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MANAGEMENT AND ACCOUNTING-COMPLEMENTS EACH OTHER

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ABSTRACT

Management and Accounting are two limbs of business. A business cannot be run success fully without the co-relation of accounting & management, Because Accountants cannot be take any observation without the help of manager and other side manager cannot take any decision without the help of accountant, therefore they are interdependent on each other. They have been closely associated for a long time. In past accounting have been to record, analyze, and report the results of business operations in various units of measurement such as rupees, units of production, standard hours and kilowatts etc. But presently the account also include value added services like as Budgeting, Planning, Forecasting, MIS, Reporting etc which are not possible without the help of Management . Now the management wants more information's through Accounting Department so that it is necessary co-relation between Management & Accounting. Or we can say in others words "Accounting & Management are helpful for each other." The present paper tries to study of necessity of both Department like management & accounting each other. How management is helpful for Accounting in Analyze, Reconcile, prepare budget, MIS, calculate costing of product etc. field. This paper will specially highlight the Co-relationship between management & accounting department and make decision for future planning for business to use mass knowledge of higher management with Accounting Data.

Keywords: *Management, Accounting, Analysis, Planning, Forecasting, Costing, Reconciliation.*

Introduction

Meaning of Accounting

Management Accounting can be referred to as "a system of accounting for management", which provides necessary information to the management for discharge of its functions. These functions include planning, organizing, directing, controlling and decision making. Management accounting assists the management to carry out these functions more efficiently in a systematic manner. Some of the important definitions of management accounting are:

- **The Institute of Chartered Accountants of England and Wales:** "Any form of accounting which enables a business to be conducted more efficiently can be regarded as management accounting."
- **Robert N. Anthony:** "Management accounting is concerned with accounting information that is
- useful to management."
- **The Institute of Chartered Accountants of India:** "Such of its techniques and procedures by which accounting mainly seeks to aid the management collectively."

In short, management accounting can be defined in simple words as "accounting for effective management."

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Literature Review

Axson (2010) states "Information is the lifeblood of the modern corporation. Without it, decisions cannot be made, customers cannot be served, and earnings cannot be grown." Whilst all information is valuable, it ironically alone doesn't have all the answers and the rapid flow of data may even result in organizations losing control over the quality of information.

Stvilia, et al., 2007: Yet good planning and control over operations via effective decisions needs to be based on a steady flow of good quality and up-to-date information. That means one of the prime challenges facing modern businesses is obtaining quality information from the vast pool of data available to take on business decisions. Because, information quality is considered one of the key determinants for the quality of an organization's decisions and actions.

Eppler & Wittig, 2000: It is perceived that high-quality information makes it easier to convert available information into knowledge, by helping to interpret and assess the information, combine with prior knowledge, and facilitate the utilization of information in new contexts in the organizations.

Popovic& Habjan, 2012: In decision-making, the contribution of information reduces uncertainty, allows organizations to quickly respond to business events, and supports companies making changes in business strategies, plans and performance indicators.

Hall, 2010: Accounting, considered to be a key source of information about business performance, can help managers to develop knowledge about the organization's environment in several ways. It makes visible those events that are not perceptible by daily activities of a manager and provides an overall quantitative perspective on their work.

Socea, 2012: Accounting information can reveal issues that are overlooked during ordinary daily activities and can provide an independent control over operations to help man-agers be aware, which allows the manager to determine the meaning and significance of all the operations.

Hopper et al., 2009: Accounting in transition and less developed economies Despite the fact that accounting has been a widely endorsed topic by academic researchers in recent decades, these studies only occasionally refer to transition economies. The reasons may concern at least two facts. Firstly, most research was done in the field of financial accounting.

