6**Cost of Sales and Inventories 147**

Types of Companies 147

Supplies 148

Merchandising Companies 148

*Acquisition Cost 148**The Basic Measurement Problem 149**Periodic Inventory Method 150**Perpetual Inventory Method 151**Comparison of Periodic and Perpetual Methods 152**Retail Method 153*

Manufacturing Companies 154

*Inventory Accounts 154**Materials Used 155**Cost of Goods Manufactured 156**Cost of Goods Sold 157**Product Costing Systems 158**Product Costs and Period Costs 158*

Service Companies 159

Inventory Costing Methods 159

*Specific Identification Method 160**Average Cost Method 160**First-In, First-Out Method 161**Last-In, First-Out Method 161**Comparison of Methods 162*

Lower of Cost or Market 165

Analysis of Inventory 166

*Inventory Turnover 166**Gross Margin Percentage 167*

Summary 167

Problems 168

Cases 170

*Case 6-1: Browning Manufacturing Company 170**Case 6-2: Lewis Corporation 173**Case 6-3: Morgan Manufacturing 174**Case 6-4: Joan Holtz (B) 176**Case 6-5: UAL Corporation 177***Chapter 7****Long-Lived Nonmonetary Assets and Their Amortization 187**

Nature of Long-Lived Assets 187

Types of Long-Lived Assets 188

Plant and Equipment: Acquisition 189

*Distinction between Asset and Expense 189**Items Included in Cost 190**Acquisitions Recorded at Other Than Cost 191**Basket Purchases 191*

Plant and Equipment: Depreciation 191

*Judgments Required 192**Service Life 193**Depreciation Methods 193**Choice of a Depreciation Method 195*

Accounting for Depreciation 196

*Change in Depreciation Rates 197**Partial-Year Depreciation 197**Disclosure 197*

Plant and Equipment: Disposal 198

*Exchanges and Trade-Ins 199**Group Depreciation 200*

Significance of Depreciation 200

Income Tax Considerations 201

*Depreciation Allowances 201**Investment Tax Credit 202*

Natural Resources 203

*Depletion 204**Accretion and Appreciation 204*

Intangible Assets 204

*Limited Useful Life 204**Indefinite Useful Life 205**Goodwill 205**Patents and Copyrights 206**Leasehold Improvements 206**Deferred Charges 206**Research and Development Costs 206**Analysis of Nonmonetary Assets 207*

Summary 208

Problems 208

Cases 210

*Case 7-1: Stern Corporation (B) 210**Case 7-2: Joan Holtz (C) 211**Case 7-3: Stafford Press 213***Chapter 8****Sources of Capital: Debt 215**

Nature of Liabilities 215

*Executory Contracts 215**Contingencies 216**Liabilities as a Source of Funds 217*

Debt Capital 218

*Term Loans 218**Bonds 218*

Accounting for Bonds 219

*Recording a Bond Issue 219**Balance Sheet Presentation 221**Bond Interest Expense 222*

<i>Retirement of Bonds</i>	223
<i>Refunding a Bond Issue</i>	224
Leased Assets	224
<i>Capital Leases</i>	225
<i>Sale and Leaseback</i>	226
Other Liabilities	226
<i>Current Liabilities</i>	226
<i>Deferred Taxes</i>	226
Analysis of Capital Structure	226
<i>Debt Ratios</i>	226
<i>Times Interest Earned</i>	228
<i>Bond Ratings</i>	228
Summary	228
Appendix: Present Value	229
Problems	236
Cases	238
<i>Case 8-1: Norman Corporation (A)</i>	238
<i>Case 8-2: Stone Industries</i>	240
<i>Case 8-3: Paul Murray</i>	242
<i>Case 8-4: Joan Holtz (D)</i>	242
Chapter 9	
Sources of Capital: Owners' Equity	245
Forms of Business Organization	245
<i>Sole Proprietorship</i>	245
<i>Partnership</i>	246
<i>Corporation</i>	246
Accounting for Proprietor's and Partners' Equity	247
<i>Proprietorship Equity</i>	247
<i>Partnership Equity</i>	247
Ownership in a Corporation	248
<i>Preferred Stock</i>	248
<i>Common Stock</i>	249
<i>Treasury Stock</i>	250
<i>Retained Earnings</i>	250
<i>Reserves</i>	251
<i>Dividends</i>	251
<i>Warrants and Stock Options</i>	253
<i>Employee Stock Ownership Plans</i>	253
<i>Balance Sheet Presentation</i>	254
Earnings per Share	254
The Line between Debt and Equity	256
<i>Zero-Coupon Bonds</i>	257
<i>Debt with Warrants</i>	257
<i>Redeemable Preferred Stock</i>	258
Equity in Nonprofit Organizations	258
Summary	259
Problems	259

