

# MANAGERIAL ACCOUNTING

## TRUE-FALSE STATEMENTS

1. Reports prepared in financial accounting are general-purpose reports, whereas reports prepared in managerial accounting are usually special-purpose reports.
2. Managerial accounting information generally pertains to an entity as a whole and is highly aggregated.
3. Managerial accounting applies to all forms of business organizations.
4. Determining the unit cost of manufacturing a product is an output of financial accounting.
5. Managerial accounting internal reports are prepared more frequently than are classified financial statements.
6. The management function of directing and motivating is mainly concerned with setting goals and objectives for the entity.
7. An organization chart in a manufacturing company replaces the chart of accounts.
8. Controlling is the process of determining whether planned goals are being met.
9. Decision-making is an integral part of the planning, directing and motivating, and controlling functions.
10. Both direct labor cost and indirect labor cost are product costs.
11. Manufacturing costs that cannot be classified as direct material or direct labor are classified as manufacturing overhead.
12. Raw materials are equal to direct materials minus indirect materials.
13. Raw materials that can be conveniently and directly associated with a finished product are called material overhead.
14. The total cost of a finished product does not generally contain equal amounts of material, labor, and overhead costs.
15. Direct material costs and indirect material costs are prime costs.
16. Conversion costs consist of direct labor and manufacturing overhead.
17. Indirect materials and indirect labor are both inventoriable costs.
18. Direct labor costs subtracted from prime costs equals manufacturing overhead costs.
19. Total period costs are deducted from total cost of work in process to calculate cost of goods manufactured.
20. Period costs are not inventoriable costs.

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21. Ending finished goods inventory appears on both the balance sheet and the income statement of a manufacturing company.
22. The beginning work in process inventory appears on both the balance sheet and the cost of goods manufactured schedule of a manufacturing company.
23. In calculating gross profit for a manufacturing company, the cost of goods manufactured is deducted from net sales.
24. Finished goods inventory does not appear on a cost of goods manufactured schedule.
25. If the ending work in process inventory is greater than the beginning work in process inventory, then the cost of goods manufactured will be less than total manufacturing costs for the period.
26. Finished goods inventory for a manufacturing company is equivalent to merchandise inventory for a merchandising company.
27. Raw materials inventory is not an asset until it is used to make a product.
28. Raw materials inventory shows the cost of completed goods available for sale to customers.
- \*29. In preparing closing entries for a manufacturing company, all revenue and expense account balances are closed to a Manufacturing Summary account.
- \*30. To balance the Cost of Goods Manufactured columns of a work sheet for a manufacturing company, an entry must be made in the income statement debit column.

**Answers to True-False Statements**

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
1.	T	6.	F	11.	T	16.	T	21.	T	26.	T
2.	F	7.	F	12.	F	17.	T	22.	F	27.	F
3.	T	8.	T	13.	F	18.	F	23.	F	28.	F
4.	F	9.	T	14.	T	19.	F	24.	T	*29.	F
5.	T	10.	T	15.	F	20.	T	25.	T	*30.	T

**MULTIPLE CHOICE QUESTIONS**

31. Managerial accounting information is generally prepared for
  - a. stockholders.
  - b. creditors.
  - c. managers.
  - d. regulatory agencies.
  
32. Managerial accounting information
  - a. pertains to the entity as a whole and is highly aggregated.
  - b. pertains to subunits of the entity and may be very detailed.
  - c. is prepared only once a year.
  - d. is constrained by the requirements of generally accepted accounting principles.
  
33. The major reporting standard for presenting managerial accounting information is
  - a. relevance.
  - b. generally accepted accounting principles.
  - c. the cost principle.
  - d. the current tax law.
  
34. Managerial accounting is also called
  - a. management accounting.
  - b. controlling.
  - c. analytical accounting.
  - d. inside reporting.
  
35. Which of the following is not an internal user?
  - a. Creditor
  - b. Department manager
  - c. Controller
  - d. Treasurer
  
36. Managerial accounting does not encompass
  - a. calculating product cost.
  - b. calculating earnings per share.
  - c. determining cost behavior.
  - d. profit planning.
  
37. Managerial accounting is applicable to
  - a. service entities.
  - b. manufacturing entities.
  - c. not-for-profit entities.
  - d. all of these.
  
38. Management accountants would not
  - a. assist in budget planning.
  - b. prepare reports primarily for external users.
  - c. determine cost behavior.
  - d. be concerned with the impact of cost and volume on profits.

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39. Internal reports must be communicated
  - a. daily.
  - b. monthly.
  - c. annually.
  - d. as needed.
  
40. Financial statements for external users can be described as
  - a. user-specific.
  - b. general-purpose.
  - c. special-purpose.
  - d. managerial reports.
  
41. Managerial accounting reports can be described as
  - a. general-purpose.
  - b. macro-reports.
  - c. special-purpose.
  - d. classified financial statements.
  
42. The reporting standard for external financial reports is
  - a. industry-specific.
  - b. company-specific.
  - c. generally accepted accounting principles.
  - d. department-specific.
  
43. Which of the following statements about internal reports is not true?
  - a. The content of internal reports may extend beyond the double-entry accounting system.
  - b. Internal reports may show all amounts at market values.
  - c. Internal reports may discuss prospective events.
  - d. Most internal reports are summarized rather than detailed.
  
44. In an analogous sense, external user is to internal user as generally accepted accounting principles are to
  - a. timely.
  - b. special-purpose.
  - c. relevance to decision.
  - d. SEC.
  
45. Internal reports are generally
  - a. aggregated.
  - b. detailed.
  - c. regulated.
  - d. unreliable.
  
46. Planning is a function that involves
  - a. hiring the right people for a particular job.
  - b. coordinating the accounting information system.
  - c. setting goals and objectives for an entity.
  - d. analyzing financial statements.

47. The managerial function of controlling
- is performed only by the controller of a company.
  - is only applicable when the company sustains a loss.
  - is concerned mainly with operating a manufacturing segment.
  - includes performance evaluation by management.
48. Which of the following is not a management function?
- Constraining
  - Planning
  - Controlling
  - Directing and motivating
49. A manager that is establishing objectives is performing which management function?
- Motivating
  - Directing
  - Planning
  - Constraining
50. The document of an organization that depicts authority relationships within the company is the
- organization's charter.
  - organization's indenture.
  - organization chart.
  - authority outline.
51. In determining whether planned goals are being met, a manager is performing the function of
- planning.
  - follow-up.
  - motivating.
  - controlling.
52. Which of the following is not a separate management function?
- Planning
  - Motivating
  - Decision-making
  - Controlling
53. Both direct materials and indirect materials are
- raw materials.
  - manufacturing overhead.
  - merchandise inventory.
  - sold directly to customers by a manufacturing company.
54. The work of factory employees that can be physically and directly associated with converting raw materials into finished goods is
- manufacturing overhead.
  - indirect materials.
  - indirect labor.
  - direct labor.

