



Topic 1

The Nature and Purpose of Management Accounting

Session Objectives

- Describe the purpose and role of cost and management accounting within an organisation's management information system
- Compare and contrast financial accounting with cost and management accounting.
- Distinguish between data and information
- Identify and explain the attributes of good information



Session Objectives

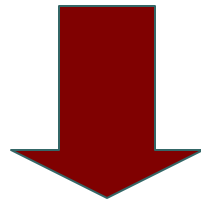
- Outline the managerial processes of planning, decision making and control
- Explain the difference between strategic, tactical and operational planning.
- Distinguish between cost, profit, investment and revenue centres.
- Explain and illustrate the concepts of cost objects, cost units and cost centres



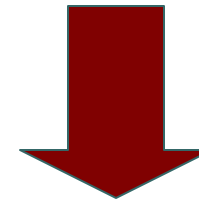
Role of Accountants

- Financial accounting
- Management and Cost accounting
- Non-financial information

Accounting



Financial



**Cost and
Management
Accounting**

Financial Accounting

- *The classification and recording of monetary transactions of an entity in accordance with established concepts, principles, accounting standards and preparation of the final accounts*

Financial Accounting

- Much of the information is financial
- Maintain ledger systems of accounting records
- Financial accounts are a source of management information but are insufficient for the management

Insufficiency of Financial Accounting Information: Example

- Profit statement does not answer questions such as:
 - Which product sells best?
 - How much profit do we earn from each product?
 - Do we make a loss with any of our products?
 - Are costs higher than expected and if so in which area?.....and many more

Management Accounting

- *Application of principles of accounting and financial management to create, protect, increase value so as to deliver that value to the stakeholder*

Management Accounting

- This involves participation of management to ensure proper:
 - Strategic planning
 - Budgeting / Profit planning
 - Financial management
 - Financial control
 - Audit

What is Cost Accounting

- A system of recording data and producing information about costs, for the products produced by the organisation and or the services it provides.
- It is also used to establish costs for particular activities or responsibility centres.

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What is Cost Accounting

- Cost accounting is a part of management accounting
- Management accounting includes cost accounting and extends to both financial as well as non-financial information
- Cost accounting is historical while management accounting is forward looking

Management Accountant vs. Financial Accountant

Basis	Management Accountant	Financial Accountant
Information User	Internal Use	External Use
Purpose	Aid planning, controlling, decision-making	Record financial performance in a specific period
Legal requirements	None	Limited companies must produce financial statements
Formats	Depends on the management	Prescribed
Nature	Financial and non-financial	Mostly financial
Time period	Historical and forward-looking	Historical

Functions of Management

- **Setting objectives for achievement**
- **Making plans for how to achieve those objectives**
- **Putting the plans into action**
- **Monitoring actual results and taking control measures**
- **Evaluating actual performance**