Research Methodology

The study based on secondary data which is collected from Published Report, Reference Books, News Paper, Journals, Websites, and my own experience. In this study, we shall discuss the importance of financial information from the organization's management point of view. The study will concentrate on internal financial reporting, leaving outside external reporting controlled by laws and regulations and operational reporting. The focus of this study is to explore the "How useful the reports generated through accounting information in managerial decision-making?" The purpose is to create a picture of the reality, an understanding of how the current accounting reports correspond to management information needs, and raised out potentials for development.

Objectives of the Study

The main objective of the study is to evaluate the role of accounting information in strategic decision making in various industries. The specific objectives of the study are:

- To identify the frequency of using accounting information in decision making
- To know about the effectiveness of accounting information in long-term strategic decisions.
- To identify the problems in generating accounting information in various organizations
- To recommend suggestions to overcome the identified problems.
- To guide for future research scholar.

Accounting, Accountability and Account

Businesses exist to provide goods or services to customers in exchange for a financial reward. Public-sector and not-for-profit organizations also provide services, although their funding comes not from customers but from government or charitable donations. Business is not about accounting. It is about markets, people and operations, although accounting is implicated in all of these decisions because it is the financial representation of business activity.

Accounting is a collection of systems and processes used to record, report and interpret business transactions. Accounting provides an **account** – *an explanation or report in financial terms* – about the transactions of an organization. It enables managers to satisfy the *stakeholders* in the organization (owners, government, financiers, suppliers, customers, employees etc.) that they have acted in the best interests of stakeholders rather than themselves. This is the notion of **accountability** to others, a result of the *stewardship* function of managers that takes place through the process of accounting. Stewardship is an important concept because in all but very small businesses, the owners of businesses are not the same as the managers.

Interpreting Financial Statements

The concept of financial statements for the purpose of individual, partnership firm or LLP is very narrow because the importance of financial statements for himself of government authorities only not for general public. Therefore, financial statements included only Balance Sheet and Statement of Profit &Loss i.e. Trading & Profit and Loss Account. But incorporate sector the financial Statements are most important for management, investors, financial institutions who funded to company, shareholders, government authorities and general public because the financial statements are mirror or blue prints of that Corporate house. Financial statements are an important part of a company's Annual Report, which is required for all companies listed on the Stock Exchange. For companies not listed, the Companies Act requires the preparation of financial statements.

The Annual Report for a listed company typically contains:

- **A Financial Summary**

  The key financial information.

- **The Chairman's or Directors' Report**

  This provides a useful summary of the key factors affecting the company's performance over the past year and its prospects for the future. It is important to read this information as it provides background to the financial statements, in particular the company's products and major market segments. It is important to 'read between the lines' in this report, since the intention of the annual report is to paint a 'glossy' picture of the business. However, as competitors will also read the annual report, the company takes care not to disclose more than is necessary.

- **The Statutory Reports by the Independent Auditors**

  These will help to identify any key issues that may be found in the accounts themselves.

- **The Financial Statements**

  Consolidated Profit and Loss account, Balance Sheet and Cash Flow statement along with Schedules & annexure thereon, the consolidated figures should be used, as these are the total figures for the group of companies that comprise the whole business.

- **Notes to the Accounts & Significant Accounting Policies**

  Which provide a Blue print of Whole Business, In the notes on accounts a details information which cannot shown in Balance sheet or profit & loss Accounts like as - Contingent liabilities, Statutory Dues, Pending cases on company & there status etc.

- **A five-year Summary of Key Financial Information**

Use of Accounting Information for Management

- **Planning and Forecasting:** Planning and forecasting are essential for achieving business objectives. Accounting information provides necessary data for forecasting and budgetary control.
- **Modification of Data:** It modifies the accounting data by rearranging in such a way that it suits the requirements of the management.
- **Analysis and Interpretation:** The accounting data is analyzed and interpreted meaningfully for effective planning and decision making.
- **Serves as a Means of Communication:** Accounting Department establishes communication within different levels of management and with the outside world. The all information for various departments like as top management, purchases department, costing department, sales departments, marketing department, advertisement & sales promotion department etc. get information from accounting department which is important for them.
- **Facilitates Managerial Control:** It enables all accounting efforts to be directed towards the attainment of goals efficiently by controlling the operations of the company. Standards of various departments and individuals are fixed and actual performance is compared with it, deviations are assessed and proper control exercised.