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55. Which one of the following would not be classified as manufacturing overhead?
- Indirect labor
  - Direct materials
  - Insurance on factory building
  - Indirect materials
56. In manufacturing a product, prime costs are
- raw materials and manufacturing overhead.
  - direct materials and manufacturing overhead.
  - direct labor and manufacturing overhead.
  - direct materials and direct labor.
57. Product costs which are considered conversion costs are direct
- materials and direct labor.
  - labor and manufacturing overhead.
  - materials and indirect labor.
  - materials and manufacturing overhead.
58. Which one of the following is not a cost element in manufacturing a product?
- Manufacturing overhead
  - Direct materials
  - Office salaries
  - Direct labor
59. A manufacturing process requires small amounts of glue. The glue used in the production process is classified as
- a prime cost.
  - an indirect material.
  - a direct material.
  - miscellaneous expense.
60. The wages of a timekeeper in the factory would be classified as
- a prime cost.
  - direct labor.
  - indirect labor.
  - compliance costs.
61. Which of the following is not a manufacturing cost category?
- Cost of goods sold
  - Direct materials
  - Direct labor
  - Manufacturing overhead
62. As current technology changes manufacturing processes, it is likely that direct
- labor will increase.
  - labor will decrease.
  - materials will increase.
  - materials will decrease.
63. For the work of factory employees to be considered as direct labor, the work must be

- conveniently and
- a. materially associated with raw material conversion.
  - b. periodically associated with raw material conversion.
  - c. physically associated with raw material conversion.
  - d. promptly associated with raw material conversion.
64. Which of the following is not classified as direct labor?
- a. Bottlers of beer in a brewery
  - b. Copy machine operators at a copy shop
  - c. Wages of supervisors
  - d. Bakers in a bakery
65. Cotter pins and lubricants used irregularly in a production process are classified as
- a. miscellaneous expense.
  - b. direct materials.
  - c. indirect materials.
  - d. nonmaterial materials.
66. Which of the following is not another name for the term manufacturing overhead?
- a. Factory overhead
  - b. Pervasive costs
  - c. Burden
  - d. Indirect manufacturing costs
67. Because of automation, which component of product cost is declining?
- a. Direct labor
  - b. Direct materials
  - c. Manufacturing overhead
  - d. Advertising
68. The product cost that is most difficult to associate with a product is
- a. direct materials.
  - b. direct labor.
  - c. manufacturing overhead.
  - d. advertising.
69. Manufacturing costs that cannot be classified as either direct materials or direct labor are known as
- a. period costs.
  - b. nonmanufacturing costs.
  - c. selling and administrative expenses.
  - d. manufacturing overhead.
70. Which one of the following costs would not be inventoriable?
- a. Period costs
  - b. Prime costs
  - c. Conversion costs
  - d. Indirect labor costs
71. Prime costs of a company are \$3,000,000, manufacturing overhead is \$1,500,000 and direct labor is \$750,000. What is the amount of direct materials?

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- a. \$1,500,000.
  - b. \$750,000.
  - c. \$2,250,000.
  - d. Cannot be determined from the information provided.
72. Prime costs of a company are \$6,000,000. If manufacturing overhead is \$3,000,000, what is direct labor cost?
- a. \$3,000,000.
  - b. \$6,000,000.
  - c. \$0.
  - d. Cannot be determined from the information provided.
73. Which of the following are period costs?
- a. Raw materials
  - b. Prime costs
  - c. Conversion costs
  - d. Selling expenses
74. Sales commissions are classified as
- a. prime costs.
  - b. period costs.
  - c. product costs.
  - d. indirect labor.
75. Product costs consist of
- a. conversion costs and unexpired expenses.
  - b. prime costs and manufacturing overhead.
  - c. selling and administrative expenses.
  - d. period costs.
76. Product costs are also called
- a. direct costs.
  - b. prime costs.
  - c. inventoriable costs.
  - d. capitalizable costs.
77. For inventoriable costs to become expenses under the matching principle,
- a. the product must be finished and in stock.
  - b. the product must be expensed based on its percentage-of-completion.
  - c. the product to which they attach must be sold.
  - d. all accounts payable must be settled.
78. As inventoriable costs expire, they become
- a. selling expenses.
  - b. gross profit.
  - c. cost of goods sold.
  - d. sales revenue.

79. Conversion costs include
- direct materials and manufacturing overhead.
  - direct labor and manufacturing overhead.
  - direct materials and direct labor.
  - manufacturing overhead and selling expenses.
80. A manufacturing company calculates cost of goods sold as follows:
- Beginning FG inventory + cost of goods purchased – ending FG inventory.
  - Ending FG inventory – cost of goods manufactured + beginning FG inventory.
  - Beginning FG inventory – cost of goods manufactured – ending FG inventory.
  - Beginning FG inventory + cost of goods manufactured – ending FG inventory.
81. A manufacturing company reports cost of goods manufactured as
- a current asset on the balance sheet.
  - an administrative expense on the income statement.
  - a component in the calculation of cost of goods sold on the income statement.
  - a component of the raw materials inventory on the balance sheet.
82. The subtotal, "Cost of goods manufactured" appears on
- a merchandising company's income statement.
  - a manufacturing company's income statement.
  - both a manufacturing and a merchandising company's income statement.
  - neither a merchandising nor a manufacturing company's income statement.
83. Cost of goods manufactured in a manufacturing company is analogous to
- Ending inventory in a merchandising company.
  - Beginning inventory in a merchandising company.
  - Cost of goods available for sale in a merchandising company.
  - Cost of goods purchased in a merchandising company.
84. Cost of goods sold
- only appears on merchandisers' income statements.
  - only appears on manufacturers' income statements.
  - appears on both manufacturers' and merchandisers' income statements.
  - is calculated exactly the same for merchandisers and manufacturers.
85. Cost of goods manufactured is calculated as follows:
- Beginning WIP + direct materials used + direct labor + manufacturing overhead + ending WIP.
  - Direct materials used + direct labor + manufacturing overhead – beginning WIP + ending WIP.
  - Beginning WIP + direct materials used + direct labor + manufacturing overhead – ending WIP.
  - Direct materials used + direct labor + manufacturing overhead – ending WIP – beginning WIP.
86. If the amount of "Cost of goods manufactured" during a period exceeds the amount of "Total manufacturing costs" for the period, then
- Ending work in process inventory is greater than or equal to the amount of the beginning work in process inventory.
  - Ending work in process is greater than the amount of the beginning work in process inventory.
  - Ending work in process is equal to the cost of goods manufactured.
  - Ending work in process is less than the amount of the beginning work in process inventory.