Cases	262
<i>Case 9-1: Xytech, Inc.</i>	262
<i>Case 9-2: Innovative Engineering Company</i>	263
<i>Case 9-3: UPC Inc.</i>	264
<i>Case 9-4: Maxim Integrated Products, Inc.</i>	267

Chapter 10

Other Items That Affect Net Income and Owners' Equity 272

Total and Other Nonowner Changes in Owners' Equity	272
Nonoperating Items	274
<i>Extraordinary Items</i>	274
<i>Pro Forma Earnings</i>	275
<i>Discontinued Operations</i>	276
<i>Change in Accounting Principles</i>	276
<i>Errors</i>	277
Personnel Costs	277
<i>Pensions</i>	278
<i>Other Postretirement Benefits</i>	280
<i>Compensated Absences</i>	281
Income Taxes	281
<i>Book-to-Tax Differences</i>	281
<i>Deferred Income Taxes</i>	283
<i>Deferred Tax Measurement</i>	284
<i>Accounting Entries</i>	286
Foreign Currency Accounting	289
<i>Foreign Currency Transactions</i>	289
<i>Foreign Currency Translation Adjustments</i>	290
Derivatives	292
Pro Forma Earnings	293
Net Income	293
Summary	293
Problems	294
Cases	296
<i>Case 10-1: Norman Corporation (B)</i>	296
<i>Case 10-2: Silver Appliance Company</i>	297
<i>Case 10-3: Kansas City Zephyrs Baseball Club, Inc.</i>	299
<i>Case 10-4: Freedom Technology Company</i>	307
<i>Case 10-5: Proxim, Inc.</i>	308

Chapter 11

The Statement of Cash Flows 310

Purpose of the Cash Flow Statement	310
<i>Sources and Uses of Cash</i>	311
The Cash Flow Statement	312
<i>Statement Categories</i>	313

<i>Investing Activities</i>	313
<i>Financing Activities</i>	315
<i>Noncash Transactions</i>	317
<i>Cash Flow from Operating Activities</i>	317
<i>Indirect Method Calculations</i>	318
<i>Summary of the Cash Flow Statement</i>	322
Misconceptions about Depreciation	323
<i>Cash Flow Worksheet</i>	324
Preparation of the Cash Flow Statement	324
<i>Cash Flow Earnings</i>	324
<i>Worksheet Entries</i>	327
<i>Statement Preparation</i>	329
<i>Summary of Preparation Procedures</i>	330
Analysis of the Cash Flow Statement	331
<i>Ratios</i>	331
<i>Cash Flow Projections</i>	332
Summary	333
Problems	333
Cases	335
<i>Case 11-1: Medieval Adventures Company</i>	335
<i>Case 11-2: Amerbran Company (A)</i>	336
<i>Case 11-3: Great Valu Variety Stores</i>	338

