DECISION MAKING AND THE ROLE OF MANAGEMENT ACCOUNTING FUNCTION – A REVIEW OF EMPIRICAL LITERATURE

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Abstract

This study examines decision making and the role of management accounting function in a business organization. Using the review of literature, I identify management accountants perform a wide variety of tasks. Only a part of management accounting activity is directed at performance improvement. Some of the activities they perform are related to the statutory reporting requirements of the organization. Some of these are related to the operational requirements of the finance function itself such as processing transactions receiving money and paying bills. Literature foresees new management accounting techniques and changes in organizational and business environments having a huge impact on management accountants’ roles, yet empirical evidence on fundamental shifts in these roles remains relatively scarce.
INTRODUCTION

Accounting can be defined as "the process of identifying, measuring and communicating economic information to permit informed judgments and decisions by users of the information" (Hogget and Edwards, 1987). The information in accounting systems relates mainly to financial data about business transactions, which is presented in monetary terms. In addition to presenting financial information about past transactions, the accounting system enables to generate forecasts and predictions as an aid to decision making.

Accounting is sometimes referred to as the “language of business”. It offers a medium through which the marketing, production, human resources and other impacts of a decision may be reflected in monetary terms. This indicates the way in which most companies use accounting and finance as an integrative function to show the combined consequences of a proposed course of action on the firm's financial situation.

The American Accounting Association formulated the definition of Accounting as the process of identifying, measuring, and communicating economic information to permit informed judgments and decisions by users of the information. Accounting is a language that communicates economic information to people who have an interest in an organization- managers, shareholders, potential investors, creditors, government and the employees. The accounting literature identifies quite a number of specialized fields of accounting. Among them, financial accounting is the original field of accounting. Its main purpose is to record transaction details in monetary terms and
prepare financial statements and reports in accordance with GAAP. The other part of accounting, Management accounting provides necessary information to assist management in decisions making and management control.

Management accounting provides necessary information to assist management in decisions making and management control. The Chartered Institute of Management Accountants (2001) describes Management Accounting as: - the application of professional information in such a way as to assist the management in the formation of policies and in the planning and control of the operations of the undertaking. Management accounting has been considered as an integral part of the management process, and management accountants have been visualized as important strategic partners in an organization's management team. Hilton (1999) states that the management team seeks to create value for the organization by managing resources, activities, and people to achieve organizational goals effectively. To this end, managers require information which is utilized in the decision making process and in controlling operations. Management accounting thus serve management in providing the needed data and information, including advice and recommendations. Although there is no commonly accepted definition of “management accountant”, for the purposes of this study, I use the term to refer to all people who report directly or indirectly to the finance function of an enterprise.

OBJECTIVE OF THE STUDY

The main objective of the present study is to identify the types of managerial decisions and the role of management accountant in decision-making process in a business organization.
RESEARCH METHODOLOGY

The source for the data is entirely from secondary sources i.e., from books, published and unpublished journals, related websites in the internet, and other documents that are related to the topic under study.

LITERATURE REVIEW

DECISION MAKING

Decision making is a fundamental part of management. Before discussing what decision-making is, let us discuss what decision is, because decision-making is a process of deciding. Collins (1999) defines decision as the act of making up one’s mind by collecting, sharing and gathering significant ideas from different sources. Moreover, Longman (2000) defines that “decision as a choice or judgment that you make after a period of discussion or thought”. Longman’s definition is very clear but it gives rise to a question on the definition of deciding or decision-making. In the end decision-making is to make a choice or judgment about something, especially after a period of not knowing what to do or in way that ends in disagreement (Alam, 2008).

Moreover, Fullan (1982) asserts that decision-making is the process of identifying and choosing alternative courses of action in a manner appropriate to the demand of the situation. The act of choosing implies that alternative courses of action must be weighed and weeded by sharing. Fremount, et, al,. 1970 defined decision-making as the “conscious and human process, involving both individual and social phenomenon based upon factual and value premises, which concludes with a choice of one behavioral activity from among one or more alternatives with the intention of moving
toward some desired state of affairs”. It represents a course of behavior or action about what must or must not be done (Herbert, 1960). Decision making is the selecting of action from among alternatives to achieve a specific objective or solve specific problem (Donald, 1963). The art of decision-making provide us a variety of approaches, methods and techniques helpful and useful for making high quality of decision. A decision maker, as an individual, or as a member of formal organization with his own philosophy and perception of the organization, selects for optimizing values within the constraints imposed by the organization (Varshney, 1997).

