
Part – I
Financial Accounting

Chapter–1

Accounting and Financial Management A Conceptual Framework

LEARNING OBJECTIVES

In this chapter we will study:

Introduction

Need for Accounting and Role of Accountant

□ *Important terms*

Defining Accounting—Traditional and Modern View

Accounting Information

Branches of Accounting

Difference between Financial Accounting, Management Accounting and Cost Accounting

Accounting Information System—Information flow chart

Users of Accounting Information

Steps in Accounting Process

Limitations of Accounting

Accounting and Financial Management—Inter-relationship

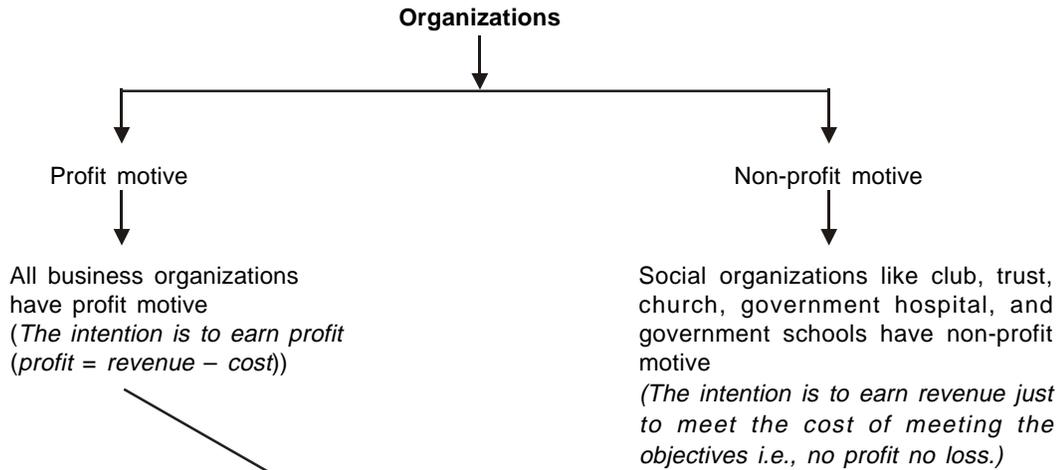
Organisation Structure for Accounting and Finance Activity

Utility of Accounting and Financial Management for Information Technology Professionals.

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1.1 INTRODUCTION

- Organizations play an important role towards economic development.
- There are different types of organizations engaged in trading and manufacturing of goods/services.
- On the basis of motive, there may be two categories of organizations.



- Both category of organizations (stated above) need money to fulfil their objectives *i.e.*, **to sustain and to grow.**

- There are two aspects of money (Fund).

Measurement of money

Management of money

- In a very limited sense **measurement of money** means how much money has been invested and where *i.e.*, record-keeping whereas, **management of money** means from where the money will come in and where it will go *i.e.*, procurement of fund (Financing decision) and utilization of fund (Investment decision).

Thus,

- **Accounting is concerned with measurement of money.**

Financial Management is concerned with management of money.

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'Measurement of money' in a broad sense means systematic record-keeping *i.e.*, maintaining books of accounts popularly known as book-keeping to generate such information which helps the interested groups/individuals in decision-making process *i.e.*, planning and controlling future activities.

