Management Accounting

Introduction

Presented by: Ms Shailja Thakur
Designation: Assistant Professor
School of Management
Maharaja Agrasen University

INTRODUCTION

- **Management Accounting** is the presentation of accounting information in such a way as to assist management in the creation of policy and the day-to-day operation of an undertaking. Thus, it relates to the use of accounting data collected with the help of financial accounting and cost accounting for the purpose of policy formulation, planning, control and decision-making by the management.
- Management accounting also is known as managerial accounting and can be defined as a process of providing financial information and resources to the managers in decision making.
- Management accounting is only used by the internal team of the organization, which makes it different from financial accounting.
- In this process, financial information and reports such as invoice, financial balance statement is shared by finance administration with the management team of the company.
- Objective of management accounting is to use this statistical data and take a better and accurate decision, controlling the enterprise, business activities, and development.

Meaning

- Management accounting is the process of identification, measurement, accumulation, analysis, preparation, interpretation, and communication of information that assists executives in fulfilling organizational objectives.
- It helps the management to perform all its functions, including planning, organizing, staffing, direction, and control. In other words, the field of accounting that provides economic and financial information for managers and other internal users is called management accounting.

Definition

- *The Institute of Cost and Management Accountants, London, has defined Management Accounting as: "The application of professional knowledge and skill in the preparation of accounting information in such a way as to assist management in the formulation of policies and in the planning and control of the operation of the undertakings.*
- *"Similarly, according to American Accounting Association: "It includes the methods and concepts necessary for effective planning for choosing among alternative business actions and for control through the evaluation and interpretation of performances."*

Definition

- The Institute of Chartered Accountants of England and Wales defines, "Management Accounting is that form of accounting which enables a business to be conducted more efficiently."
- According to R. N. Anthony, "Management Accounting is concerned with accounting information that is useful to management."
- Professor J Batty defines, "It is the term used to describe the accounting methods, systems, and techniques, which, coupled with special knowledge and ability, assist management in its task of maximizing profits or minimizing losses."

Characteristics/Nature of Management Accounting

- **Technique of Selective Nature:** It does not use the whole data provided by financial records. It selects and picks up only that information form different financial records which are relevant and useful to the management to arrive at important decisions on different aspects of the business.
- **Concerned with Future:** It collects and analyses data to plan the future. The primary function of management is to decide about the future course of action. It helps in planning the future because decisions are always taken for the future course of action.
- **Provides Data and not the Decisions:** The management accountant is not taking any decision by provides data which is helpful to the management in decision-making. It can inform but cannot prescribe. It is just like a map which guides the traveler where he will be if he travels in one direction or another. Much depends on the efficiency and wisdom of the management for utilizing the information provided by the management accountant.
- **Analysis of Different Variables:** Management accounting helps in analysing the reasons as to why the profit or loss is more or less as compared to the past period. Moreover, it tries to analyse the effect of different variables on the profits and profitability of the concern.
- **No Set Formats for Information:** Management accounting will not provide information in a prescribed proforma like that of financial accounting. It provides the information to the management in the form which may be more useful to the management in taking various decisions on the various aspects of the business.

Characteristics/Nature of Management Accounting

- **Achievement of Objectives:** Management accounting is helpful in realizing the enterprise objectives. Based on the historical information and with adjustments for predicate future changes, objectives are laid down. Actual performance is recorded. Comparison of actual with predetermined results is made. If there are deviations of actuals from the predetermined results, corrective action is taken and predicted objectives are achieved. This becomes possible with the help of management accounting techniques of standard costing and budgetary control.
- **Improving Efficiency**: The purpose of accounting is to provide information to increase efficiency. The efficiency of departments, and divisions can be improved by fixation of targets or goals for a specific period. The actual performance is compared with that of targets. Positive deviations are reviewed. The negative deviations are probed to ascertain the causes. The ways and means to tackle the causes are analysed and targets are achieved. The process of fixing and achieving the targets leads to gradual improvement in overall efficiency.
- **Use of Special Techniques and Concepts**: Management accounting employs special techniques like standard costing, budgetary control, marginal costing, fund flow, cash flow, ratio analysis, responsibility accounting, etc. to make accounting data more useful and helpful to the management. Each of these techniques or concepts is a useful tool for specific purpose in analysis and interpretation of data, establishing control over operations, etc.