Chapter 12

Acquisitions and Consolidated Statements 342

Accounting for Investments	342
<i>Fair-Value Method</i>	342
<i>Cost Method</i>	343
<i>Equity Method</i>	343
<i>Consolidated Basis</i>	344
Business Combinations	344
<i>Purchase versus Pooling</i>	344
<i>Accounting as a Pooling</i>	345
<i>Accounting as a Purchase</i>	345
Consolidated Statements	347
<i>Basis for Consolidation</i>	348
<i>Consolidation Procedure</i>	348
<i>Asset Valuation</i>	350
<i>Minority Interest</i>	351
Summary	352
Problems	352
Cases	354
<i>Case 12-1: Hardin Tool Company</i>	354
<i>Case 12-2: Carter Corporation</i>	356
<i>Case 12-3: Keane's Acquisition of Metro Information Services</i>	357
<i>Case 12-4: Productos Finas</i>	366

Chapter 13

Financial Statement Analysis 369

Business Objectives	369
<i>Return on Investment</i>	370
<i>Sound Financial Position</i>	371
<i>Structure of the Analysis</i>	371
Overall Measures	371
<i>Return on Investment</i>	371
<i>Investment Turnover and Profit Margin</i>	376
<i>Price/Earnings Ratio</i>	377
Profitability Ratios	378
<i>Profit Margin</i>	378
<i>Common-Size Financial Statements</i>	378
Investment Utilization Ratios	379
<i>Investment Turnover</i>	379
<i>Capital Asset Intensity</i>	379
<i>Working Capital Measures</i>	379
Financial Condition Ratios	381
<i>Liquidity and Solvency</i>	381
Dividend Policy	381
Growth Measures	383
Making Comparisons	384
<i>Difficulties</i>	384
<i>Possible Bases for Comparison</i>	386
<i>Use of Comparisons</i>	387
Summary	388
Problems	388
Cases	390
<i>Case 13-1: Genmo Corporation</i>	390
<i>Case 13-2: Amerbran Company (B)</i>	392
<i>Case 13-3: Identify the Industries</i>	393
<i>Case 13-4: Supplement to Identify the Industries</i>	393
<i>Case 13-5: Springfield National Bank</i>	393
<i>Case 13-6: Quality Furniture Company</i>	400
<i>Case 13-7: Sears, Roebuck and Co. vs. Wal-Mart Stores, Inc.</i>	404

Chapter 14

Understanding Financial Statements 419

Additional Information in Annual Reports	419
<i>Auditors' Opinion</i>	419
<i>Notes to Financial Statements</i>	422
<i>Segment Reporting</i>	423
<i>Full Disclosure</i>	424
<i>Comparative Statements</i>	424
<i>Management's Discussion and Analysis</i>	424
<i>Securities and Exchange Commission (SEC) Reports</i>	424

Review of Criteria and Concepts 425*Criteria 425**Concepts 426***Accounting Alternatives 430***Regulatory Requirements 430**Income Tax Principles 430**Latitude in Methods 431**Basis of Choice 431**Controversies over Principles 432**Implications of These Differences 433**Inherent Limitations 434**Ethical Problems 434***Meaning of the Financial Statements 435***Income Statement 435**Balance Sheet 436**Statement of Cash Flows 438***Summary 438****Problems 438****Cases 441***Case 14–1: Quick Lunch 441**Case 14–2: Scientific Instrument Corporation 442**Case 14–3: Limited Editions, Inc. 445**Case 14–4: Accounting at MacCloud Winery 447**Case 14–5: PolyMedica Corporation (A) 448***PART 2****MANAGEMENT ACCOUNTING 455****Chapter 15****The Nature of Management Accounting 456****Management Accounting 456***Management Accounting Is a Relatively**Young Field 457**Management Accountants 458***Contrast between Management Accounting and Financial Reporting 459***Differences 459**Similarities 461***Types of Management Accounting Information and Their Uses 462***Measurement 463**Control 464**Alternative Choice Decisions 465***Databases 465****General Observations on Management Accounting 467***Different Numbers for Different Purposes 468**Accounting Numbers Are Approximations 468**Working with Incomplete Data 468**Accounting Evidence Is Only Partial Evidence 468**People, Not Numbers, Get Things Done 469***Summary 469****Problems 470****Case 472***Case 15–1: Private Fitness, LLC 472***Chapter 16****The Behavior of Costs 474****Relation of Costs to Volume 474***Variable and Fixed Costs 474**Cost–Volume Diagrams 475**Relation to Unit Costs 477**Inherent Conditions 478**Linear Assumption 481**Estimating the Cost–Volume**Relationship 482**Measures of Volume 485***Profitgraphs 486***Break-Even Analysis 487**Target Profit 488**Operating Leverage 488**Contribution 488**Cash versus Accrual Profitgraphs 491**Using the Profitgraph 491**Several Products 492**Other Influences on Costs 494***Summary 495****Appendix: Learning Curves 495****Problems 497****Cases 499***Case 16–1: Hospital Supply, Inc. 499**Case 16–2: Prestige Telephone Company 501**Case 16–3: Bill French 504***Chapter 17****Full Costs and Their Uses 508****Cost Concepts 508***General Definition 508**Cost Object 509**Full Cost 509**Direct and Indirect Costs 509**Applicable Accounting Principles 510**Elements of Product Cost 511***Product Costing Systems 513***Account Flowchart 514*

