

Chapter 1 – Introduction to Management Accounting

Management Accounting – the processes and techniques that focus on the effective and efficient use of organisational resources to support managers in their tasks of enhancing both customer value and shareholder value

Their role in an organisation:

- Support managers in the process of making decisions (certain decisions need information and have cost implications)
 - Identify problems and help solve them
 - Apply accounting concepts and techniques to real world problems
 - Explain accounting concepts and techniques to managers who are not trained in accounting
- ✚ In most organisations, even small businesses, everybody will do some sort of management accounting role; looking at key performance indicators, budgeting, making decisions with cost implications

Some History:

- During the industrial revolution large manufacturers and producers needed information to measure their companies performance
- These companies were privately owned so did not follow accounting standards (financial)
- Owners developed management accounting as a way to track their costs relating to production of goods and services
- These methods became quite complex and laid the foundation for today's cost accounting techniques

In Recent Times – Responding to the Changing Business Environment

- Increased global competitiveness – impacts from other countries, increased competition
 - Increase reliance on strategic alliances in order to operate
 - Rapid advances in technology resulting in new business models and an increased emphasis on innovation as a source of competitive advantage
 - Increasing pressure for accountability, including a focus on ethical issues
 - Increasing awareness of sustainability issues, especially climate change – cost/strategic implications
- ★ Managers need information that is much more **detailed** than that found in financial reports to make decisions, solve problems and plan for the future (dynamic, flexible information is needed)
- ★ Contemporary management accounting and techniques have developed to support new organisational structures, systems and practices, as a response to a rapidly changing business environment

Organisations will value different things (ie. Qantas business class vs Tiger Airways) and this anchors decision making to enhance;

Customer Value – the value that a customer places on particular features of a product

- ✓ Satisfying customer needs are critical to achieving increased sales and market share, and therefore to achieving shareholder value

Shareholder Value – the value that shareholders or owners place on a business

- Shareholders are usually interested in increased profitability, increased share price and dividends

Social Value – social enterprises: commercially viable businesses with a purpose of generating **social impact**

- Involves organisations that apply commercial strategies to maximize improvements in human and environmental well-being
- May include maximising social impact rather than profits for external stakeholders

Example: Thankyou Movement

- Operates as a for-profit business involving all the normal costs involved to run a sustainable business
- All dividends paid into a charitable trust (rather than to shareholders – not much shareholder value)
- This trust finances foreign aid programmes such as:
 - Safe water access for 150, 939 people
 - Hygiene and sanitation programs for 190, 957 people
 - 12.1 million days’ worth of immediate food aid



Therefore, management accounting systems produce the information required by managers to **create value** (whatever value means in a particular business context)

Management Accounting Information:

- Estimates the cost of producing goods and services
- Information for planning and controlling operations
- Information for measuring performance
- Information for determining future plans and strategic direction

This information is difficult to extract from financial reports – need more detailed information

How Management Accounting differs from Financial Accounting

Financial Accounting – the practice of preparing and reporting accounting information for parties outside the organisation

Management Accounting – focuses on the information needs of managers inside the organisation

Financial Accounting

Management Accounting

For <i>external</i> users – shareholders, creditors, banks, stock exchange, trade unions and government agencies	For <i>internal</i> users – managers and employees
The content of financial reports is determined by <i>strict</i> accounting standards and corporation law (necessary for comparison)	<i>No standards or rules</i> are imposed – flexibility depending on the manager’s needs
Data is extracted from the <i>transaction</i> based accounting system	Information is <i>both financial and non-financial</i> depending on the managers needs and comes from a wider variety of non-regulated sources
The data reflects <i>past</i> performance, it is <i>verifiable</i> and highly <i>aggregated</i>	The data is <i>future</i> orientated, can be <i>subjective</i> (especially non-financial data) and is often highly <i>detailed</i>
Financial Accounting Information: Shareholder reports (financial statements), Other Stakeholder reports (credit reports, inventory reports), Government reports (tax returns, cost reports)	Management Accounting Information: Support organisational structures (product development), Support operating plans (budgets, analysis of product mix), Monitor and Motivate (actual vs planned performance, supplier quality)

Management Accounting – Processes and Techniques help to

- ✓ Formulate and implement strategy
- ✓ Improve competitive advantage through process improvement and cost management
- ✓ Manage resources through systems of planning and control
- ✓ Estimate the costs of an organisations inputs and outputs
- ✓ Support the strategic and operational decisions of managers

Strategy – the direction that the organisation intends to take over the long term to meet its mission and achieve its objectives

- Focus on ways to manage the organisations resources to create value for customers and shareholders

Management Accounting and Strategy

In what type of business will we operate in?

How should we compete in that business?

What systems and structures should we have in place to support our strategies?

What products/services should we launch, discontinue?

Should we outsource?

Strategic Planning – long term planning to decide how a business competes within its chosen market (competing with others who want to create the same value)

Strategy Implementation – planning and managing the implementation of strategy; new structures, new systems, new production processes, new marketing approaches, new HRM policies – all have cost implications

Overlap with financial accounting?

- Product costs are prepared to meet external reporting purposes (following rules)
- However, different product costs may also be produced outside of the financial accounting system, to better meet managers' decision-making needs (these costs may not comply with GAAP or accounting standards; **flexibility** needed)

High Level of Flexibility in Management Accounting

Focus is on the **needs** of managers within the organisation. Influenced by;

- Managers information needs and the nature of the resources they manage
- Differences in production and service technologies, organisational structure, organisational size, the external environment, level of sophistication of computer systems
- Whilst accounting staff and processes are found at the top level of an organisation, they are also found in operating divisions
- Managers from other functional areas may undertake MA activities such as customer service and warehouse managers

Cost Accounting Systems - we need ways of categorising, accumulating and analysing costs

- Job costing systems
- Process costing systems
- Hybrid costing systems
- Activity-based costing systems

- ★ No two cost accounting systems are alike, organisations differ, so too do costing systems (differing values and decisions)