Characteristics/Nature of Management Accounting

- **Providing Financial Information:** The main emphasis of management accounting is to provide financial information to management. The information is provided in a manner suitable to various levels of management for reviewing policies and decision making.
- **Decision Making:** Main objective of management accounting is to provide relevant information-to management to take various important decisions. Historical information provides a base on which the future impact is predicted, alternatives are developed and decisions are made to select to select the most beneficial course of action.
- **No Fixed Conventions:** Financial accounting has various established principles and rules in preparing the financial accounts. Management accounting has no such fixed rules. The tools or techniques applied by the management accounting are same but application of these techniques various from concern to concern and situation to situation.

Scope of Management Accounting

The scope of management accounting is very wide and broad-based. It includes all information which is provided to the management for financial analysis and interpretation of the business operations.

- **Financial Accounting:** Financial accounting is the general accounting which accounting relates to the recording of business transactions in the books of prime entry, posting them into respective ledger accounts, balancing them preparing a trial balance. Accounting for revenues, expenses, assets, liabilities, and net worth, together with the production of summary financial reports. Hence management accounting can not obtain full control and coordination of operations without a well designed financial accounting system.
- **Cost Accounting:** Accounting for current, standard and prospective costs; analysis and communication of cost data at all levels of management with the organization. It is the process and technique of ascertaining cost. The cost accounting system provides the necessary tools such as standard costing, budgetary control, inventory control, marginal costing, etc. for carrying out such functions efficiently.
- **Budgeting and Forecasting:** Forecasting on the various aspects of the business is necessary for budgeting. Budgetary control controls the activities of the business through the operations of budget by comparing the actual with the budgeted figures, finding out the deviations, analysing the deviations in order to pinpoint the responsibility and take remedial action so that adverse things may not happen in future.

Scope of Management Accounting

- **Cost Control Procedures:** These procedures are integral part of the management accounting process and includes inventory control, cost control, labour control, budgetary control and variance analysis, etc.
- **Reporting:** The management accountant is required to submit reports to the management on the various aspects of the undertaking. While reporting, he may use statistical tools for presentation of information as graphs, charts, pictorial presentation, index numbers and other devices in order to make the information more impressive and intelligent.
- **Methods and Procedures:** It includes in its study all those methods and procedures which help the concern to use its resources in the most efficient and economical manner. It undertakes special cost studies and estimations and reports on cost volume profit relationship under changing circumstances.
- **Tax Accounting:** It is an integral part of management accounting and includes preparation of income statement, determination of taxable income and filing up the return of income etc.
- **Internal Financial Control:** Management accounting includes the internal control methods like internal audit, efficient office management, etc.

Scope of Management Accounting

- **Interpretation:** Management accounting is closely related to the interpretation of financial data to the management and advising them on decision-making.
- **Office Services:** The management accountant may be required to maintain and control office services in some organizations. This function includes data processing, reporting on best use of mechanical and electronic devices, communication, etc.
- **Evaluating the Performance of the Management:** Management accounting provides methods and techniques for evaluating the performance of the management. It evaluates the performance of the management in the light of the objectives of the organisation. Thus, it helps in the implementation of the principle of management by exception.

Branches of Accounting

- **Financial Accounting**: It is that branch of accounting, which involves the recording of the transactions, inclined towards the preparation of trial balance and final accounts.
- **Cost Accounting:** Cost account is the accounting discipline, which deals with costs, i.e. the unit costs of the goods produced and services provided. It helps the management of the organization in fixing the price, controlling costs and providing relevant information for the purpose of decision making.
- **Management Accounting**: The accounting system which supplies the necessary information to the management, for rational decision making. The information may be concerned with funds, costs, profits and losses and so forth. This information is helpful in determining the effect of the decisions and analysing the performance of the entity.
- **Tax Accounting**: The accounting system that deals with the tax return and its payment, instead of preparation of final accounts of the enterprise, is called tax accounting.
- **Social Accounting**: This branch of accounting is commonly termed as social responsibility accounting. It aims at unveiling the facilities provided by the entity to the society, in terms of medical, housing, education, and so forth.

Benefits of Management accounting

- **Effective Planning**: In management accounting, the financial information and non financial information is presented at regular intervals say weekly, fortnightly to the management. This presentation includes forecasts, budgets and in-depth analysis. Hence it assists the management in planning the business activities. Policy formulation and planning of operations become more effective through the 'decision data' provided by Management Accounting.
- **Decision making:** Since management accounting presents various charts, forecasts and analysis the management uses it for decision making.
- **Identify early signs of problems:** If a product is not performing well the management can identify it early on as the accounts are presented at regular intervals. This will aid in overcoming the constraints early on and avoiding future losses.
- **Strategic management:** Based on the information presented in management accounting, the management can take decisions about continuing a product or modifying the sale strategy. Since management accounting is not regulated by any law, the management can decide the areas that require more analysis, investigation and accordingly draw up strategies.