Nonmanufacturing Costs 517

- Merchandising Companies 518*
- Service Organizations 519*
- Nonprofit Organizations 519*

Uses of Full Cost 520

- Financial Reporting 520*
- Analyses of Profitability 520*
- What Did It Cost? 520*
- Setting Regulated Prices 521*
- Product Pricing 521*

Summary 524

Problems 524

Cases 526

- Case 17-1: Delaney Motors 526*
- Case 17-2: Lipman Bottle Company 529*
- Case 17-3: Shelter Partnership, Inc. 533*

Chapter 18

Additional Aspects of Product Costing Systems 537

Job Order Costing and Process Costing 537

- Production Processes 537*
- Averaging 537*
- Basic Types of Systems 538*
- Job Order Costing 538*
- Process Costing 539*
- Choice of a System 541*
- Variations in Practice 542*

Measurement of Direct Costs 542

- Direct Labor Cost 543*
- Direct Material Cost 544*
- Direct versus Variable Cost 544*

Allocation of Indirect Costs 545

- Distinction between Direct and Indirect Costs 545*
- Nature of Allocation 546*
- Cost Centers 546*
- Calculating Overhead Rates 547*
- Cost Drivers (Allocation Bases) 551*
- Predetermined Overhead Rates 553*
- Procedure for Establishing Predetermined Rates 554*
- Underabsorbed and Overabsorbed Overhead 557*
- Activity-Based Costing 557*
- Cross-Subsidies 559*
- Activity-Based Costing Concepts 559*

Summary 565

Problems 566

Cases 569

- Case 18-1: Huron Automotive Company 569*
- Case 18-2: California Creamery, Inc. 573*

Case 18-3: Wilkerson Company 575

Case 18-4: Safety Monitoring Devices, Inc. 578

Case 18-5: Dakota Office Products 582

Chapter 19

Standard Costs, Variable Costing Systems, Quality Costs, and Joint Costs 586

Standard Costs 586

- Standard Cost Sheet 586*
- Account Flowchart 587*
- Variations in the Standard Cost Idea 591*
- Terminology Ambiguities 592*
- Uses of Standard Costs 592*

Variable Costing Systems 594

- Comparison of Absorption and Variable Costing 594*
- Why Use Full Costing? 597*

Quality Costs 599

Joint Products and By-Products 600

- Joint-Product Costing 600*
- By-Product Costing 601*

Accuracy of Costs 602

- Judgment Calls 602*
- Tendencies toward Uniformity 602*

Cost System Design Choices 603

Summary 603

Appendix A: Standard Costing

Illustration 604

Appendix B: Absorption versus Variable

Costing's Impact on Income 610

Problems 611

Cases 613

- Case 19-1: Bennett Body Company 613*
- Case 19-2: Black Meter Company 615*
- Case 19-3: Brisson Company 615*
- Case 19-4: Landau Company 616*
- Case 19-5: Lynch's Chicken Ranch, Inc. 618*