Decision-making and its role in organizations can be viewed in a number of ways. Kreitner (1999) believes good management can be defined in terms of good coordination of an organization’s employees. Mullins (2000), Moorhead and Griffin (2000) posit that decision making is one of the first and a crucial step in management. Criteria of decision and its nature vary in terms of kinds and types. Decision-making is the backbone of administrative functions. This is because decisions direct actions (Marvin, cited in Igwe, 1995). Good and effective decisions can only be made when right information is made available at the right time to the right recipient. Johnson, Newell and Vergin (1972) stated that information for decision-making is dynamic; therefore, it needs to be constantly up-dated. Decision-making, itself, is a dynamic process (Harrison, 1995; Daft, 1983). Managers need continuous flow of information in order to make appropriate decisions. Decision-making efficiency of managers can therefore be greatly enhanced by the quality of information they are able to utilize in decision-making.

Right decisions give direction for a right course of action. Daft (1983) stated that when an organization is designed to provide correct information to managers, decision processes work extremely well and tasks will be accomplished. However, when
information is poorly designed, problem-solving and decision processes will be ineffective and managers may not understand why.

An individual or multiple participants that are involved in decision-making can be called decision makers. Individual decisions can be made by a computer or a single person meanwhile the multi participant decision makers can be divided into unilateral and negotiated decisions. In the first one, which is also called team decisions, one of the participants has the power to decide. The others although, can highly influence how the decision will look like. In negotiated decisions the participants share the authority of making a decision. This type distinguishes between group decisions where the participants have nearly equal authorities and discuss their different viewpoints in various meeting and organization decisions. In the latter one the authority of making a decision is unequally shared according to the organizations hierarchy and the coordination between the decision participants is highly structured.

Classification of decisions

From the descriptive model of the basic features and assumptions of the management accounting perspective of business, it is easy to recognize that decision-making is the focal point of management accounting. The concept of decision-making is a complex subject with a vast amount of management literature behind it. How businessmen make decisions has been intensively studied. In management accounting, it is useful to classify decisions as:

1. Strategic and tactical

2. Short-run and long-run
Strategic and Tactical Decisions

In management accounting, the objective is not necessarily to make the best decision but to make a good decision. Because of complex interacting relationships, it is very difficult, even if possible, to determine the best decision. Management decision-making is highly subjective.

Whether a decision is good or acceptable depends on the goals and objectives of management. Consequently, a prerequisite to decision-making is that management has set the organization’s goals and objectives. For example, management must decide strategic objectives such as the company’s product line, pricing strategy, quality of product, willingness to assume risk, and profit objective.

In setting goals and objectives, it is useful to distinguish between strategic and tactical decisions. Strategic decisions are broad-based, qualitative type of decisions which include or reflect goals and objectives. Strategic decisions are non quantitative in nature. Strategic decisions are based on the subjective thinking of management concerning goals and objectives. A strategic decision is one which is made during a current time but whose primary effect will be felt during some future time. Strategic decisions affect organizational structure and objectives. Strategic decision cannot be delegated lower than a particular level (March, 1988).

Tactical decisions are tactical in nature and called routine decision. They are important repetitive need little thoughts with few alternatives. The decision are taken up by middle and first line managers and do not involve any higher risk or uncertainty. Tactical decisions support and compliment organizational strategy. The tactical decision may be delegated to lower levels in the organization. Moreover, what might
be strategies decision for one organization may be tactical decision for another? (Prasad, 1997)

Tactical decisions are quantitative executable decisions which result directly from the strategic decisions. The distinction between strategic and tactical is important in management accounting because the techniques of management accounting pertain primarily to tactical decisions. Management accounting does not typically provide techniques for assisting in making strategic decisions.

Once a strategic decision has been made, then a specific management tool can be used to aid in making the tactical decision. For example, if the strategic decision has been made to avoid stock outs, then a safety stock model may be used to determine the desired level of inventory.

The classification of decisions as strategic and tactical logically results in thinking about decisions as qualitative and quantitative. In management accounting, the approach to decision-making is basically quantitative. Management accounting deals with those decisions that require quantitative data. In a technical sense, management accounting consists of mathematical techniques or decision models that assist management in making quantitative type decisions.