Planning
And
Control



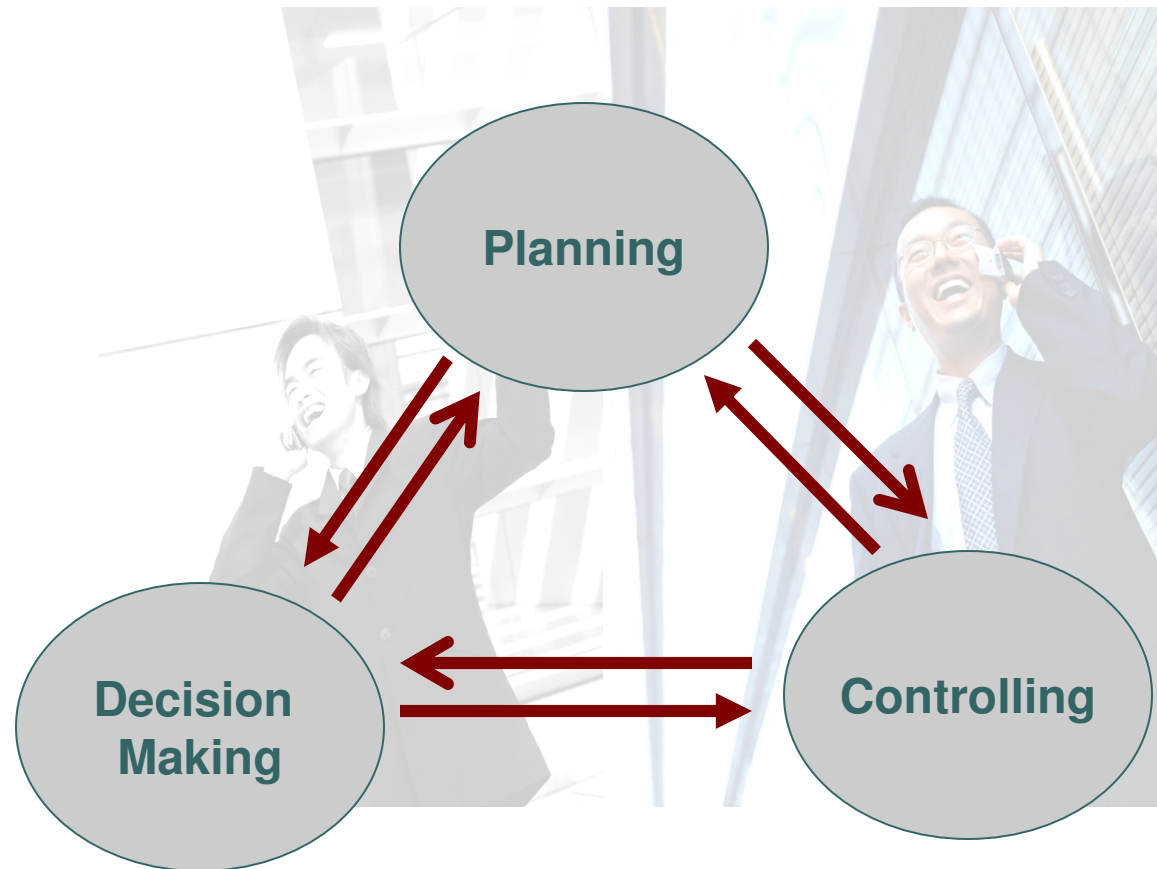
At all levels of
management

Why Does Management Need Information

- To make plans
- Monitor performance
- Take one-off decisions



Information for Planning, Control and Decision Making



Information vs. Data



Data has no clear meaning until it is processed, analysed and organised into information

Qualities of Good Information

- Understandable
- Relevant and purposeful
- Timely
- Accurate
- Complete but not excessive
- Communicated to the right person
- Value of information > Cost of producing it
- Communicated by appropriate channel

Value of Information

- Value of information helps in:
 - Reducing unnecessary costs
 - Adopting better marketing strategies
 - Better analysis of cost drivers
 - Optimising techniques

