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## **INTRODUCTION TO MANAGEMENT ACCOUNTING**

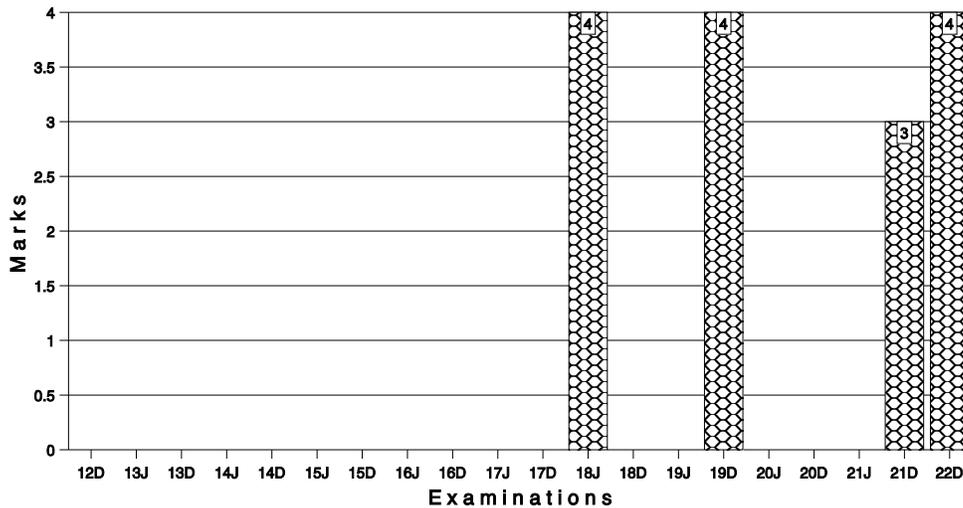
### **THIS CHAPTER INCLUDES**

- Conceptual Understanding
- Relationship between Management Accounting and Cost Accounting
- Role of a Management Accountant in Modern Business World

Marks of Objective, Short Notes, Distinguish Between, Descriptive & Practical Questions

### **Legend**

 Objective  Short Notes  Distinguish  Descriptive  Practical



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## CHAPTER AT A GLANCE

### What is Management Accounting?

Management Accounting comprise of two terms 'management' and 'accounting'. Management accounting is accounting (i.e. producing useful information) for management (people with the task of running the business). In this sense, management accounting includes the production of all information useful in running the organisation.

### Scope of Management Accounting

Some of the broad areas considered to be part of 'management accounting' is summarised in the following lines.

- Budgeting, planning and forecasting
- Measuring organisational, divisional and departmental performance
- Comparing results and performance within and between organisations
- Assisting in the process of increasing effectiveness and efficiency
- Assessing the performance of past and future capital investments
- Advising on decisions about product mix, markets to be served and selling prices
- Advising on decisions on whether to outsource products, components, activities and services
- Advising on decisions involving the investment of scarce funds between a range of possible alternatives
- Assisting in the making of a wide range of strategic decisions

### The key difference between financial accounting and management accounting is

Basis for Comparison	Financial Accounting	Management Accounting
<b>Purpose</b>	Financial Accounting classifies, analyses, records, and summarizes	Management accounting helps management

	the financial transactions of a particular period of the company.	make effective decisions about the business.
<b>Application</b>	Financial accounting is prepared to reflect true and fair picture of financial affairs.	Management accounting helps management to take meaningful steps and strategize.
<b>Scope</b>	The scope is pervasive, but not as much as the management accounting.	The scope is much broader.
<b>Information type</b>	Quantitative.	Quantitative and qualitative.
<b>Inter dependence</b>	It is not dependent on management accounting.	Management accounting is basically decision making accounting and depends on information created by Financial Accounting as well as Cost Accounting.
<b>Statutory requirement</b>	It is legally mandatory to prepare financial accounts of all companies. (for example in the Indian Context Companies Act 2013, relevant rules of Accounting standards furnishes the statutory requirements)	Management accounting has no statutory requirement.
<b>Format</b>	Financial accounting has specific formats for presenting and recording information.	There's no set format for presenting information in management accounting.
<b>Users</b>	Mainly for potential investors as well as all stakeholders.	Only for management;
<b>Verifiable</b>	The information presented is	The information