Chapter 20

Production Cost Variance Analyses 621

Variances 621

Direct Material and Labor Variances 622

- Direct Material Variances 622*
- Direct Labor Variances 626*

Overhead Variances 627

- Production Volume Variance 628*
- Spending Variance 629*
- Calculation of Overhead Variances 630*

Summary 633

Cases 636

- Case 20-1: SunAir Boat Builders, Inc.* 636
- Case 20-2: Medi-Exam Health Services, Inc.* 638
- Case 20-3: Cotter Company, Inc.* 639
- Case 20-4: Lupton Company* 640

Chapter 21**Other Variance Analyses 643**

Overview of the Analytical Process 643

- The Need for Variance Analysis* 643
- Types of Variances* 644

Marketing Variances 644

- Expense Variances* 644
- Gross Margin Variances* 646

Production Cost Variances 652

- Correct Volume Measures* 652

Other Variances 653

Complete Analysis 654

- Marketing Variances* 654
- Production Cost Variances* 654
- Uses of Variances* 656

Summary 657

Problems 658

Cases 660

- Case 21-1: Campar Industries, Inc.* 660
- Case 21-2: Darius Company* 662
- Case 21-3: Woodside Products, Inc.* 662

Chapter 22**Control: The Management Control Environment 664**

Management Control 664

The Environment 665

- The Nature of Organizations* 665
- Rules, Guidelines, and Procedures* 667
- Culture* 667
- External Environment* 667

Responsibility Centers and Responsibility

Accounts 668

- Inputs and Outputs* 668
- Responsibility Accounting* 669
- Effectiveness and Efficiency* 671

Types of Responsibility Centers 671

- Revenue Centers* 672
- Expense Centers* 672
- Profit Centers* 673
- Transfer Prices* 674

Investment Centers 677*Nonmonetary Measures* 679

Summary 679

Problems 679

Cases 681

- Case 22-1: Behavioral Implications of Airline Depreciation Accounting Policy Choices* 681
- Case 22-2: Shuman Automobiles, Inc.* 683
- Case 22-3: Zumwald AG* 687
- Case 22-4: Enager Industries, Inc.* 689
- Case 22-5: Piedmont University* 693

Chapter 23**Control: The Management Control Process 696**

Phases of Management Control 696

- Strategic Planning* 696
- Budgeting* 697
- Measurement and Reporting* 697
- Evaluation* 698

Accounting Information Used in Management

Control 698

- Controllable Costs* 698
- Engineered, Discretionary, and Committed Costs* 702

Behavioral Aspects of Management Control 704

- Behavior of Participants* 704
- Motivation* 705
- Incentives* 706
- Goal Congruence* 707
- Cooperation and Conflict* 708
- Other Types of Control* 709

Summary 709

Problems 709

Cases 712

- Case 23-1: Tru-Fit Parts, Inc.* 712
- Case 23-2: Industrial Electronics, Inc.* 715
- Case 23-3: Las Ferreterías de México, S.A. de C.V.* 716
- Case 23-4: Boise Cascade Corporation* 719
- Case 23-5: Berkshire Industries PLC* 727

Chapter 24**Strategic Planning and Budgeting 733**

Strategic Planning 733

- Ongoing Programs* 734
- Proposed New Programs* 735
- Formal Strategic Planning Systems* 736