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- 0 87. On the costs of goods manufactured schedule, depreciation on factory equipment
- is not listed because it is included with Depreciation Expense on the income statement.
  - appears in the manufacturing overhead section.
  - is not listed because it is not a product cost.
  - is not an inventoriable cost.
88. On the costs of goods manufactured schedule, the item raw materials inventory (ending) appears as
- an addition to raw materials purchases.
  - an addition to raw materials available for use.
  - a subtraction from raw materials available for use.
  - a subtraction from raw material purchases.

Use the following information for questions 89–91.

Craft Manufacturing Company's accounting records reflect the following inventories:

	<u>Dec. 31, 2002</u>	<u>Dec. 31, 2001</u>
Raw materials inventory	\$310,000	\$260,000
Work in process inventory	300,000	160,000
Finished goods inventory	190,000	150,000

During 2002, \$500,000 of raw materials were purchased, direct labor costs amounted to \$600,000, and manufacturing overhead incurred was \$480,000.

89. The total raw materials available for use during 2002 for Craft Manufacturing Company is
- \$810,000.
  - \$260,000.
  - \$450,000.
  - \$760,000.
90. Craft Manufacturing Company's total manufacturing costs incurred in 2002 amounted to
- \$1,530,000.
  - \$1,490,000.
  - \$1,390,000.
  - \$1,580,000.
91. If Craft Manufacturing Company's cost of goods manufactured for 2002 amounted to \$1,390,000, its cost of goods sold for the year is
- \$1,500,000.
  - \$1,250,000.
  - \$1,350,000.
  - \$1,430,000.
92. Stevens Manufacturing Company reported the following year-end information: beginning work in process inventory, \$180,000; cost of goods manufactured, \$516,000; beginning finished goods inventory, \$252,000; ending work in process inventory, \$220,000; and ending finished goods inventory, \$264,000. Stevens Manufacturing Company's cost of goods sold for the year is
- \$504,000.
  - \$528,000.
  - \$476,000.
  - \$252,000.

93. Nolte Manufacturing Company reported the following year-end information:

Beginning work in process inventory	\$360,000
Beginning raw materials inventory	100,000
Ending work in process inventory	300,000
Ending raw materials inventory	160,000
Raw materials purchased	320,000
Direct labor	300,000
Manufacturing overhead	200,000

Nolte Manufacturing Company's cost of goods manufactured for the year is

- a. \$760,000.
  - b. \$820,000.
  - c. \$700,000.
  - d. \$880,000.
94. The sum of the direct materials costs, direct labor costs, and manufacturing overhead incurred in the current year is the
- a. cost of goods manufactured.
  - b. cost of goods available for sale.
  - c. total cost of work in process.
  - d. total manufacturing cost.
95. The sum of the cost of the beginning work in process and the total manufacturing costs for the current period is the
- a. cost of goods manufactured.
  - b. cost of goods available for sale.
  - c. total cost of work in process.
  - d. cost of goods sold.
96. Total manufacturing costs consist of
- a. direct materials and direct labor only.
  - b. direct labor and manufacturing overhead only.
  - c. manufacturing overhead only.
  - d. direct materials, direct labor, and manufacturing overhead.
97. Which one of the following does not appear on the balance sheet of a manufacturing company?
- a. Finished goods inventory
  - b. Work in process inventory
  - c. Cost of goods manufactured
  - d. Raw materials inventory
98. The equivalent of finished goods inventory for a merchandising firm is referred to as
- a. purchases.
  - b. cost of goods purchased.
  - c. merchandise inventory.
  - d. raw materials inventory.

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- 2 99. Manufacturing inventories are generally listed in
- alphabetical order.
  - order of their liquidity.
  - order from largest to smallest.
  - any order the company desires.
100. The term that describes all activities associated with providing a product or service is the
- manufacturing chain.
  - product chain.
  - supply chain.
  - value chain.
101. Many companies manage their value chain by using
- activity-based costing.
  - enterprise resource planning systems.
  - just-in-time methods.
  - total quality management systems.
102. Many companies have significantly lowered inventory levels and costs using
- activity-based costing.
  - an enterprise resource planning system.
  - the just-in-time method.
  - a total quality management system.
103. Systems implemented to reduce defects in finished products with the goal of achieving zero defects are
- activity-based costing systems.
  - enterprise resource planning systems.
  - value chain systems.
  - total quality management systems.
104. In order to obtain more accurate product costs, many companies now allocate overhead using
- activity-based costing.
  - enterprise resource planning systems.
  - just-in-time methods.
  - total quality management systems.
105. Many companies can now manufacture products that are untouched by human hands through
- activity-based costing.
  - computer-integrated manufacturing.
  - enterprise resource planning systems.
  - total quality management systems.
- \*106. In preparing a work sheet for a manufacturing company, the account Indirect Labor, is extended to the
- Adjustment columns.
  - Income Statement columns.
  - Cost of Goods Manufactured columns.
  - Balance Sheet columns.

- \*107. In order to balance the cost of goods manufactured columns of a manufacturing company's work sheet, the offsetting entry is in the
- balance sheet debit column.
  - income statement debit column.
  - balance sheet credit column.
  - income statement credit column.
- \*108. Which of the following accounts would not appear in the cost of goods manufactured columns of a work sheet?
- Beginning Raw Materials Inventory
  - Ending Finished Goods Inventory
  - Ending Work in Process Inventory
  - Direct Labor
- \*109. When making closing entries for a manufacturing company, all accounts that appear on the cost of goods manufactured schedule are closed to the
- Income Summary account.
  - Materials, Labor, and Overhead accounts.
  - Manufacturing Summary account.
  - Finished Goods Inventory account.
- \*110. The Income Summary account of a manufacturing corporation is closed to the
- Retained Earnings account.
  - Manufacturing Summary account.
  - Finished Goods Inventory account.
  - Work in Process Inventory account.

**Answers to Multiple Choice Questions**

Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.	Item	Ans.
31.	c	43.	d	55.	b	67.	a	79.	b	91.	c	103.	d
32.	b	44.	c	56.	d	68.	c	80.	d	92.	a	104.	a
33.	a	45.	b	57.	b	69.	d	81.	c	93.	b	105.	b
34.	a	46.	c	58.	c	70.	a	82.	b	94.	d	*106.	c
35.	a	47.	d	59.	b	71.	c	83.	d	95.	c	*107.	b
36.	b	48.	a	60.	c	72.	d	84.	c	96.	d	*108.	b
37.	d	49.	c	61.	a	73.	d	85.	c	97.	c	*109.	c
38.	b	50.	c	62.	b	74.	b	86.	d	98.	c	*110.	a
39.	d	51.	d	63.	c	75.	b	87.	b	99.	b		
40.	b	52.	c	64.	c	76.	c	88.	c	100.	d		
41.	c	53.	a	65.	c	77.	c	89.	d	101.	b		
42.	c	54.	d	66.	b	78.	c	90.	a	102.	c		

## EXERCISES

### Ex. 111

Financial accounting information and managerial accounting information have a number of distinguishing characteristics. For each of the characteristics listed below, indicate which characteristics are more closely related to financial accounting by placing the letter "F" in the space to the left of the item and indicate those characteristics which are more closely associated with managerial accounting by placing the letter "M" to the left of the item.