	verifiable.	presented is predictive and not immediately verifiable.
<b>Cost Accounting and Management Accounting – a comparative analysis</b>		
<b>The Basis for Comparison</b>	<b>Cost Accounting</b>	<b>Management Accounting</b>
<b>Meaning</b>	Cost accounting revolves around cost computation, cost control, and cost reduction.	Management accounting helps management make effective decisions about operations of the business.
<b>Application</b>	Cost accounting prevents a business from incurring costs beyond budget.	Management accounting offers a big picture of how management should strategize.
<b>Scope</b>	The scope is much narrower.	The scope is much broader.
<b>Measuring grid</b>	Quantitative.	Quantitative and qualitative.
<b>Sub-set</b>	Cost accounting is one of the many sub-sets of management accounting.	Management accounting is the universal set.
<b>Basis of decision making</b>	The task of decision making very less. Even if there is some, it is based on historic information	Historic and predictive information is the basis of decision-making.
<b>Statutory requirement</b>	Statutory audit of cost accounting is a requirement in some specified industries	The audit of management accounting has no statutory requirement.
<b>Dependence</b>	Cost accounting isn't dependent on management	Management accounting is dependent on both cost &

	accounting to be successfully implemented.	financial accounting for successful implementation.
<b>Used for</b>	Management, shareholders, and vendors.	Only for management.

### Functions of the Management Accountant

- (a) **Planning and Accounting:** Management accountants prepare an accounting system covering costs, sales forecasts, profit planning, production planning, and allocation of resources. It should also include capital budgeting, short-term and long-term financial planning.
- (b) **Controlling:** Management accountants assist in the control of an organization's performance through the use of standard costing, budget control, accounting ratios, funds flow statements, cost-cutting initiatives, and assessing capital expenditure proposals and returns on investment.
- (c) **Reporting:** Management accountants assist the top management in finding out the root cause of an unfavorable operation or event by identifying the real reasons for the adverse events as well as the responsible parties and comprehensively reporting them.
- (d) **Coordinating:** Management accountants improve an organization's efficiency and profits by providing various coordination tools such as budgeting, financial reporting, financial analysis and interpretation.
- (e) **Communication:** Management accountants create a wide range of reports to communicate results to the superiors. Through published financial statements and returns, they also inform the outside world about their company's success.
- (f) **Financial evaluation and Interpretation:** Management accountants analyze the data and present it to the management in a non-technical approach, together with their comments and ideas, so that the shareholders and senior management can understand it and make informed decisions.
- (g) **Tax Administration:** Management accountants are in charge of tax policies and processes. They make the reports that are required by various authorities.

- (h) **Evaluation of external effects:** There may be changes in government policy and existing laws. These amendments and policy changes can affect business goals. Management accountants assess the extent of any impact of these external factors on the business and report it to the stakeholder to take necessary precautionary measures.
- (i) **Economic appraisal:** When the government makes regular announcements about the country's economic situation, management accountants is entrusted with making the economic study and determine the influence of current economic conditions on the company's operations. They compile a report containing their observations and present it to high management.
- (j) **Asset Protection:** Management accountants separate fixed asset registers for each type and provide internal checks and controls to protect the company's assets. They also create the rules and regulations for each type of fixed asset and get insurance coverage for all types of fixed assets.

## SHORT NOTES

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**2018 - June [5]** Write short note on the following.

(a) Concept of Management Accounting.

**(4 marks)**

**Answer:**

Management Accountants (also called managerial accountants) look at the events that happen in and around a business while considering the needs of the business. From this, data and estimates emerge. Cost accounting is the process of translating these estimates and data into knowledge that will ultimately be used to guide decision-making.