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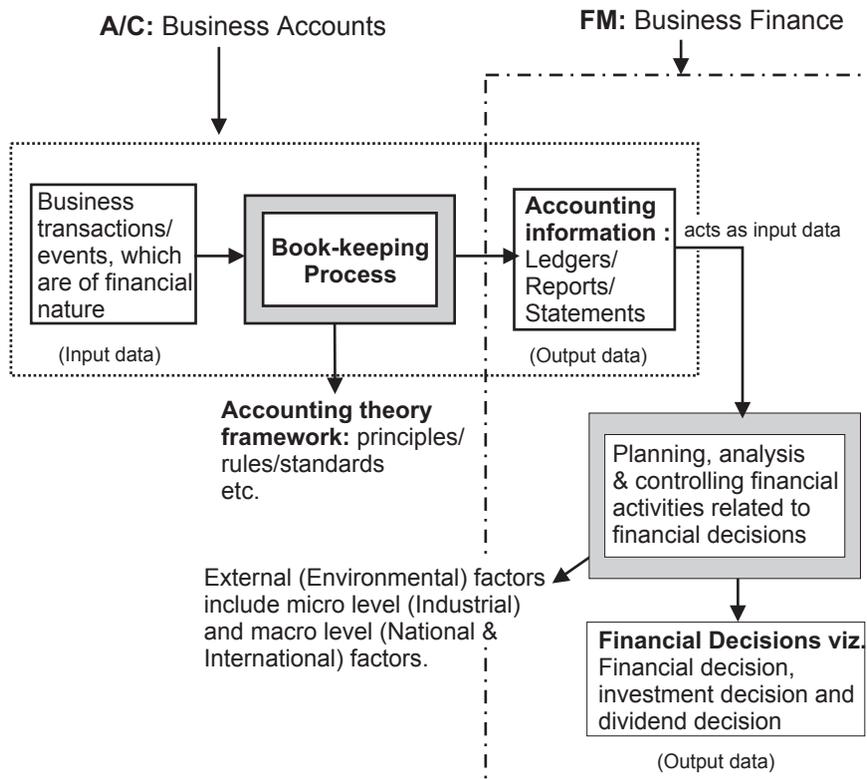
Thus, in a nutshell, **Accounting** is information-generating system whose objective is to collect, process and report financial data of an organization to all the interested parties (internal and external both) for decision-making *i.e.*, planning and controlling financial activities.

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'Management of money' in a broad sense includes all the financial decisions starting from planning to controlling financial activities under external/environmental factors (micro and macro both).

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Thus, in a nutshell **Financial Management** is a decision-making system whose objective is planning, analysis and controlling financial decisions under external environmental factors (micro level and macro level both).



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1.2 NEED FOR ACCOUNTING AND ROLE OF ACCOUNTANT

1.2.1 Need for Accounting

Accounting helps in knowing:

- What is the result of business operation after a certain interval *i.e.*, profit/loss?
- Financial health: Will the organization be able to meet commitments/obligations in the near future?
- What is fund/cash position?
- What the organization owns *i.e.*, assets to the organization.
- What the organization owes *i.e.*, liabilities of the organization.

and many more things, which help in decision-making process. This creates need for accounting.

Now, before going into details of accounting, first have a look on important terms frequently used in accounting. This will help in clear understanding of accounting concept and process.

1.2.2 Role of Accountant

With the help of proper accounting system, accountant helps the management in three ways:

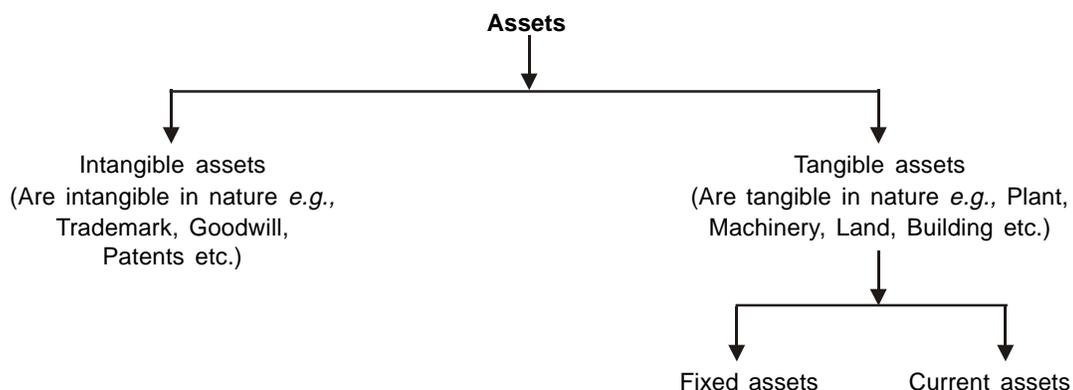
- Record-keeping/book-keeping
- Attention-directing
- Problem-solving
 - Accountant in his record-keeping role maintains books of account.
 - Accountant in his attention-directing role generates different statutory and non-statutory routine accounting information to bring the attention of management towards strength and weakness of the organization concerned.
 - Accountant in his problem-solving role helps the management by providing crucial information *i.e.*, non-routine information and number of alternate options to solve particular problem related to financial decisions (Financing, Investment and Dividend decision).

SOME IMPORTANT TERMS AND DEFINITIONS

Assets

Assets mean what an organization owns. In other words, anything which enables a business enterprise to get cash or a benefit in future, is an asset.