- 1. General-purpose reports
- 2. Reports are used internally
- 3. Prepared in accordance with generally accepted accounting principles
- 4. Special purpose reports
- 5. Limited to historical cost data
- 6. Reporting standard is relevant to the decision to be made
- 7. Classified financial statements
- 8. Reports generally pertain to the company as a whole
- 9. Reports generally pertain to subunits
- 10. Reports issued quarterly or annually

### Solution 111 (7–11 min.)

- |      |       |
|------|-------|
| 1. F | 6. M  |
| 2. M | 7. F  |
| 3. F | 8. F  |
| 4. M | 9. M  |
| 5. F | 10. F |

**Ex. 112**

Presented below is a list of costs and expenses incurred in the factory by Nu-Way Corporation, a manufacturer of recreational vehicles.

- \_\_\_ 1. Property taxes on the factory land
- \_\_\_ 2. Metal used in manufacturing
- \_\_\_ 3. Cabinet maker's wages
- \_\_\_ 4. Nails and glue used in production
- \_\_\_ 5. Factory supervisors' salaries
- \_\_\_ 6. Depreciation on factory machines
- \_\_\_ 7. Factory utilities
- \_\_\_ 8. Carpeting for the recreational vehicles
- \_\_\_ 9. Property taxes on the factory building
- \_\_\_ 10. Insurance on factory equipment

**Instructions**

Classify the above items into the following categories:

- DM — Direct Materials
- DL — Direct Labor
- MO — Manufacturing Overhead

**Solution 112** (8–10 min.)

- 1. MO
- 2. DM
- 3. DL
- 4. MO
- 5. MO
- 6. MO
- 7. MO
- 8. DM
- 9. MO
- 10. MO

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**6 Ex. 113**

For each item, identify all applicable cost labels. Use the following code in your answer:

- 1 — Prime Cost
- 2 — Conversion Cost
- 3 — Product Cost
- 4 — Period Cost

- a. Advertising \_\_\_\_\_
- b. Direct materials used \_\_\_\_\_
- c. Sales salaries \_\_\_\_\_
- d. Indirect factory labor \_\_\_\_\_
- e. Repairs to office equipment \_\_\_\_\_
- f. Factory manager's salary \_\_\_\_\_
- g. Direct labor used \_\_\_\_\_
- h. Indirect materials \_\_\_\_\_

**Solution 113** (6–9 min.)

- a. Advertising 4
- b. Direct materials used 1, 3
- c. Sales salaries 4
- d. Indirect factory labor 2, 3
- e. Repairs to office equipment 4
- f. Factory manager's salary 2, 3
- g. Direct labor used 1, 2, 3
- h. Indirect materials 2, 3

**Ex. 114**

Assume you have just taken a position as controller for a new company that manufactures and sells wooden chairs. Although the founder of the company, who is the president and CEO, is a great artisan, she has very limited knowledge of accounting. To help your new boss better understand accounting for a manufacturing organization, write a memo to her in which you: (1) identify, (2) describe, and (3) provide examples of the three manufacturing costs and the three inventory accounts used in accounting for a manufacturing company.

**Solution 114** (6–9 min.)

The three manufacturing costs are: Direct Materials, Direct Labor, and Manufacturing Overhead. Raw materials that can be physically and directly associated with the finished product during the manufacturing process are called direct materials. The wood used in making the chairs is an example of direct materials. The work of factory employees that can be physically and directly associated with converting raw materials to finished goods is considered direct labor. Manufacturing overhead consists of costs that are indirectly associated with the manufacture of the finished product. These costs may also be manufacturing costs that cannot be classified as direct materials or direct labor. Manufacturing overhead includes indirect materials, indirect labor, and depreciation on factory buildings, and machinery, utilities, insurance, taxes and maintenance on factory facilities.

The three inventory accounts are: raw materials, work in process, and finished goods. Raw materials inventory represents the cost of the materials and parts that are to be used in the manufacturing process. The wood purchased to make the chairs would be considered raw materials until the time it was put into production. Work in process is the cost applicable to units that have been started into production but are only partially complete. Chairs on the assembly line that are in various stages of completion would be work in process. The finished goods inventory represents the cost of completed goods that have not been sold. The cost of chairs that are completed but have not been sold would be finished goods.

**Ex. 115**

For each item listed below, indicate in the space to the left whether the item would be considered an inventoriable cost or a period cost for a manufacturing company. Use the following code:

I = Inventoriable cost  
P = Period cost

- \_\_\_\_\_ 1. Factory supervisory salaries
- \_\_\_\_\_ 2. Sales commissions
- \_\_\_\_\_ 3. Income tax expense
- \_\_\_\_\_ 4. Indirect materials used
- \_\_\_\_\_ 5. Indirect labor
- \_\_\_\_\_ 6. Office salaries expense
- \_\_\_\_\_ 7. Property taxes on factory building
- \_\_\_\_\_ 8. Sales manager's salary
- \_\_\_\_\_ 9. Factory wages expense
- \_\_\_\_\_ 10. Direct materials used

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8 Solution 115 (7–10 min.)

1. I
2. P
3. P
4. I
5. I
6. P
7. I
8. P
9. I
10. I

Ex. 116

Yates Manufacturing Company incurs the following manufacturing costs and expenses during the month of May.

1. Assembly line wages
2. Raw materials used directly in product
3. Depreciation on office equipment
4. Property taxes on factory building
5. Rent on factory building
6. Sales commissions
7. Depreciation on factory equipment
8. Factory utilities
9. Wages for factory maintenance workers
10. Advertising
11. Indirect materials used in production
12. Factory manager's salary

**Instructions**

Complete the following matrix by placing an X mark under the appropriate headings.

<u>Cost Item</u>	<u>Direct Materials</u>	<u>Direct Labor</u>	<u>Manufacturing Overhead</u>	<u>Prime Costs</u>	<u>Conversion Costs</u>	<u>Period Costs</u>
1.						
2.						
3.						
4.						
5.						
6.						
7.						
8.						
9.						
10.						
11.						
12.						