- **Increase in Efficiency**: Management accounting contributes significantly towards increasing efficiency in operations of a firm. Budgets, standards, reports etc., usually elevate the level of performance.
- **Performance Evaluation**: Evaluating performance of employees, departments, etc., is facilitated by Management accounting through Variance Analysis, control ratios etc.
- **Profit Maximization**: Management accounting is helpful in profit planning to pursue decisions which can optimize profits.
- **Reliability**: The Tools used by Management accounting usually make the data supplied to Management accurate and reliable.
- **Elimination of Wastages**: Standard costs, Budgets, cost control techniques, etc., contribute towards elimination of wastages, production of defectives etc.

- **Effective Communication**: Regular and systematic reporting ensures constant flow of information about operations to various levels of Management.

- **Employee Morale**: Morale of employees can be created and sustained through attainable standards, practical budgets and incentive schemes.

- **Control and Co-ordination**: Control on costs and coordination in the efforts of different segments of an organisation can be achieved through performance reporting, variance analysis and follow up action etc.

- The greatest benefit of Management accounting is its advisory role in making the Management to take the best possible decisions on a day-to-day basis on routine matters and also vital policy matters.

Limitations of Management Accounting

- **Dependence for Basic Records**: Management Accounting rarely maintains basic and primary records of operations, expenses and revenues. It derives all of its Primary data from Financial Accounting, cost Accounting and other relevant records. So, the accuracy .and reliability of the conclusions derived by Management Accounting is limited to the reliability of its sources of data, so, it suffers from several of the limitations of Finance Accounts and cost Accounts.

- **Personal Bias**: Analysis and interpretation of financial information depends upon the capability of the analyst and interpreter. Personal Judgment and usage of discretion become necessary in several areas of Management accounting. Personal 'Prejudices' and 'Bias' of individuals can affect the objectivity and effectiveness of the conclusions and recommendations.

- **Management Accounting is only a Tool**: Management accounting cannot be considered as an alternative or substitute to Management. Management accountant acts as an adviser and facilitator for decision making by management. The actual decisions, their implementation and follow up action are the prerogative of the Management.

- **Management Accounting provides only Data**: The Main function of Management Accounting is to provide data in the form of 'Alternatives' to the Management. It is for Management to make suitable choice among the alternatives or even discard all of them. So, Management Accounting can 'only Inform and not prescribe'.

- **Broad Based Scope**: The scope of Management accounting is very wide and broad based. It uses information from varied disciplines like Financial Accounting, economics, Statistics, Cost Accounts, engineering etc. It considers Monetary and Non-Monetary Transaction of the firm. Limitations of the knowledge and experience of the Management Accountant in such diverse fields can make the data unreliable and undependable.

- **Resistance to Change**: Installation of Management accounting involves basic changes in the organisational set up and Traditional accounting practices. The personnel concerned may resist such change unless they are taken into confidence and convinced of the need for such changes.

- **Costly to Install**: Installation of Management Accounting involves huge expenditure because of the elaborate organisation needed and the large number of changes in procedures, forms and rules. So, small firms may not be able to afford the cost. Only big organisations can afford to Maintain Management accounting as a department or aid to management.

- **Evolutionary Stage**: Management accounting is of-recent-origin, as a discipline and it is still in development stage. So, its concepts are fluid, Techniques are still evolving and analytical tools imperfect. There are several experts who are skeptical of the utility of Management accounting because of such an important limitation.

- **Lack of knowledge:** The use of management accounting requires knowledge of several related subjects. Deficiency in knowledge in related subjects like accounting principles statistics, economics, principles of management, etc. will limit the use of management accounting.

- **Persistent Efforts:** The conclusions and decisions drawn by the management accountant are not executed automatically. Thus, there is a need for continuous and coordinated efforts of each management level to execute these decisions. He has to convince people at all levels. In other words, he must be an efficient salesman in selling his ideas.

- **Intensive Decision:** Decision making based on management accounting that provides scientific analysis of various situations will be a time-consuming one. As such, management may avoid systematic procedures for making a decision and arrive at a decision using intuitive and intuitive limits the usefulness of management accounting.