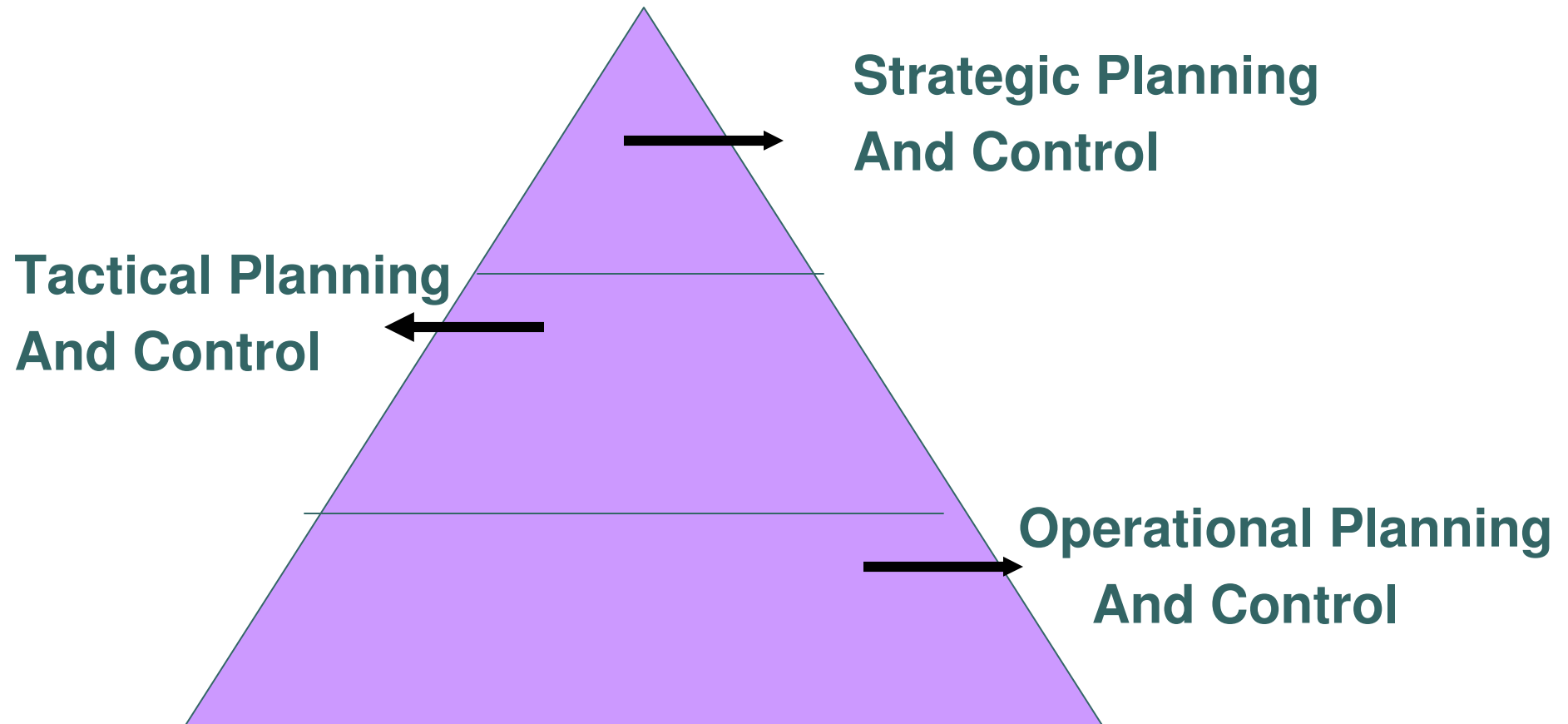
Assessing Value of Information

- Who uses the information?
- What is it used for?
- How often is it used?
- How often it is provided but not used?
- What is achieved by its use?

Cost of Information

- Cost of gathering data
- Cost of processing data
- Cost of storing data and information
- Cost of providing information

Planning Hierarchy





- A **process**
- Of **deciding on objectives** of the organisation
- On **changes in these objectives**
- On **resources** used to attain these objectives
- **Policies** that govern the acquisition, use and disposition of these resources

Examples: Strategic Planning

- Selection of products
- Markets to sell the product in
- Required level of company profitability
- Purchase and disposal of companies
- Purchase and disposal of major fixed assets
- Total manning needs
- Raising new funds

Management Control

- A process by which the managers assure that resources are obtained and used effectively and efficiently in the accomplishment of the organisation's objectives.
- Also called **Tactical planning**
- **Examples:** setting budgets for sales, production etc.