- **Use of Qualitative Information:** Management accounting uses qualitative information also to assist the management in decision making process engineering records, case studies, special surveys etc. are used in purpose.
- **Decision-making:** Management accounting supplies analytical information regarding various alternatives and selection is made easy.

Users of Accounting Information

- **Owners:** Owners refers to a person or group of persons who have supplied capital for running the business. It refers to Individual in case proprietor partners in case of partnership firm and shareholders in case of Joint Stock Company. Information needs of shareholders have assumed great significance in the corporate business world because of separation of ownership and management in case of joint stock companies. Owners are interest in the financial information to know about *safety* of amount invested and *return* on amount investment.
- **Managers:** For managing business profitably, information about financial results and financial position is needed by management. By providing this information, accounting helps managers in efficient and smooth running of a business enterprise.
- **Investors:** Prospective investors would like to know about the past performance of the business enterprise before making investment in that concern. By analyzing historical information provided by accounting records, they can arrive at a decision about the expected return and the risk involved in investing in a particular business enterprise.
- **Creditors and Financial Institutions:** Whosoever is extending credit or loan to a business enterprise, would like to have information about its repaying capacity, credit worthiness etc. Analyzing and interpreting the financial statements of the business enterprise can obtain the required information.
- **Employees:** Employees are concerned about job security and future prospects. Both of these are intimately related with the performance of the business enterprise. Thus by analyzing financial statements they can draw conclusions about their job-security and future prospects.
- **Government:** Government policies relating to taxation, providing subsidies etc. are guided by relevance of the industry in the economic development of the country and the past performance of the industry. Information about past performance is provided by the accounting system. Collection of taxes is also based on accounting records.
- **Researchers:** Researchers need financial information for testing hypothesis and development of theories and models. The required information is provided by accounting system.
- **Customers:** Customers who have developed loyalties to a business are certainly interested in the continuance of the business. They certainly want to know about the future directions of the enterprise with which they are associating themselves. The way to information about the enterprise is through their financial statements.
- **Public:** An enterprise affects the public at large in many ways such as a provider of employment to a number of persons, being a customer to many suppliers, a provider of amenities in the locality or a cause of concern to the public due to pollution etc.

Hence, public at large is interested in knowing the future directions of enterprise and the only window to peep inside the enterprise is their financial statements. Above-mentioned list of group of users of accounting information is not exhaustive. Anyone having an interest in the business enterprise can use information for decision-making.

Ratio Analysis

Ratio Analysis is more important for decision making for Management, Investors , share holders, Financers and Various Group of person. Ratio analysis is based on accounting information therefore the relation between accosting & managements is more closer .The Profit and Loss account, Balance Sheet and Cash Flow statement can be studied using ratios. *Ratios* are typically two numbers, with one being expressed as a percentage of the other. Ratio analysis can be used to help interpret *trends* in performance year on year and by *benchmarking* to industry averages or to the performance of individual competitors. Ratio analysis can be used to interpret performance against five criteria:

- The rate of profitability;
- Liquidity, i.e. cash flow;
- Gearing, i.e. the proportion of borrowings to shareholders' investment;
- How efficiently assets are utilized; and
- The returns to shareholders.

Ratio Analysis

There are different definitions that can be used for each ratio. However, it is important that whatever ratios are used, they are meaningful to the business and applied consistently. Ratios are nearly always expressed as a percentage.