The main difference between **financial and managerial accounting** is whether there is an internal or external focus. **Financial accounting** focuses on creating and evaluating financial statements that will be reported externally, like creditors and investors. In contrast, **managerial accounting**

analyses and results are kept in-house for business leaders to use to drive decision-making and run the company more effectively. Managerial accountants handle many facets of accounting. These include margins, constraints, capital budgeting, trends and forecasting, valuation and product costing.

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**2019 - Dec [5] Write short note on the following:**

(a) Significance of Management Accounting.

**(4 marks)**

**Answer:**

**Significance of Management Accounting:**

**The various advantages of management accounting are discussed below:**

1. **Delegation of Authority:** Now a days the function of management is no longer personal. Management accounting helps the organization in proper delegation of authority for the attainment of the vision and mission of the business.
2. **Need of the Management:** Management Accounting plays the role in meeting the need of the management.
3. **Qualitative information:** Management Accounting accumulates the qualitative information so that management would concentrate on the actual issue to deliberate and attain the specific conclusion even for the complex problem.
4. **Objective of the Business:** Management Accounting provides measure and reports to the management thereby facilitating in attainment of the objective of the business.

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**2021 - Dec [4] Write Short Note on Significance of Management Accounting  
(3 marks) [Sec. C Six LAQ]**

**Answer :**

***Please refer 2019 - Dec [5] (a) on page no. 17***

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2022 - Dec [5] Write short note on the following:

(a) Strategic Management Accounting

(4 marks)

TOPIC NOT YET ASKED BUT EQUALLY IMPORTANT FOR EXAMINATION

## DESCRIPTIVE QUESTIONS

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**Q1.** What is Management Accounting? Discuss the Significance of Management Accounting.

**Answer:**

“Management Accounting is concerned with the efficient management of a business through the presentation to management of such information that will facilitate efficient planning and control”. — Brown and Howard

**Management Accounting is an integral part of management concerned with identifying, presenting and interpreting information for:**

1. Formulating strategy
2. Planning and controlling activities
3. Decision taking
4. Optimizing the use of resources
5. Disclosure to shareholders and others, external to the entity
6. Disclosure to employees
7. Safeguarding assets

**The various advantages that accrue out of management accounting are enumerated below:**

- (1) **Delegation of Authority:** Now a day the function of management is no longer personal, management accounting helps the organisation in proper delegation of authority for the attainment of the vision and mission of the business.
- (2) **Need of the Management:** Management Accounting plays the role in meeting the need of the management.

- (3) **Qualitative Information:** Management Accounting accumulates the qualitative information so that management would concentrate on the actual issue to deliberate and attain the specific conclusion even for the complex problem.
- (4) **Objective of the Business:** Management Accounting provides measure and reports to the management thereby facilitating in attainment of the objective of the business.

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**Q2.** Discuss the role of Management Accounting in Management process.

**Answer:**

The role of Management Accounting is significant in making the firm both efficient and effective. Management Accounting has brought out clear shift in the objective of accounting. From mere recording of transactions, the emphasis is on analyzing and interpreting to help the management to secure better results. In this way, Management Accounting eliminates intuition, which is not at all dependable, from the field of business management to the cause and effect approach.

**Management accounting plays a vital role in the managerial functions performed by the managers:**

1. **Planning:** Planning is the real beginning of any activity. Planning establishes the objectives of the firm and decides the course of action to achieve it. It is concerned with formulating short-term and long-term plans to achieve a particular end.  
While planning, management accountant uses various techniques such as budgeting, standard costing, marginal costing etc. for fixing targets.
2. **Organising:** Organising is a process of establishing the organizational framework and assigning responsibility to people working in the organization for achieving business goals and objectives.  
The management accountant may prepare reports on product lines, based on which managers can decide whether to add or eliminate a product line in the current product mix.