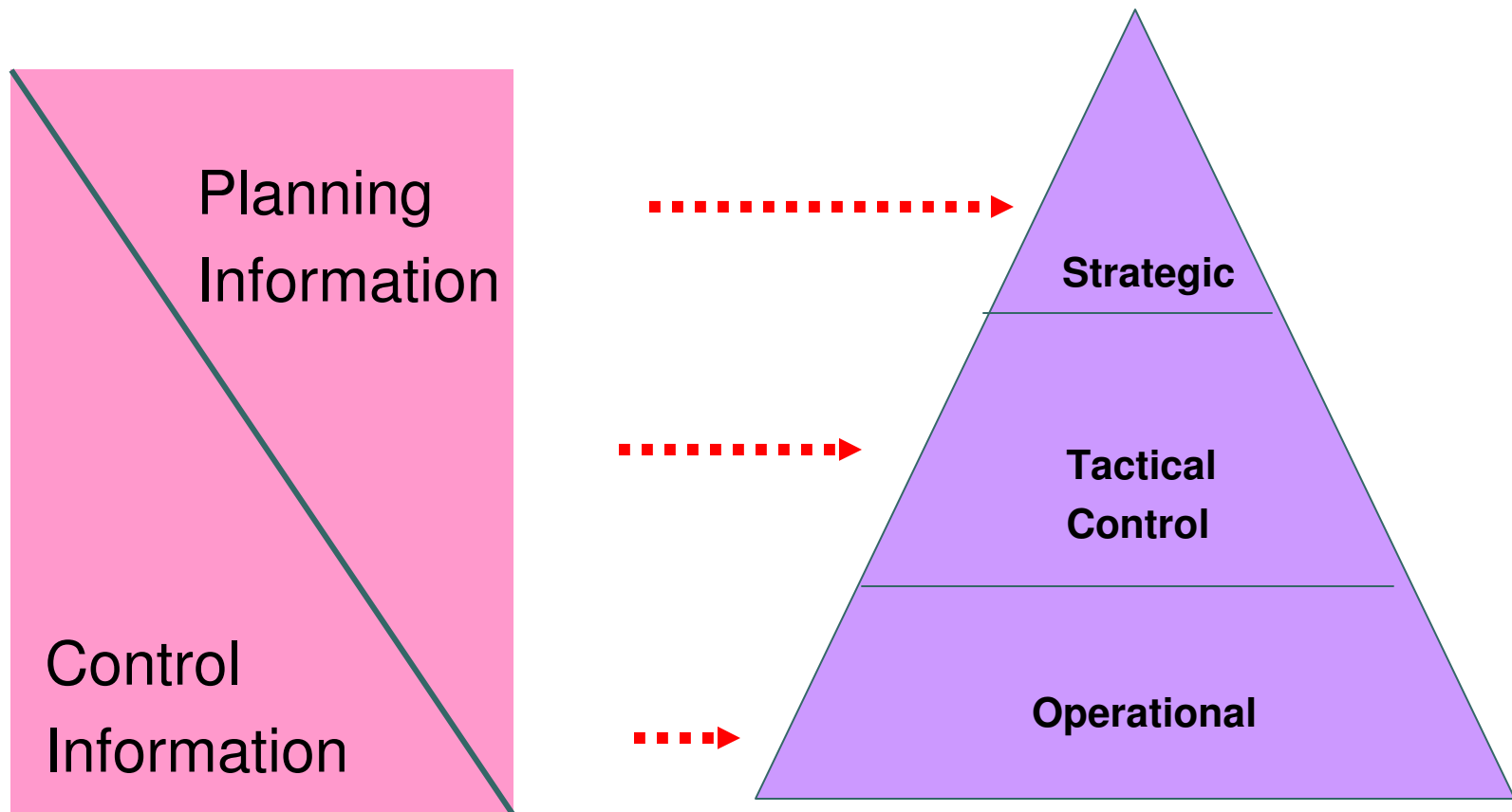


Operational Control

- Also called **operational planning**
- Process of assuring that specific tasks are carried out effectively and efficiently
- **Example:** allocation of particular staff to particular tasks, handling customer complaints etc.

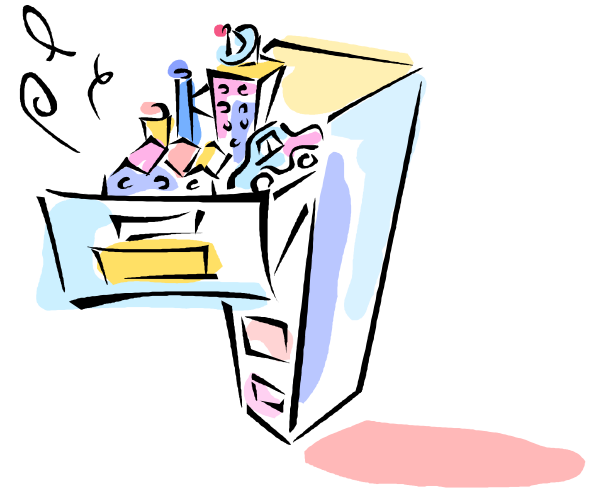


Type of Information Requirements



Sources of Information

- Inside and outside the organisation
- Structured information systems
- Non-structured ways



Structured Internal Information System

- Gathers data within the organisation and then processes the data to provide reports to management
- All businesses have a structured system for financial accounting and financial reporting
- Many businesses also have cost accounting system or management accounting system