Rate of Profitability

- **Return on (Shareholders') Investment (ROI)**

$$\frac{\text{Net Profit After Tax}}{\text{Shareholders' Funds}} \times 100$$

- **Return On Capital Employed (ROCE)**

$$\frac{\text{Operating Profit Before Interest And Tax}}{\text{Shareholders' Funds + Long-Term Debt}} \times 100$$

- **Operating Profit/Sales**

$$\frac{\text{Operating Profit Before Interest And Tax}}{\text{Sales}} \times 100$$

- **Gross Profit/Sales**

$$\frac{\text{Gross Profit}}{\text{Sales}} \times 100$$

- **Net Profit/Sales**

$$\frac{\text{Net Profit}}{\text{Sales}} \times 100$$

Each of the profitability ratios provides a different method of interpreting profitability. Satisfactory business performance requires an adequate return on shareholders' funds and total capital employed in the business. Profit must also be achieved as a percentage of sales, which must itself grow year on year. The operating profit and gross profit margins emphasize different elements of business performance.

Liquidity Ratios

- **Working Capital**

$$\frac{\text{Current Assets}}{\text{Current Liabilities}}$$

- **Acid Test (Or Quick Ratio)**

$$\frac{\text{Current Assets} - \text{Inventory}}{\text{Current Liabilities}}$$

A business that has an acid test of less than 100% may experience difficulty in paying its debts as they fall due. On the other hand, a company with too high a working capital ratio may not be utilizing its assets effectively.

Capital Gearing Ratio

- **Gearing Ratio**

$$\frac{\text{Long-Term Debt}}{\text{Shareholders' Funds + Long-Term Debt}} \times 100$$

Table 1: Risk and return – effect of different debt/equity mix

Particulars	**100% Equity**	**50% Equity 50% Debts**	**10% Equity 90% Debts**
Capital Employed			
Equity	10,00,000/-	500,000/-	1,00,000/-
Debts	0	500,000/-	9,00,000/-
Total Capital Employed	10,00,000/-	10,00,000/-	10,00,000/-
Operating Profit	1,00,000/-	1,00,000/-	1,00,000/-
Interest On Debts @10%	0	50,000/-	90,000/-
PBT (Profit Before Tax)	*1,00,000/-*	50,000/-	10,000/-
Tax @30%	30,000/-	15,000/-	3,000/-
PAT (Profit After Tax)	70,000/-	35,000/-	7,000/-
ROI (Return On Investment)	PAT/Equity*100	PAT/Equity*100	PAT/Equity*100
	7%	3.5%	0.70%

Source: Fictitious data, for illustration purposes only

- **Interest Cover**

$$\frac{\text{Profit Before Interest and Tax(PBIT)}}{\text{Interest Payable}} \text{ X } 100$$

The higher the gearing, the higher the risk of repaying debt and interest. The lower the interest cover, the more pressure there is on profits to fund interest charges. However, because external funds are being used, the *rate of profit* earned by shareholders is higher where external funds are used. The relationship between risk and return is an important feature of interpreting business performance. Consider the example in Table of risk and return for a business whose capital employed is derived from different mixes of debt and equity.

Efficiency ratio

- **Asset Turnover**

$$\frac{\text{Sales}}{\text{Total Assets}} \text{ X } 100$$

This is admeasure of how efficiently assets are utilized to generate sales. Investment in assets has as its principal purpose the generation of sales. Three other efficiency ratios are those concerning debtor's collections, stock turnover and creditor's payments.

- **Shareholder Return**

We use illustration for learn more easier to this ratio:

Let us Number of shares issued 1,00,000

Market value of shares	Rs. 10/- Each
Profit after Interest & Tax	Rs. 5,00,000/-
Dividend Paid	Rs. 2,50,000/-

- **Dividend Per Share (DPS)**

$$\frac{\text{Dividends Paid}}{\text{Number of Shares}} = \frac{2,50,000}{1,00,000} = \text{Rs. 2.50 /- Per Share}$$