**Short-run Versus Long-run Decision-making**

As stated above, decisions can be grouped into short- and long-term decisions. It is necessary to consider decisions from both perspectives. Drury (2000) defined the short-term is usually as being one year or even less. In short-term decisions the
importance of the time value of money is low. These decisions are mainly based on today’s data. Short-term decisions can usually be changed easily as opposed to long term ones. Operating activities encompass what managers must do to run the business on a day-to-day basis. Operating decisions for manufacturing companies include whether to accept special orders, how many parts or other raw materials to buy (or whether to make the parts internally), whether to sell a product or process it further, whether to schedule overtime, which products to produce, and what price to charge. Other operating decisions affecting all organizations include assigning tasks to individual employees, whether to advertise, and whether to hire full-time employees or to outsource.

Long-term decisions have effects on longer periods of time. Consequently, such decisions demand a firm’s resources for a longer episode of time. Such decisions can influence future decisions and can have an impact on long-term potentials. Strategic planning addresses long-term questions of how an organization positions and distinguishes itself from competitors. Long-term decisions about where to locate plants and other facilities, whether to invest in new state-of-the-art production equipment, and whether to introduce new products or services and enter new markets are strategic planning decisions. Strategic planning also involves the determination of long-term performance and profitability measures, such as market share, sales growth, and stock price.

MANAGEMENT ACCOUNTANT’S ROLE IN DECISION MAKING

The decision making process can be looked at as a group of people (decision makers, agents, actors) trying to decide on the correct actions to achieve goals using
information about the results of past actions. It is clear that management accountants have - as they've always had - a significant contribution to make at each stage of the decision-making process (see figure 1.1 below). This is good news for financial managers who have technical know-how, understand the business and use good communication and influencing skills.

The decision-making process can be characterized by the following (Peter Simons, 2007):

- Decision-making is not the end of the process. It extends through to achieving results and is a continuous process.
- Accountants contribute to the strategic planning and enterprise governance framework (the CIMA Strategic Scorecard), which articulates the business's competitive position and objectives,
- Individuals' personal contexts and attitudes can impair decision-making, but business partners can address this problem by championing evidence-based decision-making.
- Business partners can help to "frame" a decision, provide management information, and contribute insights and analyses alternatives to help the decision maker.
Figure 1.1: depicts the six steps in the decision process, and the relationship between quantitative and qualitative analysis.

1. Clarify the decision
2. Specify the criterion
3. Identify the alternatives
4. Develop a decision model
5. Collect the data
6. Make a decision

Source: Adapted from Hilton et al., 2008
The managerial accountant’s role in the decision-making process is to provide data relevant to the decision. Managers can then use these data in preparing a quantitative analysis of the decision. Qualitative factors are considered also in making the final decision. In order to be relevant to a decision, a cost or benefit must: (1) bear on the future, and (2) differ under the various decision alternatives.

**Tasks of managerial accountants**

In business organizations, accountants have remained to be primary providers of financial data and analytical reports on which managers rely to pass decisions. The paper by M. Newman, C. Smart and I. Vertinsky (1989) suggest that major tasks of management accountants are score-keeping and maintenance of financial records for internal and external users. However, in 1995 R. Kaplan identified new tasks and roles for management accountants. Kaplan (1995) proposes that in the future management accountants would be involved in formulating and implementing corporate strategy and designing organizations management information systems. Similarly, Cooper (1996a, 1996b) argues that management accountants need to develop skills in systems design and implementation, change and strategy management as well as in cost management.

The role of the Management Accountant in particular, has become more important, not only in the corporate level, but also at the national level, and even more importantly, at the international level. Management accountants have long played multiple roles variably described as scorekeeping, attention-directing, and problem-solving roles (Simon, Kozmetsky, Guetzkow & Tyndall, 1955). Whereas scorekeeping and attention-directing roles typically focus on compliance reporting and control-type issues respectively, the problem-solving role centers on providing business unit managers with relevant information for decision making (Hopper, 1980). These roles respectively match two commonly held images of the typical accountant: the bean
counter and the business partner (Friedman & Lyne, 2001; Granlund & Lukka, 1998; Vaivio, 2006; Vaivio & Kokko, 2006).

Two roles played by the management accountant are commonly highlighted: the role of bookkeeper and the role of decision-making facilitator (Emsley, 2005; Hopper, 1980; Indjejikian & Matejka, 2006; Sathe, 1978; 1982; 1983). Each of these roles may be associated with both benefits and risks (Sathe, 1983). The bookkeeper management accountant must “ensure that the financial data of a business unit is fair and that internal control practices comply with procedures and the company’s policy” (Sathe, 1983: 31). The benefit tied to the bookkeeper is that this role ensures accurate information and financial reporting about an entity and its activity (Maas & Matejka, 2009). The risk is that the bookkeeper may be seen as an ‘outsider’, thereby making any ‘before the fact’ control difficult to achieve (Sathe, 1983). The role of aiding decision making makes mid-level operational managers the primary clients of management accountants. Here, the accountant’s main task is to provide managers with data required for self-control (Hopper, 1980: 402). The benefit associated with this style of management accounting function is its contribution to business decision making (Granlund & Lukka, 1998b). However, the management accountant’s involvement can also stifle operational management initiative and creativity (Sathe, 1983).