Responsibility Accounting

A system of providing financial information to management, where the structure of the reporting system is based on identifying individual parts of a business which are the responsibility of a single manager

Cost

- A cost may be defined as a sacrifice or giving up of resources for a particular purpose.
- Costs are frequently measured by the monetary units that must be paid for goods and services.
- Costs are different from expense

Cost Object

- Anything for which a separate measurement of costs is desired.
 - Cost of making a product
 - Cost of service
 - Cost of department
 - Cost of Sales Region

Cost Driver

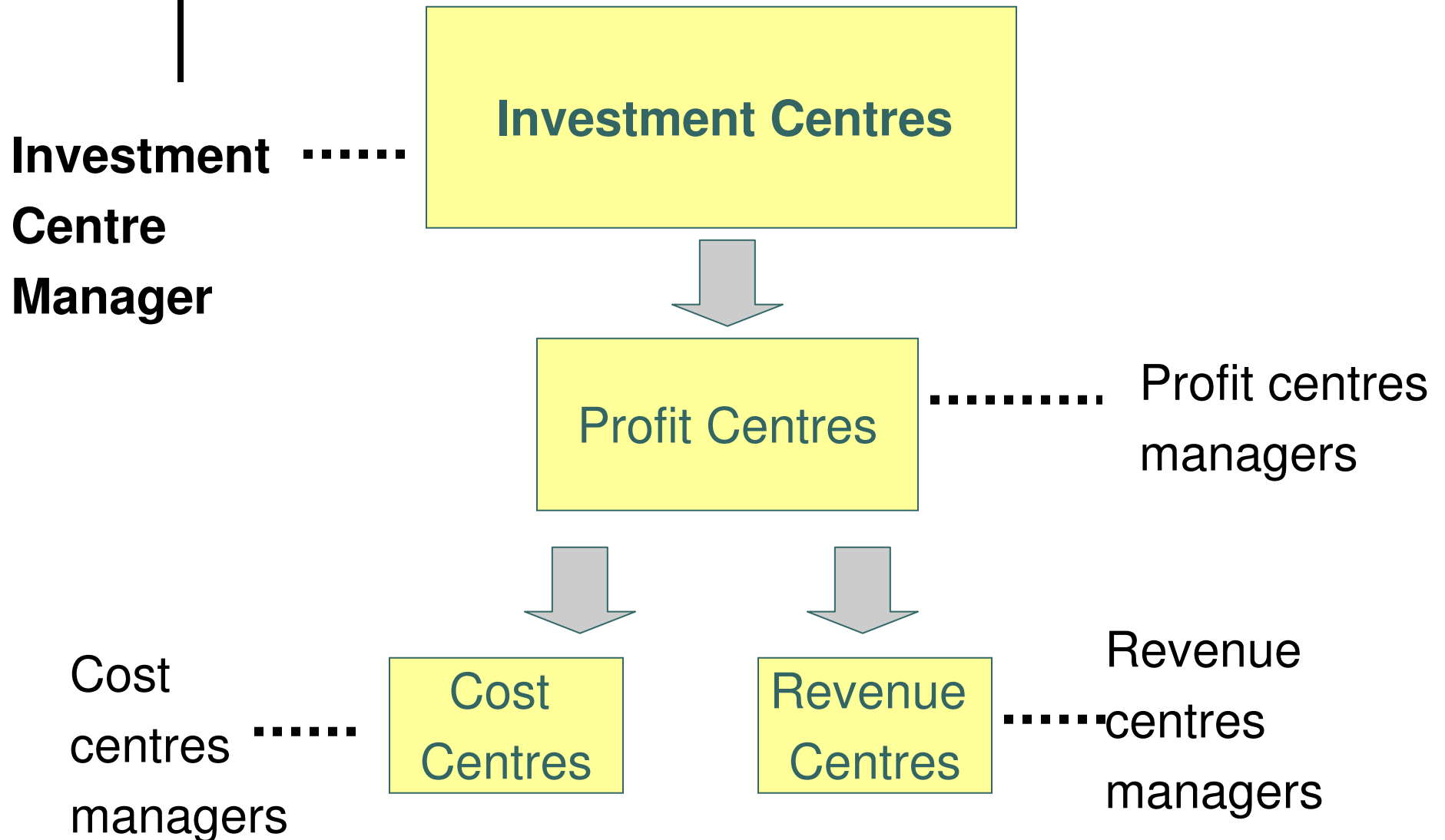
Any factor whose change causes a change in the total cost of a related cost object