Role of management accountant

- **Planning of Accounting Function**: An accounting system is maintained in an organization which should cover standards of costs, sales forecast, production planning, profit planning, allocation of resources, capital budgeting and short term and long term financial planning. Moreover, he has to prepare the necessary procedures to implement the plan effectively.

- **Controlling**: The management accountant has to measure the actual performance and compare with standard. Based on this comparison, he has to find the differences and interpret the results of operation and submit the same to all levels of management. This is done through appropriate accounting reports for controlling.

- **Reporting**: The top management requests the management accountant to prepare the report for the root causes for an unfavorable event or operations. In this report, the accountant can pin point real reasons and the persons who are responsible.

- **Coordinating**: He consults all levels of management for framing a policy or an action programme. Such type of consultation brings co-ordination between the accounts department and top management.

- **Interpreting**: The accounting information is modified and presented before the management with interpretation. The interpretation is made in different phases. If so, real reasons for the operating results can be understood by the management.

- **Evaluation**: He has to evaluate the effectiveness of policies, organization structure and procedures adopted for attaining the objectives. For which, he has to consult the same with functional managers and top executives.

- **Advising**: He has to advise the management in order to improve the performance of operations.

- **Administration of Tax:** A business organization is liable to pay value added tax, income tax and other taxes to the local government, state government and central government. In this aspect, the management accountant is expected to pay the taxes and maintain the accounting records as the case may be.

- **Government Reporting**: He will have to supervise all the statements and returns which are to be submitted to the government periodically within due date.

- **Appraisal of External Effects**: There may be changes in the state and central government policy. Sometimes, there may be amendments in the existing laws. These policy changes and amendments have an impact on the attainment of business objectives. The extent of impact has to be assessed by the management accountant.

- **Economic Appraisal**: The economic condition of the nation is periodically published by the central government. Now, the management accountant is to make economic appraisal and find the influence of economic condition over the business activities. In this aspect, he can prepare a report and submit before top management along with his/her comments.

- **Protection of Assets**: This function is performed through maintenance of separate fixed assets register for each type of fixed assets. Moreover, he can frame the rules and regulation for using each type of fixed assets. He can take insurance coverage to all types of fixed assets.

S.No.	Cost Accounting	Management Accounting
1	The main objective of cost accounting is to assist the management in cost control and decision-making.	The primary objective of management accounting is to provide necessary information to the management in the process of its planning, controlling, and performance evaluation, and decision-making.
2	Cost accounting system uses quantitative cost data that can be measured in monitory terms.	Management accounting uses both quantitative and qualitative data. It also uses those data that cannot be measured in terms of money.
3	Determination of cost and cost control are the primary roles of cost accounting.	Efficient and effective performance of a concern is the primary role of management accounting.
4	Success of cost accounting does not depend upon management accounting system.	Success of management accounting depends on sound financial accounting system and cost accounting systems of a concern.
5	Cost-related data as obtained from financial accounting is the base of cost accounting.	Management accounting is based on the data as received from financial accounting and cost accounting.

6	Provides future cost-related decisions based on the historical cost information.	Provides historical and predictive information for future decision-making.
7	Cost accounting reports are useful to the management as well as the shareholders and creditors of a concern.	Management accounting prepares reports exclusively meant for the management.
8	Only cost accounting principles are used in it.	Principals of cost accounting and financial accounting are used in management accounting.
9	Statutory audit of cost accounting reports are necessary in some cases, especially big business houses.	No statutory requirement of audit for reports.
10	Cost accounting is restricted to cost-related data.	Management accounting uses financial accounting data as well as cost accounting data.

BASIS FOR COMPARISON	FINANCIAL ACCOUNTING	MANAGEMENT ACCOUNTING
Meaning	Financial Accounting is an accounting system that focuses on the preparation of financial statement of an organization to provide the financial information to the interested parties.	The accounting system which provides relevant information to the managers to make policies, plans and strategies for running the business effectively is known as Management Accounting.
Is is compulsory?	Yes	No
Information	Monetary information only.	Monetary and non-monetary information
Objective	To provide financial information to outsiders.	To assist the management in planning and decision making process by providing detailed information on various matters.

Format	Specified	Not specified
Time Frame	Financial Statements are prepared at the end of the accounting period which is usually one year.	The reports are prepared as per the need and requirements of the organization.
User	Internal and external parties	Only internal management.
Reports	Summarized Reports about the financial position of the organization	Complete and Detailed reports regarding various information.
Publishing and auditing	Required to be published and audited by statutory auditors	Neither published nor audited by statutory auditors.

THANK YOU