**Solution 116** (10–15 min.)

<u>Cost Item</u>	<u>Direct Materials</u>	<u>Direct Labor</u>	<u>Manufacturing Overhead</u>	<u>Prime Costs</u>	<u>Conversion Costs</u>	<u>Period Costs</u>
1.		X		X	X	
2.	X			X		
3.						X
4.			X		X	
5.			X		X	
6.						X
7.			X		X	
8.			X		X	
9.			X		X	
10.						X
11.			X		X	
12.			X		X	

**Ex. 117**

Among the items that Lane Print Shop accounts for are the following:

1. Direct labor \_\_\_\_\_
2. Office supplies used \_\_\_\_\_
3. Depreciation on printing machines \_\_\_\_\_
4. Finished goods inventory, 12/31 \_\_\_\_\_
5. Raw materials inventory, 1/1 \_\_\_\_\_
6. Cost of goods manufactured \_\_\_\_\_
7. Work in process, 1/1 \_\_\_\_\_
8. Office supplies inventory, 12/31 \_\_\_\_\_
9. Indirect labor \_\_\_\_\_
10. Heat and electricity for the print shop \_\_\_\_\_

Lane prepares the following schedule and financial statements on a yearly basis:

- (a) Cost of goods manufactured schedule.
- (b) Income statement.
- (c) Balance sheet.

**Instructions**

For each item, indicate by using the appropriate letter(s) the schedule and/or financial statements in which the item will appear.

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**0 Solution 117** (8–12 min.)

- |   |                                   |
|---|-----------------------------------|
| 1. Direct labor                             | <u>          (a)          </u>    |
| 2. Office supplies used                     | <u>          (b)          </u>    |
| 3. Depreciation on printing machines        | <u>          (a)          </u>    |
| 4. Finished goods inventory, 12/31          | <u>         (b), (c)         </u> |
| 5. Raw materials inventory, 1/1             | <u>          (a)          </u>    |
| 6. Cost of goods manufactured               | <u>         (a), (b)         </u> |
| 7. Work in process, 1/1                     | <u>          (a)          </u>    |
| 8. Office supplies inventory, 12/31         | <u>          (c)          </u>    |
| 9. Indirect labor                           | <u>          (a)          </u>    |
| 10. Heat and electricity for the print shop | <u>          (a)          </u>    |

**Ex. 118**

Jordan Company manufactures boats. During September, 2002, the company purchased 100 cellular phones at a cost of \$150 each. Jordan withdrew 70 phones from the warehouse during the month. Twenty of these phones were installed in salesmen's cars and the remaining 50 phones were put in boats manufactured during the month.

Of the boats put into production during September, 2002, 80% were completed and transferred to the company's storage lot. Fifty percent of the boats completed during the month were sold by September 30.

**Instructions**

Determine the cost of cellular phones that would appear in each of the following accounts at September 30, 2002:

Raw materials inventory  
Work in process inventory  
Finished goods inventory  
Cost of goods sold  
Selling expenses

**Solution 118** (12–17 min.)

Raw materials:	$(100 - 70) \times \$150 = \$4,500$
Work in process:	$(50 \times 20\%) \times \$150 = \$1,500$
Finished goods:	$(50 \times 80\% \times 50\%) \times \$150 = \$3,000$
Cost of goods sold:	$(50 \times 80\% \times 50\%) \times \$150 = \$3,000$
Selling expenses:	$20 \times \$150 = \$3,000$

Costs to account for:  $100 \times \$150 = \$15,000$

Raw materials inventory	\$ 4,500
Work in process inventory	1,500
Finished goods inventory	3,000
Cost of goods sold	3,000
Selling expenses	<u>3,000</u>
Total	<u>\$15,000</u>

**Ex. 119**

Klugman Manufacturing Company has the following data at June 30, 2002:

Raw materials inventory, June 1	\$ 13,800
Work in process inventory, June 1	18,100
Finished goods inventory, June 1	43,500
Total manufacturing costs	450,000
Sales	590,000
Work in process inventory, June 30	30,400
Finished goods inventory, June 30	60,200
Raw materials inventory, June 30	18,000

**Instructions**

- (a) Prepare an income statement through gross profit for the month of June.
- (b) Indicate the balance sheet presentation of the June 30 inventories.

**Solution 119** (10–15 min.)

(a) **KLUGMAN MANUFACTURING COMPANY**  
(Partial) Income Statement  
For the Month Ended June 30, 2002

Sales .....		\$590,000
Cost of good sold		
Finished goods inventory, June 1 .....	\$ 43,500	
Cost of goods manufactured .....	<u>437,700*</u>	
Cost of goods available for sale .....	481,200	
Finished goods inventory, June 30 .....	<u>60,200</u>	
Cost of goods sold .....		<u>421,000</u>
Gross profit .....		<u>\$169,000</u>

\*\$18,100 + \$450,000 – \$30,400 = \$437,700

(b) **KLUGMAN MANUFACTURING COMPANY**

Current assets		
Cash .....		\$ XXXX
Accounts receivable .....		XXXX
Inventories:		
Finished goods .....	\$60,200	
Work in process .....	30,400	
Raw materials .....	<u>18,000</u>	108,600

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2 Ex. 120

From the account balances listed below, prepare a schedule of cost of goods manufactured for Reagan Manufacturing Company for the month ended December 31, 2002.

	<u>Account Balances</u>
Finished Goods Inventory, December 31	\$42,000
Factory Supervisory Salaries	12,000
Income Tax Expense	18,000
Raw Materials Inventory, December 1	12,000
Work In Process Inventory, December 31	35,000
Sales Salaries Expense	14,000
Factory Depreciation Expense	5,000
Finished Goods Inventory, December 1	35,000
Raw Materials Purchases	60,000
Work In Process Inventory, December 1	30,000
Factory Utilities Expense	4,000
Direct Labor	70,000
Raw Materials Inventory, December 31	19,000
Sales Returns and Allowances	5,000
Indirect Labor	21,000

**Solution 120** (12–16 min.)

REAGAN MANUFACTURING COMPANY  
Cost of Goods Manufactured Schedule  
For the Month Ended December 31, 2002

Work in process, December 1	\$ 30,000
Direct materials	
Raw materials inventory, December 1	\$12,000
Raw materials purchases	<u>60,000</u>
Total raw materials available for use	72,000
Less: Raw materials inventory, December 31	<u>19,000</u>
Direct materials used	53,000
Direct labor	70,000
Manufacturing overhead	
Indirect labor	\$21,000
Factory supervisory salaries	12,000
Factory depreciation expense	5,000
Factory utilities expense	<u>4,000</u>
Total manufacturing overhead	<u>42,000</u>
Total manufacturing costs	<u>165,000</u>
Total cost of work in process	195,000
Less: Work in process, December 31	<u>35,000</u>
Cost of goods manufactured	<u>\$160,000</u>

**Ex. 121**

Loggia Manufacturing Company has developed the following information for the year ended December 31, 2002:

Work In Process Inventory, December 31	\$150,000
Total manufacturing costs incurred during the year	660,000
Raw Materials Purchases	190,000
Raw Materials Inventory, December 31	65,000
Prime manufacturing costs for the year	350,000
Conversion costs for the year	400,000

The Work In Process Inventory on January 1, 2002 was 80% of the Work In Process Inventory on December 31, 2002.

