In this course we study how accounting information is used in decision making and performance evaluation. The intent is to encourage one to think beyond applying handy recipes and rules. We will often do so by solving examples wherein application of seemingly standard rules will lead to errors. Presumably, the use of information (accounting and otherwise) in decision making and control issues is circumstance specific. Hence, the sooner we develop a habit of critically examining the situation-at-hand and making judgments, the better off we will be.

The above is not to say that the course is bereft of accounting details. In fact, unique accounting topics such as full absorption costing, cost allocations, transfer pricing, CVP analysis, inventory management, capital budgeting, make vs. buy are the underpinnings of the course. A related intent is to see if there are endogenous reasons for accounting rules to develop in the manner they do. For example, is there a reason for a decentralized firm to employ reciprocal cost allocations given such allocations involve (at least somewhat) tedious calculations? Similarly, is transfer pricing a mere exchange issue as far as the firm is concerned and, if not, how can the firm alleviate divisional squabbles? Even more critically, does the firm even want to eliminate all internal frictions in the first place?

A way in which the course differs from (some) standard accounting textbook treatment is that we recognize that "in the real world" there exist interactions among individuals who are differentially informed about the firm. Moreover, managers may benefit by concealing or disguising this private information, to the detriment of the organization as a whole. This approach forces a focus on how managerial control systems (accounting practices and incentive schemes) can mitigate losses to the organization that would otherwise result. The goal here is to provide subtle explanations for observed practices; explanations which may be overlooked if one is not appreciative of the role of private information. As an example, can
rejecting positive NPV projects be optimal for an informationally disadvantaged firm owner? Are there any gains to permitting managers to earn budgetary slack? How does residual income (EVA) compare with a measure such as return on investment in evaluating managerial performance? How do information issues impact a firm's decision to outsource production? And so on.

Class Participation, Grading, and Required Materials

I encourage class participation. During class, I will frequently ask if you have questions, and will sometimes request assistance in working problems. However, I will not insist you come to the board or speak up – presumably, whether or not you choose to volunteer to do so is a valuable signaling instrument in conveying your (private) learning.

Another way to communicate what you have learned is by solving one (take home) group assignment, and one (in-class) individual exam. Working in teams is a skill that is important to a successful career, so the use of a group assignment is in line with such thinking. The individual exam is closed-book and closed-notes. The exam will be held on October 14 (Wednesday) from 8.30 - 10.15 am for both sections of this course in GE 365. If you are unable to take the exam at the assigned time for a valid reason (i.e., one permitted by the University), I will arrange for you to take a make up exam. In such cases please contact me at the earliest.

Your course grade will be calculated as follows: Group Assignment (40%) and Exam (60%). A reasonable question to ask is whether the absence of subjective evaluation (e.g., points for class participation) provides desirable or harmful incentives. But enough with grading and incentives; the desire to learn, by itself, should be sufficient motivation for graduate students.

I will provide you with a course package consisting of lecture notes and several problems; you do not need to purchase any textbook. The notes provided to you of course make use of ideas from many books and research papers. I recommend that (at least over time) you purchase some of these books for your personal library.


In particular, the class notes on cost allocation and transfer pricing (including several of the examples) are borrowed heavily from Zimmerman [1997]. The discussions on aggregation and on control problems are borrowed from Demski [1994] and Zimmerman [1997]; in this regard, papers written by Rick Antle, Brian Mittendorf, Joel Demski, John Fellingham and others were critical, and I will give you precise references when we deal with each topic. Many of the notes are prepared jointly with Rick Young and Jon Glover. Several of the nice problems in the package are written by Joel Demski. So, to Joel, Jon, and Rick our sincere thanks. Finally, helpful comments from colleagues, in particular, John Fellingham, Brian Mittendorf, and Doug Schroeder are gratefully acknowledged.