Classification of assets

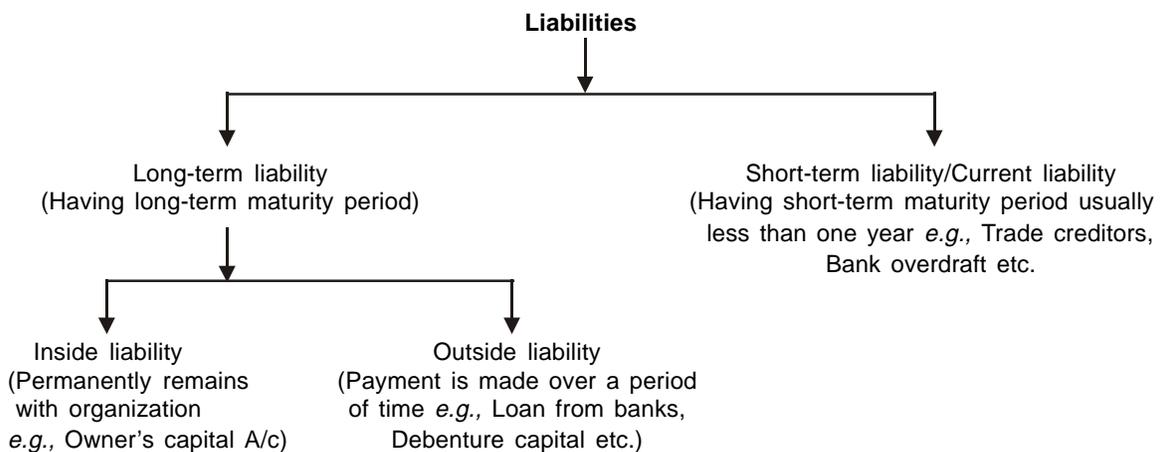


- **Fixed Assets:** Assets that are acquired for relatively long periods for carrying on the business of the enterprise and not meant for resale, *e.g.*, land, building, plant, and machinery etc.
- **Current Assets (CA):** Assets which are either in the form of cash or can be converted into cash within one year/short period *i.e.*, get converted into cash within one operating cycle of business *e.g.*, Cash, Inventories, Debtors, Bills Receivable, etc.
- **Liquid/Quick Assets:** Assets, which are immediately convertible into cash without much loss, *e.g.*, debtors, marketable securities, stamps etc. *i.e.*, except stock, all CA are liquid assets.

Liabilities

Liabilities mean what the organization owes. In other words, it is an amount, which a business owes and has to return or account for. For example, loan from banks, trade creditors, etc.

Classification of liabilities



Capital: It refers to the amount invested by the proprietor in business enterprises.

Revenue: It means income of a recurring nature from any source related to business.

Capital Expenditure: An expenditure, which has been incurred for the purpose of obtaining a long-term advantage for the business, *e.g.* expenditure incurred for purchase of fixed assets.

Revenue Expenditure: It denotes the cost of services and things used for generating revenue. In other words, all items of expenditure, whose benefit expires within a year or which have been incurred merely to maintain the business or to keep the assets in good working condition, is taken as revenue expenditure. For example, salaries and wages paid to employees, depreciation of business assets, maintenance expenses of motor vehicle, etc. Revenue expense is different from loss. An expense is supposed to bring some benefit to the firm, whereas a loss brings no benefit to the firm. For example, loss by theft, loss by fire, etc. While calculating the income or the profit of a business for a particular period, the revenue earned during that period is to be matched with the expense incurred in earning that revenue (matching concept).

Deferred Revenue Expenses: A revenue expenditure whose benefit is to continue for period of two or more years. Such expenditure is written off not in one year but over a period of two or three years. For example, expenditure incurred on heavy advertisement, preliminary expenditure, etc.

Creditor: Any person who gives credit is a creditor. The supplier supplying goods on credit is creditor. Creditor is one to whom the business owes. Owner is a creditor under 'Separate Entity Concept'.

Debtor: A person who owes money to the business is called a debtor. He is a customer to whom goods are sold on credit.

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Solvent: A person who is in a position to pay his debts as they become due.

Insolvent: A person who is not in a position to pay his debts as they become due. The dues from an insolvent debtor are known as Bad Debts.

Reserve for Bad Debt: A reserve from the profit of the organization is created for bad and doubtful debts. It is a buffer for anticipated loss (under conservatism).

Shares: Shares represent ownership securities.