**Instructions**

Prepare a Cost of Goods Manufactured Schedule for Loggia Manufacturing Company for the year ended December 31, 2002.

**Solution 121** (13–17 min.)

LOGGIA MANUFACTURING COMPANY  
Cost of Goods Manufactured Schedule  
For the Year Ended December 31, 2002

Work in process, January 1 (a)		\$120,000
Direct materials		
Raw materials inventory, January 1 (f)	\$135,000	
Raw materials purchased (given)	<u>190,000</u>	
Total raw materials available for use (e)	325,000	
Less: Raw materials inventory, December 31 (given)	<u>65,000</u>	
Direct materials used (d)	260,000	
Direct labor (c)	90,000	
Manufacturing overhead (b)	<u>310,000</u>	
Total manufacturing costs (given)		<u>660,000</u>
Total cost of work in process		780,000
Less: Work in process, December 31 (given)		<u>150,000</u>
Cost of goods manufactured		<u>\$630,000</u>

- (a)  $\$150,000 \times 80\% = \$120,000$ .
- (b)  $\$660,000 - \$350,000 = \$310,000$ .
- (c)  $\$400,000 - \$310,000 = \$90,000$ .
- (d)  $\$660,000 - \$310,000 - \$90,000 = \$260,000$ .
- (e)  $\$65,000 + \$260,000 = \$325,000$ .
- (f)  $\$325,000 - \$190,000 = \$135,000$ .

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4 Ex. 122

Manufacturing costs for Carson Company for selected months are as follows:

	<u>April</u>	<u>July</u>	<u>October</u>
Beginning work in process	\$ 80,000	(f)	\$ 98,000
Direct materials used	280,000	\$190,000	155,000
Direct labor	195,000	170,000	(j)
Manufacturing overhead	(a)	150,000	90,000
Total manufacturing costs	870,000	510,000	430,000
Total cost of work in process	(b)	640,000	(k)
Ending work in process	75,000	(g)	(l)
Cost of goods manufactured	(c)	505,000	385,000
Beginning finished goods	(d)	38,000	(m)
Cost of goods available for sale	960,000	(h)	480,000
Ending finished goods	(e)	75,000	(n)
Cost of goods sold	820,000	(i)	355,000

**Instructions**

Indicate the missing amounts. (Show computations.)

**Solution 122** (12–17 min.)

- (a) \$395,000 (\$870,000 – \$280,000 – \$195,000).
- (b) \$950,000 (\$870,000 + \$80,000).
- (c) \$875,000 (\$950,000 – \$75,000).
- (d) \$85,000 (\$960,000 – \$875,000).
- (e) \$140,000 (\$960,000 – \$820,000).
- (f) \$130,000 (\$640,000 – \$510,000).
- (g) \$135,000 (\$640,000 – \$505,000).
- (h) \$543,000 (\$505,000 + \$38,000).
- (i) \$468,000 (\$543,000 – \$75,000).
- (j) \$185,000 (\$430,000 – \$90,000 – \$155,000).
- (k) \$528,000 (\$98,000 + \$430,000).
- (l) \$143,000 (\$528,000 – \$385,000).
- (m) \$95,000 (\$480,000 – \$385,000).
- (n) \$125,000 (\$480,000 – \$355,000).

**Ex. 123**

Fill in the missing information on the cost of goods manufactured schedule of Miley Manufacturing Company:

**MILEY MANUFACTURING COMPANY**  
Cost of Goods Manufactured Schedule  
For the Year Ended December 31, 2002

Work in process (1/1)				\$320,000
Direct materials				
Raw materials inventory (1/1)	\$ _____ ?		-	
Raw materials purchases	<u>246,000</u>			
Raw materials available for use	_____ ?			
Raw materials inventory (12/31)	<u>37,000</u>			
Direct materials used		\$235,000		
Direct labor		_____ ?		
Manufacturing overhead				
Indirect labor	19,000			
Factory depreciation	38,000			
Factory utilities	39,000			
Total overhead		_____ ?		
Total manufacturing costs				_____ ?
Total cost of work in process				_____ ?
Less: Work in Process (12/31)				<u>292,000</u>
Cost of goods manufactured				<u>\$440,000</u>

**Solution 123** (6–9 min.)

**MILEY MANUFACTURING COMPANY**  
Cost of Goods Manufactured Schedule  
For the Year Ended December 31, 2002

Work in process (1/1)				\$320,000
Direct materials				
Raw materials inventory (1/1)	\$ 26,000			
Raw materials purchases	<u>246,000</u>			
Raw materials available for use	272,000			
Raw materials inventory (12/31)	<u>37,000</u>			
Direct materials used		\$235,000		
Direct labor		81,000		
Manufacturing overhead				
Indirect labor	19,000			
Factory depreciation	38,000			
Factory utilities	<u>39,000</u>			
Total overhead		<u>96,000</u>		
Total manufacturing costs				<u>412,000</u>
Total cost of work in process				732,000
Less: Work in Process (12/31)				<u>292,000</u>
Cost of goods manufactured				<u>\$440,000</u>

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**6 Ex. 124**

Data for the cost of direct materials for the month ended March 31, 2002, are as follows:

Materials inventory, March 1, 2002	\$76,000
Materials inventory, March 31, 2002	85,000

During March, the company purchased \$200,000 of raw materials on account from Rye Company and \$72,000 of raw materials for cash from Frye Company. In addition, \$50,000 was paid on the Rye account balance.

**Instructions**

Compute the cost of direct materials used during March.

**Solution 124** (5–7 min.)

Raw materials inventory, March 1	\$ 76,000
Raw materials purchases (\$200,000 + \$72,000)	<u>272,000</u>
Total raw materials available for use	348,000
Less: Raw materials inventory, March 31	<u>85,000</u>
Direct materials used during March	<u>\$263,000</u>

Note: Payment on account to Rye is irrelevant to the direct materials used calculation.

**Ex. 125**

CinMark, the manufacturer of inexpensive printers, was organized in September 2002. CinMark purchases the toner cartridges used in the printers from a local distributor. Early in September, CinMark bought 50,000 cartridges at a cost of \$20 each. During September, 40,000 cartridges were transferred from Raw Materials Inventory. Of the 40,000 cartridges withdrawn from Raw Materials Inventory, 8,000 were given to sales personnel to be given to customers as an incentive to buy a large quantity of printers. Another 2,000 cartridges were transferred to the corporate office to be used by members of the clerical staff. The remaining 30,000 cartridges were transferred to Work in Process Inventory. Of the units started into production during September, 90 percent of them were completed. Seventy percent of the units completed during September were sold and shipped to customers.