- **Dividend Payout Ratio**

$$\frac{\text{Dividends Paid}}{\text{Profit After Tax}} \text{x100} = \frac{250000}{500000} = 50\%$$

- **Dividend Yield**

$$\frac{\text{Dividends Paid Per Share}}{\text{Market Value Per Share}} \text{x100} = \frac{2.5}{10.00} = 25\%$$

- **Earnings Per Share**

$$\frac{\text{Profit After Tax}}{\text{Number of Shares}} = \frac{5,00,000}{1,00,000} = \text{Rs. 5/- per share}$$

- **Price/Earnings (P/E) Ratio**

$$\frac{\text{Market Value Per Share}}{\text{Earnings Per Share}} = \frac{10}{5} = 2$$

The shareholder ratios are measures of returns to shareholders on their investment in the business. The dividend and earnings ratios reflect the annual return to shareholders, while the P/E ratio measures the number of years over which the investment in shares will be recovered through earnings.

Interpreting Financial Information using Ratios

The interpretation of any ratio depends on the industry. In particular, the ratio needs to be interpreted as a trend over time, or by comparison to industry averages of competitor ratios. These comparisons help determine whether performance is improving and where improvement maybe necessary. Based on the understanding of the business context and competitive conditions, and the information provided by ratio analysis, users of financial statements can make judgments about the pattern of past performance and prospects for a company and its financial strength.

Broadly Speaking, Businesses Seek

- Increasing rates of profit on shareholders' funds, capital employed and sales;
- Adequate liquidity (current ratio not less than 1.33)
- To ensure that debts can be paid as they fall due, but not an excessive rate to suggest that funds are inefficiently used;
- A level of debt commensurate with the business risk taken;
- High efficiency as a result of maximizing sales from the business's investments;
- A satisfactory return on the investment made by shareholders.

When considering the movement in a ratio over two or more years, it is important to look at possible causes for the movement. These can be gained by understanding that either the numerator (top number in the ratio) or denominator (bottom number in the ratio) or both can influence the change.

Other accounting techniques that provide management with control information are:

õ **Standard Cost**

Standard Costs are predetermined costs developed from past experience, motion and time study, expected future manufacturing costs, or some combination of these. They contrast with actual costs, which are the amounts actually incurred in the manufacturing process. Examples of Standard Costs are – standard labor costs, standard material cost and standard overhead costs.

õ **Responsibility Accounting**

In responsibility accounting costs are identified with those individuals who are responsible for their control. The authority of the person being considered must be recognized; thus, responsibility accounting classifications must fit the organization structure. Furthermore, a minimum of cost allocation should be employed; that is, consideration should be given only to those costs that are clearly influenced by a particular individual.

õ **Deciding**

The manager can obtain accounting information designed to aid him in deciding between alternative courses of action in two ways:

- The reutilized collection of relevant data for certain types of anticipated decisions is called programmed analysis.
- Non- programmed analysis develops special cost information for specific decisions.

õ **Analysis of Past Performance**

Financial accounting statements contain valuable information that managers can use to analyze past performance. Management can analyze financial data by:

- Comparisons of two or more periods, and
- Comparison within one period.

The former includes the analysis of successive balance sheets and income statements to determine trends in individual items. The latter involves the analysis of current financial statements to determine the state of the firm with respect to its solvency, stability and profitability. Another very useful technique of the managerial accountant is called source and application of funds analysis.

This technique involves the determination of where funds (working capital) have come from and how they were used, that is, a focus on cash flow. Most of the information needed for analysis can be obtained from a comparison of two balance sheets plus some supplemental information added to reflect the flow of funds. From managements point of view, the value of the analysis of source and use of funds is that it gives valuable insight on the efficiency of management in allocating funds.

Conclusion

The accounting information performs a crucial role on management decisions and organization performance which has been shown to be major force in decision making. The accounting information plays a vital role in taking the effective, accurate and significant strategic decision in manufacturing, human resource, long term investment and marketing related factors.

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