In particular, it was speculated that management accountants would become full members of management team and regain a central role in performance management (Couto et al, 2005; IBM Business Consulting Services, 2004; Kaplan, 1995). In the wake of the publication of the Johnson and Kaplan book, a number of new tools were proposed including Strategic Cost Management, Activity Based Costing, EVA and the Balanced Scorecard. However a strong argument can be made that changes in management accounting practice so far have not been significant.
The role of Management Accountant in a corporate world is closely involved in supporting, planning, controlling, directing, communicating and coordinating with the decision-making activities. Specifically, the role of management accountant in an organization is to support the information needs of management. However, the type, size, structure, and form of the organization can affect the complex role of management accountant (Kariyawasam, 2009). Management accountants were not participants in the decision-making process but provide the information that can highly affect the decision within the organization because they are the keepers of financial records.

The capacity for implementing change due to resource availability, supporting investment in new technology, retaining and restructuring as part of adaptation of new roles for the management accountant are part of the evolution (Cooper and Dart, 2009). The evolution of the role of a management accountant defines its broad and deep responsibility. The accountant has the authority to tell the executives about the information she or he gathered for over the years and expected to suggest ways to improve the quality of the decision (Siegel and Sorensen, 1999). The accountants’ credentials and skills are needed for their own success as well as the organization. The communication, oral, written, and presentation skills are highly appreciated by the business leaders to help them understand the financial reports and react on it. Accountants have the ability to work in different surroundings and with a team can make them have a solid understanding about the corporate accounting. And understanding the business transactions can make it easier for an accountant to provide fruitful information (Siegel and Sorensen, 1999).

The managers in Pierce’s and O’Dea’s (2003) survey emphasized also team work. Management accountants should work as a member in the management team and be considered by him/herself and other managers as business managers with special
knowledge in accounting and finance. In addition, Pierce and O’Dea (2003) suggest that future management accountants need not only knowledge of accounting and finance but also knowledge of the company’s business especially understanding of production and sales activities.

In his research, Leonard (1950) explains the extent to which cost analysis is a major role of the management accountant. The management accountant devotes a large share of his time in determining what cost should be at a given level of output and then analyzing why, in fact, that target cost was not achieved. An effective cost control program is usually built around the management accountant's reports and summaries of operating data, and management's corrective action taken as a result of studying these reports and summaries. Thus, cost control is the responsibility of both of the management accountant and management. The management accountant is responsible for the recording and reporting phase of cost control, while management is responsible for taking corrective action (Crossman, 1953:25).

Accountants prepare and submit to management progress reports that summarize activities to show how efficiently various divisions are performing. By comparing actual results with the budget amounts, they identify areas of deviation where problems may be developing. They then provide feedback or information about current performance designed to encourage needed changes (Rayburn, 1993:4). In cost-benefit analysis accountants undertake detailed analysis of the benefits and costs of alternative course of actions. The manager then selects the optimal alternative that benefits his/her organization. The alternative chosen depends on the manager's beliefs about the future events, the accountant's forecasts or estimates, and the manager's feelings about the various outcomes. In deciding what to forecast or estimate, Lere (1991) considers two issues: identifying the forecasts and estimates that are relevant to the
decision being made and selecting the forecasts and estimates that has potentially the greatest benefit over the costs.

CONCLUSION

This paper has provided in depth insights into the decision making and role of management accountant in a business organizations. The role of an accountant is diverse and critical. They can affect the decisions that the business leaders are going to create. They can also keep their eyes tracked in any changes that might happen while the decision has been in the process of assimilation. Accountants’ job is broad and complex but still, those individuals can handle the presence of the pressure. The change of their role in a management is another type of approach where they can manage the challenges brought by the globalization and the change in the world of business.

It has been established that the role of the management accountant in an organization is to support the information needs of management. The type, size, structure and form of ownership of the organization will influence the management role, and thus, determine the complexity of the management accountant’s role. Such differences in size do not change the basic role of the management accountant, nor the basic work which he or she does. However, the size of the organization may change the degree of formality or sophistication with which the function is carried out, or the level of resources devoted to management accounting. But, the management accounting function remains essentially the same.

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