Cost Units

- A unit of product or service in relation to which costs are ascertained
 - For an accountancy firm the cost unit might be the hours of work provided to client

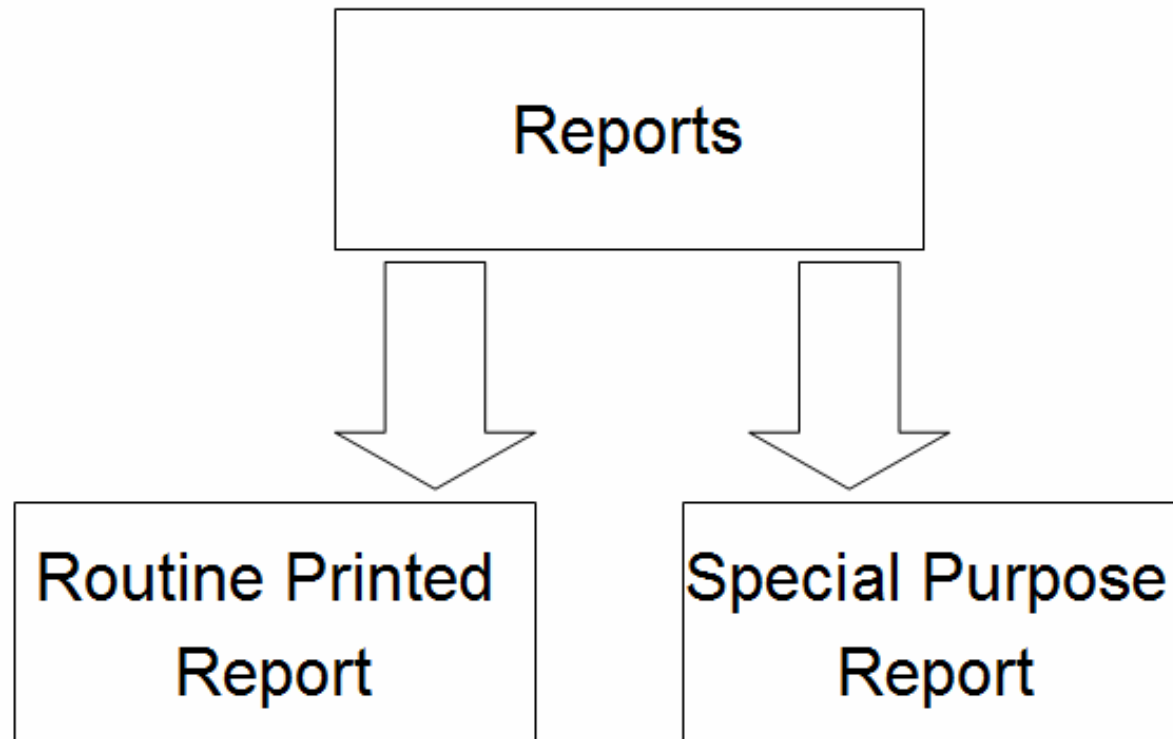
Hierarchy of Responsibility Centres



Impact of Responsibility Accounting On Management Information

- A responsibility centre affects the nature of management reporting. Managers need enough information to control their responsibility centres.

Presenting Information to Management



Principles of Writing Reports

- Conciseness
- Structure
- Style
- Presentation
- Graphical

Sample Exam Question

- Which of the following is correct about data and information?
 - A. Information collected from external sources cannot be classified as data
 - B. Strategic information deals with formulation of short-term plans only
 - C. Data can be discrete or continuous
 - D. Non-financial data is classified as processed information

Answer

- C
- Data can be discrete or continuous. A set of data is said to be discrete if the values belonging to it are distinct and separate.

Sample Exam Question

- Mark is a profit centre manager. What is he responsible for in his segment of the organisation?
 - A. Costs only
 - B. Revenues only
 - C. Both costs and revenues
 - D. Cost, revenue as well as investment

Answer

C

A profit centre manager is responsible for both costs and revenues of his centre.