**Instructions**

Determine the cost of cartridges to be found in each of the following accounts:

- Raw Materials Inventory
- Work in Process Inventory
- Finished Goods Inventory
- Cost of Goods Sold
- Selling Expenses
- Administrative Expenses

**Solution 125** (8–10 min.)

a. Raw Materials Inventory	$(50,000 - 40,000) \times \$20 =$	\$ 200,000
b. Work in Process Inventory	$(30,000 \times .10) \times \$20 =$	60,000
c. Finished Goods Inventory	$(30,000 \times .90) = 27,000$ $(27,000 \times .30) = 8,100$ $(8,100 \times \$20) =$	162,000
d. Cost of Goods Sold	$(30,000 \times .90) = 27,000$ $(27,000 \times .70) = 18,900$ $(18,900 \times \$20) =$	378,000
e. Selling Expenses	$(8,000 \times \$20) =$	160,000
f. Administrative Expenses	$(2,000 \times \$20) =$	<u>40,000</u>
		<u>\$1,000,000</u>

**Ex. 126**

The following costs and inventory data were taken from the accounts of Hatfield Company as of December 31, 2002:

	<u>January 1, 2002</u>	<u>December 31, 2002</u>
Inventories:		
Raw materials	\$10,000	\$ 9,000
Work in process	12,000	15,000
Finished goods	8,500	7,500
Costs incurred:		
Raw materials purchases		\$60,000
Direct labor		45,000
Factory rent		25,000
Factory utilities		4,000
Indirect materials		7,000
Indirect labor		5,000
Selling expenses		6,000
Administrative expenses		8,000

**Instructions**

- Prepare a schedule showing the amount of direct materials used in production during the year.
- Compute the amount of manufacturing overhead incurred during the year.
- Prepare a schedule of Cost of Goods Manufactured for Hatfield Company for the year ended December 31, 2002 in good form.
- Prepare the Cost of Goods Sold section of the Income Statement for Hatfield Company for the year ended December 31, 2002 in good form.

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8 **Solution 126** (18–20 min.)

a. **Schedule of Direct Materials Used**

Raw materials inventory, January 1	\$10,000
Raw materials purchases	<u>60,000</u>
Total raw materials available for use	\$70,000
Less: Raw materials inventory, December 31	<u>9,000</u>
Direct materials used	<u>\$61,000</u>

b. **Manufacturing overhead:**

Factory rent	\$25,000
Factory utilities	4,000
Indirect materials	7,000
Indirect labor	<u>5,000</u>
Total manufacturing overhead	<u>\$41,000</u>

c. **HATFIELD COMPANY**  
**Schedule of Cost of Goods Manufactured**  
**For the Year Ended December 31, 2002**

Work in process, January 1		\$ 12,000
Direct materials		
Raw materials inventory, January 1	\$10,000	
Raw materials purchases	<u>60,000</u>	
Total raw materials available for use	\$70,000	
Less: Raw materials inventory, Dec. 31	<u>9,000</u>	
Direct materials used		\$61,000
Direct labor		45,000
Manufacturing overhead		
Factory rent	\$25,000	
Factory utilities	4,000	
Indirect materials	7,000	
Indirect labor	<u>5,000</u>	
Total manufacturing overhead		41,000
Total manufacturing costs		<u>147,000</u>
Total cost of work in process		159,000
Less: Work in process, December 31		<u>15,000</u>
Cost of goods manufactured		<u>\$144,000</u>

d. **HATFIELD COMPANY**  
**(Partial) Income Statement**  
**For the Year Ended December 31, 2002**

Cost of goods sold	
Finished goods inventory, January 1	\$ 8,500
Cost of goods manufactured	<u>144,000</u>
Cost of goods available for sale	152,500
Finished goods inventory, December 31	<u>7,500</u>
Cost of goods sold	<u>\$145,000</u>

**Ex. 127**

Listed below are current asset items for Howell Company at December 31, 2002. Prepare the current assets section of the balance sheet. (Include a complete heading.)

Finished goods inventory	\$30,000	Short-term investments	\$25,000
Cash	20,000	Raw materials inventory	12,000
Prepaid expenses	2,000	Work in process inventory	13,000
Accounts receivable	4,000	Supplies on hand	500

**Solution 127** (6–9 min.)

HOWELL COMPANY  
(Partial) Balance Sheet  
December 31, 2002

Current assets			
Cash			\$20,000
Short-term investments			25,000
Accounts receivable			4,000
Inventories:			
Finished goods	\$30,000		
Work in process	13,000		
Raw materials	<u>12,000</u>		55,000
Prepaid expenses			2,000
Supplies on hand			<u>500</u>
Total current assets			<u>\$106,500</u>

### COMPLETION STATEMENTS

128. Financial accounting information is prepared mainly for \_\_\_\_\_ users while managerial accounting information is prepared primarily for \_\_\_\_\_ users.
129. The types of reports prepared in managerial accounting are often \_\_\_\_\_-purpose reports prepared for a specific decision.
130. Managerial accounting reports generally pertain to \_\_\_\_\_ of an entity and may be very detailed.
131. Three broad managerial functions are: (1) \_\_\_\_\_, (2) \_\_\_\_\_ and \_\_\_\_\_, and (3) \_\_\_\_\_.
132. The \_\_\_\_\_ function is concerned with setting goals and objectives for the entity.
133. Exercising good judgment in performing the managerial functions and choosing among alternative courses of action is called \_\_\_\_\_.
134. The three cost elements in manufacturing a product are (1) \_\_\_\_\_, (2) \_\_\_\_\_, and (3) \_\_\_\_\_.
135. The work of factory employees that can be physically and directly associated with converting raw materials into products is classified as \_\_\_\_\_.
136. Indirect materials and indirect labor are classified as \_\_\_\_\_.
137. Direct materials and direct labor are referred to as \_\_\_\_\_ costs while direct labor and manufacturing overhead are often referred to as \_\_\_\_\_ costs.
138. A major difference between the income statements of a merchandising company and a manufacturing company is that the cost of goods section of a merchandising company shows cost of goods \_\_\_\_\_, whereas a manufacturing company shows cost of goods \_\_\_\_\_.
139. \_\_\_\_\_ is added to direct labor and manufacturing overhead to get total manufacturing costs for the current period.

140. The ending work in process inventory is subtracted from the total cost of work in process to calculate \_\_\_\_\_.
141. A manufacturing company computes cost of goods sold by adding cost of goods manufactured to the \_\_\_\_\_ and subtracting the \_\_\_\_\_.
142. A manufacturing company usually has three inventory accounts which are (1)\_\_\_\_\_, (2)\_\_\_\_\_, and (3)\_\_\_\_\_.

