

King Fahd University of Petroleum and Minerals

College of Industrial Management

Department of Accounting & MIS

ACCT 510: Managerial Accounting

MBA Program

## Chapter 7 (Lecture Notes)

### Management Accounting and Control Systems (MACS)

**The Concept of Control:** refers to set of procedures, tools, techniques, performance measures, and systems that organizations use to guide and motivate all employees to achieve organizational objectives.

**In control:** refers to a system that is on the path to achieving its strategic objectives.

**Out of control:** a state when a system is not on a path to achieving organizational objectives.

The process of keeping an organization in control consists of five stages:

- **Planning:** consists of developing an organization's objectives, choosing activities to accomplish the objectives, and selecting measures to determine how well the objectives were met.
- **Execution:** Implementation of plans.
- **Monitoring:** the process of measuring the system's current level of performance.

- Evaluation: occurs when feedback about the system's current level of performance is compared to the planned level so that any discrepancies can be identified and corrective action prescribed.

**Correcting consists** of taking appropriate actions to return the system to in control state.  
e.g Excessive defect rates for a new product may suggest a flawed product design.  
Management may then want to reevaluate their product strategies.

Characteristics of Well-Designed MACS

**Behavioral considerations:**

- Embedding the organization's ethical code of conduct into MACS design.
- Using a mix of short-term and long-term qualitative and quantitative performance measures (or the balanced scorecard approach, see pp. 408-409)
- Empowering employees to be involved in design making and MACS design, and
- Developing an appropriate incentive system to reward performance (see pp. 417-421)

**Technical considerations**

a. Relevance of Information: measured by four characteristics:

- Accurate e.g use costing systems/ procedures that trace costs to activities.
- Timely: late information is of little use for decision making. Information must be fed back to appropriate units in the most expedient way possible
- Consistency: Designers must structure the MACS to provide a consistent framework. Consistency means the language used and the technical methods of producing and reporting management accounting information do not conflict within various parts of the organization.

- **Flexibility:** to accommodate the local needs of all divisions. In absence ad hoc system may develop which can lead to poor decisions and confusion.

b. **Scope of the system:** the scope of the MACS must be comprehensive and include all activities across the entire value chain of activities.

**The Value chain:** a sequence of activities that contribute to the ultimate value of the product.

**Total-life-cycle costing:** the process of managing all costs along the value chain. TLCC system provides information to managers to understand and manage costs through a product's design, development, growth, manufacturing growth, marketing, distribution, maintenance, service and disposal stages.

**Note Traditional focus of management accounting has been only on the manufacturing process**

**Target costing:** is a method of profit planning and cost management that focuses on products with discrete manufacturing processes.

The goal of target costing is to design costs of the product during its RD & E stage of a product total life cycle rather than to reduce the costs during the manufacturing stage.

**Concern about Target Costing**

- Conflicts can arise between various parties involved in the target costing process. Often companies put excessive pressure on subcontractors and suppliers to conform to schedule and reduce costs

- Employees in many Japanese companies working under target costing goals experience burnout due to pressure to meet the target cost (e.g design engineers)
- Increase in development time because of repeated value engineering cycles to reduce cost and hence delay in the product coming late to market.

**Value Engineering process:** includes examination of each component of a product to determine whether it is possible to reduce costs while maintaining functionality and performance.

**Supply Chain Management:** A management system that develops cooperative, mutually beneficial, long-term relationships between buyers and sellers.

**Benchmarking:** A technique which is used by companies to aid them to understand the best practices of other companies and how to apply what they learn to their organizations.

### **Benchmarking Process:**

Four Stages (see pp. 299-302)

#### A. Internal Study and Preliminary Competitive Analysis

The organization identify what key areas to benchmark for the study e.g profit, sales and cost performance; products, management accounting methods

#### B. Developing long-term commitment to the benchmarking Coalescing the benchmarking team

e.g gaining senior management support, develop a clear set of objectives, empower employees to make change, use experienced coordinator.

#### C. Identifying benchmarking partners: willing participants who know the process

Some critical factors:

- Size of partners: depend on the specific activity
- Number of partners: considering a wide array of partners
- Relative position of partners within and across industries e.g. established industry leader
- Degree of trust among partners

#### D. Information gathering and sharing methods

##### **Type of information**

##### **Three broad classes of information focus:**

1. Product benchmarking: examining other organizations' products
2. Functional process benchmarking: study of other organizations' practices and costs with respect to functions or processes
3. Strategic benchmarking: study of others' strategies and strategic decisions

##### **Methods of gathering information:**

- Unilateral (covert) benchmarking: companies independently gathering information about one or several others companies (from trade associations)
- Cooperative benchmarking: voluntary sharing information through mutual agreements:

##### **Three categories:**

1. Database benchmarking: pay a fee for information and gain access

Advantage: existence of a large amount of data in one place

2. Indirect/third-party benchmarking: uses an outside consultant to act as a liaison among firms engaged in benchmarking

3. Group benchmarking: participants meet openly to discuss their methods. They coordinate their efforts, define common terminology, visit each other's Sites.

5. Taking action to meet or exceed the benchmark