Chapter 1

Managerial Accounting: An Overview

Solutions to Questions

**1-1** Financial accounting is concerned with reporting financial information to external parties, such as stockholders, creditors, and regulators. Managerial accounting is concerned with providing information to managers for use within the organization. Financial accounting emphasizes the financial consequences of past transactions, objectivity and verifiability, precision, and companywide performance, whereas managerial accounting emphasizes decisions affecting the future, relevance, timeliness, and segment performance. Financial accounting is mandatory for external reports and it needs to comply with rules, such as generally accepted accounting principles (GAAP) and international financial reporting standards (IFRS), whereas managerial accounting is not mandatory and it does not need to comply with externally imposed rules.

**1-2** Five examples of planning activities include (1) estimating the advertising revenues for a future period, (2) estimating the total expenses for a future period, including the salaries of all actors, news reporters, and sportscasters, (3) planning how many new television shows to introduce to the market, (4) planning each television show’s designated broadcast time slot, and (5) planning the network’s advertising activities and expenditures.

Five examples of controlling activities include (1) comparing the actual number of viewers for each show to its viewership projections, (2) comparing the actual costs of producing a made-for-television movie to its budget, (3) comparing the revenues earned from broadcasting a sporting event to the costs incurred to broadcast that event, (4) comparing the actual costs of running a production studio to the budget, and (5) comparing the actual cost of providing global, on-location news coverage to the budget.

**1-3** The quantitative analysis would focus on determining the potential cost savings from buying the part rather than making it. The qualitative analysis would focus on broader issues such as strategy, risks, and corporate social responsibility. For example, if the part is critical to the organization’s strategy, it may continue making the part regardless of any potential cost savings from outsourcing. If the overseas supplier might create quality control problems that could threaten the end consumers’ welfare, then the risks of outsourcing may swamp any cost savings. Finally, from a social responsibility standpoint, a company may decide against outsourcing if it would result in layoffs at its domestic manufacturing facility.

**1-4** Companies use budgets to translate plans into formal quantitative terms. Budgets are used for various purposes, such as forcing managers to plan ahead, allocating resources across departments, coordinating activities across departments, establishing goals that motivate people, and evaluating and rewarding employees. These various purposes often conflict with one another, which makes budgeting one of management’s most challenging activities.

**1-5** Managerial accounting is relevant to all business students because all managers engage in planning, controlling, and decision making activities. If managers wish to influence co-workers across the organization, they must be able to speak in financial terms to justify their proposed courses of action.

**1-6** The Institute of Management Accountants estimates that 80% of accountants work in non-public accounting environments. Accountants that work in corporate, non-profit, and governmental organizations are expected to use their planning, controlling, and decision-making skills to help improve performance.

**1-7** Deere & Company is an example of a company that competes in terms of product leadership. The company’s slogan “nothing runs like a Deere” emphasizes its product leadership customer value proposition.

Amazon.com competes in terms of operational excellence. The company focuses on delivering products faster, more conveniently, and at a lower price than competitors.

Charles Schwab competes in terms of customer intimacy. It focuses on building personal relationships with clients so that it can tailor investment strategies to individual needs.

**1-8** Planning, controlling, and decision making must be performed within the context of a company’s strategy. For example, if a company that competes as a product leader plans to grow too quickly, it may diminish quality and threaten the company’s customer value proposition. A company that competes in terms of operational excellence would select control measures that focus on time-based performance, convenience, and cost. A company that competes in terms of customer intimacy may decide against outsourcing employee training to cut costs because it might diminish the quality of customer service.

**1-9** This answer is based on Nike, which has suppliers in over 40 countries. One risk that Nike faces is that its suppliers will fail to manage their employees in a socially responsible manner. Nike conducts Management Audit Verifications at its overseas plants to minimize this risk.

Nike faces the risk that unsatisfactory environmental performance will diminish its brand image. The company is investing substantial resources to develop products that minimize adverse impacts on the environment.

Nike faces the risk that customers will not like its new products. The company uses focus group research to proactively assess the customers’ reaction to its new products.

**1-10** Airlines face the risk that large spikes in fuel prices will lower their profitability. Therefore, they may reduce this risk by spending money on hedging contracts that enable them to lock-in future fuel prices that will not change even if the market price increases.

Steel manufacturers face major risks related to employee safety, so they create and monitor control measures related to occupational safety compliance and performance.

Restaurants face the risk that an economic downturn will reduce customer traffic and lower sales. They reduce this risk by choosing to create menus during economic downturns that offer more low-priced entrees.

**1-11** Barnes & Noble could segment its companywide performance by individual store, by sales channel (i.e., bricks-and-mortar versus on-line), and by product line (e.g. non-fiction books, fiction books, music CDs, toys, etc.).

Procter & Gamble could segment its performance by product category (e.g., beauty and grooming, household care, and health and well-being), product line (e.g., Crest, Tide, and Bounty), and stock keeping units (e.g., Crest Cavity Protection toothpaste, Crest Extra Whitening toothpaste, and Crest Sensitivity toothpaste).

**1-12** Timberland publishes quarterly corporate social responsibility (CSR) metrics (see <http://responsibility.timberland.com/reporting/goals-and-progress/>. Three of those metrics include metric tons of carbon emissions, the percentage of total cotton sourced that is organic, and renewable energy use as a percent of total energy usage.

Timberland’s corporate slogan of “doing well by doing good” suggests that the company publishes CSR reports because it believes that its financial success (i.e., doing well) is positively influenced by its social and environmental performance (i.e., doing good).

**1-13** Companies that use lean production only make units in response to customer orders. They produce units just in time to satisfy customer demand, which results in minimal inventories.

**1-14** Organizations are managed by people that have their own personal interests, insecurities, beliefs, and data-supported conclusions that ensure unanimous support for a given course of action is the exception rather than the rule. Therefore, managers must possess strong leadership skills if they wish to channel their co-workers’ efforts towards achieving organizational goals.

**1-15** Ethical behavior is the lubricant that keeps the economy running. Without that lubricant, the economy would operate much less efficiently—less would be available to consumers, quality would be lower, and prices would be higher.