Budgeting 736

Uses of the Budget 736

The Master Budget 738

The Operating Budget 739

Project Budgets 740

Flexible (Variable) Budgets 740

Management by Objectives 740

Preparing the Operating Budget 742

Organization for Budget Preparation 742

Budget Timetable 743

Setting Planning Guidelines 744

Preparing the Sales Budget 744

Initial Preparation of Other Budget

Components 745

Negotiation 746

Coordination and Review 748

Final Approval and Distribution 748

Revisions 748

Variations in Practice 749

The Cash Budget 750

The Capital Expenditure Budget 751

Project Proposals 751

Authorization 752

Follow-Up 752

Beyond Budgeting 752

Summary 753

Problems 753

Cases 755

Case 24-1: Body Glove 755

Case 24-2: Waikerie Co-Operative

Producers Ltd. 762

Case 24-3: Patagonia, Inc. 771

Case 24-4: Borealis 784

Chapter 25

Reporting and Evaluation 795

Control Reports 795

Key Success Factors 795

Types of Management Reports 796

Period of Control Reports 797

Contents of Control Reports 797

Use of Control Reports 801

Feedback 803

Steps in the Control Process 803

Reporting and Continuous Improvement 804

Incentive Compensation 805

Summary 806

Problems 806

Cases 809

Case 25-1: Olympic Car Wash 809

Case 25-2: Armco, Inc.: Midwestern Steel

Division 810

Case 25-3: Formosa Plastics Group 821

Chapter 26

Short-Run Alternative Choice

Decisions 829

The Differential Concept 829

Cost Constructions for Various Purposes 829

Differential Costs and Revenues 830

Contrasts with Full Costs 830

Contribution Analysis 831

Types of Cost 833

Alternative Choice Problems 834

Steps in the Analysis 835

Differential Costs 836

Mechanics of the Calculation 837

Other Terminology 839

Estimates of Future Costs 840

Sunk Costs 840

Importance of the Time Span 841

Example: Operating an Automobile 842

Types of Alternative Choice Problems 843

Problems Involving Costs 843

Problems Involving Both Revenues and Costs 844

Differential Investment 847

Sensitivity Analysis 847

The "Just One" Fallacy 848

Expected Values 849

Decision Tree Analysis 850

Some Practical Pointers 850

Summary 851

Problems 851

Cases 854

Case 26-1: Import Distributors, Inc. 854

Case 26-2: Forner Carpet Company 855

Case 26-3: Precision Worldwide, Inc. 857

Case 26-4: Baldwin Bicycle Company 859

Chapter 27

Longer-Run Decisions: Capital

Budgeting 862

Nature of the Problem 862

General Approach 863

Net Present Value 864

Return on Investment 864

Estimating the Variables	866
<i>Required Rate of Return</i>	866
<i>Economic Life</i>	868
<i>Cash Inflows</i>	868
<i>Investment</i>	872
<i>Terminal Value</i>	873
<i>Nonmonetary Considerations</i>	873
<i>Summary of the Analytical Process</i>	875
Other Methods of Analysis	875
<i>Internal Rate of Return Method</i>	875
<i>Payback Method</i>	877
<i>Unadjusted Return on Investment Method</i>	878
<i>Multiple Decision Criteria</i>	879
Preference Problems	880
<i>Criteria for Preference Problems</i>	880
<i>Comparison of Preference Rules</i>	880
Nonprofit Organizations	881
Summary	881
Problems	882
Cases	884
<i>Case 27-1: Sinclair Company</i>	884
<i>Case 27-2: Rock Creek Golf Club</i>	886
<i>Case 27-3: Phuket Beach Hotel: Valuing Mutually Exclusive Capital Projects</i>	887

Chapter 28 Management Accounting System Design 890

Types of Accounting Information	890
<i>Measurement</i>	890
<i>Control</i>	891
<i>Alternative Choice Problems</i>	891
<i>Relative Importance</i>	891
Cost Categories	892
Designing the Management Accounting System	894
<i>Accounting Database</i>	894
<i>Level of Detail</i>	894
<i>Cost Accounting Systems</i>	895
<i>Management Control Systems</i>	895
Cases	896
<i>Case 28-1: Puente Hills Toyota</i>	896
<i>Case 28-2: Axxon N. V.</i>	908

Appendixes 915

Index 917