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Departmental Accounting

DEMONSTRATION PROBLEM

For a number of years, the Security System Department of Strutz Corporation has incurred losses. As a consequence, Strutz's board of directors is considering closing the department. A condensed departmentalized income statement with operating expenses apportioned is shown on the next pages. Allocation data for the fiscal year ended August 31 are presented here.

Expense	Basis of Allocation
Sales Commissions Expense	10 percent of net sales
Depreciation Expense, Store Equipment	Average cost of equipment in use
Advertising Expense	Leaflets distributed by each department portraying the department's products
Miscellaneous Selling Expense	Amount of net sales
Office Salary Expense	Amount of net sales
Officers' Salary Expense	Amount of net sales
Rent Expense	Amount of floor space occupied
Utilities Expense	Amount of floor space occupied
Insurance Expense	Average cost of equipment used, plus average cost of inventory in stock
Miscellaneous General Expense	Amount of net sales

Instructions

1. Prepare a departmentalized income statement showing departmental margin. (Because the departmentalized income statement is so wide, it is impossible to read on a single screen and difficult to interpret when split on two screens. You may want to print out the income statement and tape the pages together for ease of understanding.)
2. Prepare a brief statement of your recommendation to the board regarding the possible closing of the Security System Department.

DEMONSTRATION PROBLEM (continued)

Strutz Corporation

Income Statement

For Year Ended August 31, 20 —

		SECURITY SYSTEM DEPARTMENT		
1	<i>Revenue from Sales:</i>			
2	<i>Sales (net)</i>			\$45,750.00
3	<i>Cost of Goods Sold</i>			30,375.00
4	<i>Gross Profit</i>			\$15,375.00
5				
6	<i>Operating Expenses:</i>			
7	<i>Selling Expenses:</i>			
8	<i>Sales Commissions Expense</i>	\$4,575.00		
9	<i>Advertising Expense</i>	600.00		
10	<i>Depreciation Expense, Store Equipment</i>	1,425.00		
11	<i>Miscellaneous Selling Expense</i>	686.00		
12	<i>Total Selling Expenses</i>		\$ 7,286.00	
13	<i>General Expenses:</i>			
14	<i>Office Salary Expense</i>	\$3,660.00		
15	<i>Officers' Salary Expense</i>	2,745.00		
16	<i>Rent Expense</i>	2,160.00		
17	<i>Utilities Expense</i>	1,620.00		
18	<i>Insurance Expense</i>	1,350.00		
19	<i>Miscellaneous General Expense</i>	460.00		
20	<i>Total General Expenses</i>		11,995.00	
21	<i>Total Operating Expenses</i>			19,281.00
22	<i>Income (Loss) from Operations</i>			(\$ 3,906.00)
23				
24	<i>Other Income:</i>			
25	<i>Interest Income</i>			
26	<i>Income Before Income Tax</i>			
27	<i>Income Tax Expense</i>			
28	<i>Net Income</i>			
29				

DEMONSTRATION PROBLEM (continued)

OTHER DEPARTMENTS			TOTAL		
					1
		\$682,500.00		\$728,250.00	2
		416,250.00		446,625.00	3
		\$266,250.00		\$281,625.00	4
					5
					6
					7
\$ 68,250.00			\$ 72,825.00		8
19,500.00			20,100.00		9
16,125.00			17,550.00		10
10,238.00			10,924.00		11
	\$114,113.00			\$121,399.00	12
					13
\$ 32,631.00			\$ 36,291.00		14
24,617.00			27,362.00		15
15,840.00			18,000.00		16
11,880.00			13,500.00		17
15,075.00			16,425.00		18
6,825.00			7,285.00		19
	106,868.00			118,863.00	20
		220,981.00		240,262.00	21
		\$ 45,269.00		\$ 41,363.00	22
					23
					24
				760.00	25
				\$ 42,123.00	26
				8,447.00	27
				\$ 33,676.00	28
					29

SOLUTION

Strutz Corporation

Income Statement

For Year Ended August 31, 20 —

		SECURITY SYSTEM DEPARTMENT		
1	<i>Revenue from Sales:</i>			
2	<i>Sales (net)</i>			\$45,750.00
3	<i>Cost of Goods Sold</i>			30,375.00
4	<i>Gross Profit</i>			\$15,375.00
5				
6	<i>Direct Departmental Expenses:</i>			
7	<i>Sales Commissions Expense</i>		\$4,575.00	
8	<i>Advertising Expense</i>		600.00	
9	<i>Depreciation Expense, Store Equipment</i>		1,425.00	
10	<i>Insurance Expense</i>		1,350.00	
11	<i>Total Direct Departmental Expenses</i>			7,950.00
12	<i>Departmental Margin</i>			\$ 7,425.00
13				
14	<i>Indirect Expenses:</i>			
15	<i>Office Salary Expense</i>			
16	<i>Officers' Salary Expense</i>			
17	<i>Rent Expense</i>			
18	<i>Utilities Expense</i>			
19	<i>Miscellaneous Selling Expense</i>			
20	<i>Miscellaneous General Expense</i>			
21	<i>Total Indirect Expenses</i>			
22	<i>Income from Operations</i>			
23				
24	<i>Other Income:</i>			
25	<i>Interest Income</i>			
26	<i>Income Before Income Tax</i>			
27	<i>Income Tax Expense</i>			
28	<i>Net Income</i>			
29				

SOLUTION (continued)

OTHER DEPARTMENTS			TOTAL			
						1
		\$682,500.00			\$728,250.00	2
		416,250.00			446,625.00	3
		\$266,250.00			\$281,625.00	4
						5
						6
	\$ 68,250.00			\$72,825.00		7
	19,500.00			20,100.00		10
	16,125.00			17,550.00		8
	15,075.00			16,425.00		9
		118,950.00			126,900.00	10
		\$147,300.00			\$154,725.00	11
						12
						13
				\$36,291.00		14
				27,362.00		15
				18,000.00		16
				13,500.00		17
				10,924.00		18
				7,285.00		19
					113,362.00	20
					\$ 41,363.00	21
						22
						23
					760.00	24
					\$ 42,123.00	25
					8,447.00	26
					\$ 33,676.00	27
						28

When the income statement is departmentalized through departmental margin, it is clear that the Security System Department should not be closed. The department contributed \$7,425 to the firm's operating income. If the Security System Department is closed and no other department takes its place, the firm's operating income will decrease by \$7,425.