3. **Controlling:** Control is the process of monitoring, measuring, evaluating and correcting actual results to ensure that a firm's goals and plans are achieved. Control is achieved through the process of feedback. Feedback allows the managers to allow the operations continue as they are or take corrective action, by some rearranging or correcting at midstream.
4. **Decision-Making:** Decision-Making is a process of choosing among competing alternatives. Decision-making is inherent in all the above three functions of management planning, organizing and controlling. There may be different methods or objectives. The manager can plan or choose only one of the competing plans.
5. **Staffing:** Staffing is the process of recruitment, selection, development, training, compensation and overseeing employee in an organisation. The role of the management accounting in this regard is manning the entity structure through proper and effective selection, appraisal, and development of the personnel to fill the role assigned to the employer.

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**Q3.** State the functions of Management Accounting.

**Answer:**

The primary objective of Management Accounting is to maximize profits or minimize losses. This is done through the presentation of statements in such a way that the management is able to take corrective policy or decision. The manner in which the Management Accountant satisfies the various needs of management is described as follows:

1. **Storehouse of Reliable Data:** Management wants reliable data for Planning, Forecasting and Decision-making. Management accounting collects the data from various sources and stores the information for appropriate use, as and when needed. Though the main source of data is financial statements, Management Accounting is not restricted to the use of monetary data only.

2. **Modification and Presentation of Data:** Data collected from financial statements and other sources is not readily understandable to the management. The data is modified and presented to the management in such a way that it is useful to the management.
3. **Communication and Coordination:** Targets are communicated to the different departments for their achievement. Coordination among the different departments is essential for the success of the organisation.
4. **Financial Analysis and Interpretation:** Management accounting helps in strategic decision making. Top managerial executives may lack technical knowledge. Accountant gives facts and figures about various policies and evaluates them in monetary terms.
5. **Control:** It is absolutely essential that there should be a system of monitoring the performance of all divisions and departments so that deviations from the desired path are brought to light, without delay and are corrected then and there. This process is termed as control. For the discharge of this important function, management accounting provides meaningful information in a systematic and effective manner.
6. **Supplying Information to Various Levels of Management:** Every level of management requires information for decision-making and policy execution. Top-level management takes broad policy decisions, leaving day-to-day decisions to lower management for execution. Supply of right information, at proper time, increases efficiency at all levels.
7. **Reporting to Management:** Reporting is an important function of management accounting to achieve the targets. The reports are presented in the form of graphs, diagrams and other statistical techniques so as to make them easily understandable.

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**Q4.** Discuss the limitation of Management Accounting.

**Answer:**

Despite the development of Management Accounting as an effective discipline to improve the managerial performance, some of the limitations are as under:

1. **Accuracy is not Ensured:** Management Accounting is largely based on estimates. It does not deal with actual, alone, and thus total accuracy is not ensured under Management Accounting.
2. **A Tool in the Hands of Management:** Management Accounting is definitely a tool in the hands of management, but cannot replace management.
3. **Strength and Weakness:** Management Accounting derives information from Financial Accounting, Cost Accounting and other records. The strength and weakness of these basic information providers become the strength and weakness of Management Accounting too.
4. **Costly Affair:** The installation of Management Accounting is a costly affair so all the organizations, in particular, small firms cannot afford.
5. **Lack of Knowledge and Understanding:** The emergence of Management Accounting is the fusion of a number of subjects like statistics, economics, engineering and management theory. Any inadequate grounding in any one or more of the subjects is bound to have an unfavourable effect on the consideration and solution of the problems, relating to management performance.
6. **Evolutionary Stage:** Comparatively, Management Accounting is a new discipline and is still very much in a stage of evolution. Therefore, it comes across the same difficulties or obstacles, which a relatively new discipline has to face.
7. **Psychological Resistance:** Adoption of a system of Management Accounting brings about a radical change in the established pattern of the activity of the management personnel. It calls for rearrangement of personnel as well as their activities. This is bound to encounter opposition from some quarter or other.

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