### Answers to Completion Statements

128. external, internal
129. special
130. subunits
131. planning, directing and motivating, controlling
132. planning
133. decision making
134. direct materials, direct labor, manufacturing overhead
135. direct labor
136. manufacturing overhead
137. prime, conversion
138. purchased, manufactured
139. Direct materials used
140. cost of goods manufactured
141. beginning finished goods inventory, ending finished goods inventory
142. Finished Goods Inventory, Work in Process Inventory, Raw Materials Inventory

### MATCHING

143. Match the items in the two columns below by entering the appropriate code letter in the space provided.

- |                              |                           |
|------------------------------|---------------------------|
| A. Managerial accounting     | G. Direct materials       |
| B. Financial accounting      | H. Manufacturing overhead |
| C. Planning                  | I. Period costs           |
| D. Directing and motivating  | J. Prime costs            |
| E. Controlling               | K. Conversion costs       |
| F. Work in process inventory |                           |

- \_\_\_ 1. The cost of products which are partially complete.
- \_\_\_ 2. The function of keeping activities in accordance with plans.
- \_\_\_ 3. Primarily concerned with internal users and reports pertain to subunits of the entity.
- \_\_\_ 4. Materials which can be physically and directly associated with manufacturing a product.
- \_\_\_ 5. The function of setting goals and objectives.
- \_\_\_ 6. Indirect costs of manufacturing a product.
- \_\_\_ 7. Primarily concerned with external users and reports pertain to the entity as a whole.
- \_\_\_ 8. Costs which are noninventoriable.
- \_\_\_ 9. Direct materials and direct labor.
- \_\_\_ 10. The function of coordinating diverse activities and human resources of a company.
- \_\_\_ 11. Direct labor and manufacturing overhead costs incurred in converting raw materials into finished goods.

#### Answers to Matching

- |      |       |
|------|-------|
| 1. F | 7. B  |
| 2. E | 8. I  |
| 3. A | 9. J  |
| 4. G | 10. D |
| 5. C | 11. K |
| 6. H |       |

**SHORT-ANSWER ESSAY QUESTIONS****S-A E 144**

Financial and managerial accounting are both concerned with the economic events of an enterprise. Similarities between financial and managerial accounting do exist, but they do have different focus. Briefly distinguish between financial and managerial accounting as they relate to (1) the primary users, (2) the type and frequency of reports, (3) the purpose of reports, and (4) the content of reports.

**Solution 144**

Financial accounting is primarily concerned with external users such as stockholders and creditors, while the primary users of managerial accounting are those within the company (internal users) such as officers, managers, supervisors, etc. Quarterly and annual classified financial statements are the end product of financial accounting. Internal reports, prepared as often as needed are the result of managerial accounting. The financial statements produced by financial accounting are general-purpose reports which are highly aggregated, pertain to the enterprise as a whole, and are constrained by generally accepted accounting principles. The internal reports prepared by management accountants are special purpose reports which are detailed, pertain to subunits of the enterprise, and may contain any information relevant to the decision at hand.

**S-A E 145**

A manufacturing company makes the products that it sells. Briefly identify and define the cost elements that are incurred in making a product. After product cost elements are identified, how is the cost of goods manufactured for a period determined?

**Solution 145**

Costs incurred to manufacture a product include direct materials which can be physically and directly associated with the finished product; direct labor, which is the work of factory employees which can be physically and directly associated with the finished product; and manufacturing overhead, those manufacturing costs which are indirectly associated with production of the finished product. Cost of goods manufactured is computed by adding the cost of direct materials used, direct labor, and manufacturing overhead to the beginning work in process, and subtracting the ending work in process.

**S-A E 146 (Ethics)**

Million Dollar Mills is a textile manufacturing firm located in the southern United States. The company carefully prepares all financial statements in accordance with GAAP, and gives a copy of all financial statements to each department. In addition, the company keeps records on quality control, safety, and environmental pollution by the company. It then prepares "scorecards" for each department indicating their performance. Recently, the financial impact of the second set of information was added, and the information has been used in the evaluation of employees for merit pay and promotions.

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**4 S-A E 146 (cont.)**

At the most recent employee meeting, Tyler Hanes, marketing manager, expressed his discomfort with the system. He said that there was no guarantee that the second set of information was fair, since there were no generally accepted principles for this kind of information. He also said that it was kind of like keeping two sets of books—one following all legal requirements, and the other one actually used by the company.

**Required:**

1. Is it ethical to evaluate managers in the way described? Explain briefly.
2. Name at least two safeguards the company could build into its system to ensure the ethical treatment of employees.

**Solution 146**

1. It is ethical for a company to use all available data in order to evaluate managers, and even to collect data not routinely available. In fact, such a method seems preferable to one in which the company may only use specified financial data in its evaluation of a manager's performance. It does not imply a departure from GAAP, nor that the company does not actually use the information prepared according to GAAP. It supplements the standard reports, it does not replace them.
2. The company should make certain that the appropriate information is calculated in the same way each period. All the relevant data should be collected and reported each period. New data should be limited. The qualitative information should be complemented, not replaced, by the regular financial information.

**S-A E 147 (Communication)**

Volumetrica, a producer of audio equipment for large computer systems, is reviewing its policies as part of a biannual self-examination of the company. As part of this process, all managers have been asked to carefully examine costs and determine as closely as possible which costs are direct and which are indirect.

Mary Peters and Sam Wilson, managers of different manufacturing departments in the same building, have been working together. They found the following four costs that could be economically traced to the products, but have historically been a part of overhead:

- Cost of setting up the machinery for a different production run.
- Cost of minor assembly components such as knobs and switches.
- Cost of packaging, which is quite different for each model.
- Cost of inspecting and testing each model.

None of the costs is significant by itself, but together these four costs make up between 10 and 15% of the total cost of the product. Mary favors "leaving well enough alone," as she puts it, and leaving these costs in overhead. She is afraid that her volunteering to trace these costs will result in her having to trace many more costs in the future. Sam, on the other hand, prefers to have the product cost as accurate as possible. He points out that these costs are already known, and the process would require little extra work.

**S-A E 147** (cont.)

**Required:**

You have been called on in your function as accounting manager to resolve the dispute. Write a memo to Mary and Sam, supporting one or the other position. Be sure to adequately defend your position, but be brief.

**Solution 147**

TO: Mary Peters and Sam Wilson  
FROM: Mary West, Accounting Manager  
RE: Tracing overhead

I strongly support the tracing of as much of what is now overhead directly to the products as possible (sorry, Mary). Besides giving more accurate product costs now, as Sam says, it will help us considerably in the future. We can evaluate products better, the more we know about which costs they generate. Otherwise, we just assign them some amount of overhead, which may be either more or less than they actually cause.

Thank you both for your hard work. It is true, as Mary says, that our reviews will (temporarily) cause us more work (sorry, Sam). However, I think you'll both agree that the benefits of knowing the costs of our products better will make the effort well worthwhile.

So, let's start tracing the four costs you mentioned now. Once we have the glitches ironed out, we'll share the results with the other departments.

(signed)