- In case of joint stock companies, owner's capital is divided into very small fractions say Rs. 5/-, Rs. 10/-, Rs. 20/- etc. each fraction is termed as Shares.
- The person (natural or legal) who purchases/subscribes these shares are known as shareholders.
- Whatever shareholder receives against their investment is known as dividend. This may be in form of cash or kind.
- Shareholders act as part owner to the concern organization because they possess voting right. The extent of ownership depends upon the extent of share holding. Voting right means right to vote, which in turn means right to elect board of directors, which constitute the apex body of concerned organization.

Debentures: Debentures represent creditorship securities.

- In case of joint stock companies, a part of debt capital is divided into very small fractions say Rs. 5/-, Rs. 10/-, Rs. 20/- etc. each fraction is termed as Debentures.
- The person (natural or legal) who purchases/subscribes these debentures are known as debenture holders.
- Debenture holder receives interest against their investment.
- Debenture holder act as creditors to the organization concerned because they have legal right to receive interest and principal repayment at the end of maturity, depending upon the nature of debenture.

1.3 DEFINING ACCOUNTING

There are two views in this regard viz.

1. Traditional view
2. Modern view

1.3.1 Traditional View

Traditionally *i.e.*, up to first decade of 20th century, accounting was merely restricted to book-keeping leading to preparation of income statement and balance sheet only, referred as financial statements (Audited financial statements are statutory requirement demanded by government for the purpose of income tax liability).

- Income statement presents summary of all the expenses and incomes during the financial year (1st April to 31st March).
- Balance sheet presents what the organization owns *i.e.* assets and what the organization owes *i.e.* liabilities at a particular point of time, usually at the end of financial year *i.e.* on 31st March.

1.3.1.1 Book-keeping

- Book-keeping means systematic recording of all the financial transactions/events in the book of accounts. *Book-keeping is not concerned with disclosing or interpreting the results of the business.*
- Systematic recording means identifying, measuring, recording, classifying and summarizing (trial balance only) financial transactions/events, under accounting theory framework. **Note:** *Accounting theory framework will be discussed later in the book.*
- Transaction means exchange of money with money's worth *e.g.* sale of goods for Rs 10,000.
- Event means happenings *e.g.* loss of stock due to fire worth Rs. 5000.
- Books of accounts are the place where financial transaction/events are recorded.

1.3.1.2 Evolution of Modern Accounting

With the passage of time the role of accounting has changed significantly and in present stage it is accepted as an information system, which helps the management in economic decision-making. In other words, modern Accounting is book-keeping plus much more. The following definition of accounting arranged in chronological order are evidences regarding changing role of accounting over a period of time:

- (i) **1941:** The American Institute of Certified Public Accountants (AICPA) defined accounting as: “The arts of recording, classifying and summarizing in a significant manner and in terms of money transactions and events, which are in part, at least, of a financial character and interpreting the result thereof.”
- (ii) **1966:** The American Accounting Association (AAA) defined accounting as: “The process of identifying, measuring and communicating economic information to permit informed judgements and decisions by uses of the information.”
- (iii) **1970:** Accounting Principles Board (APB) and AICPA states: “The function of accounting is to provide quantitative information, primarily financial in nature, about economic entities, that is intended to be useful in making economic decisions.”

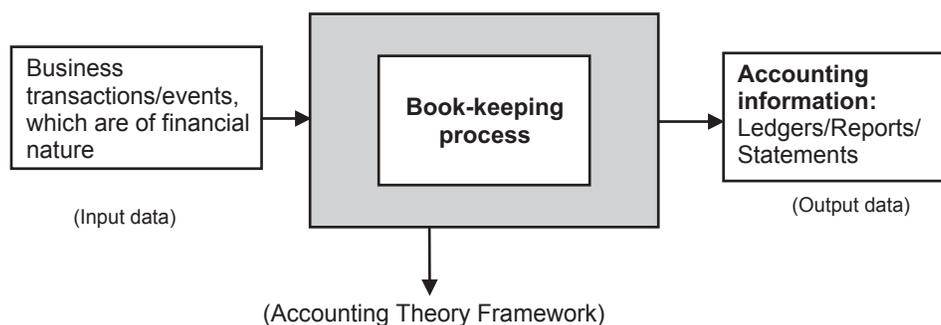
1.3.2 Modern View of Accounting

According to this view, accounting is an information generating system. It takes business transactions/ events as input data, process it which is popularly known as book-keeping process which includes identifying, recording, classifying and summarizing business transactions and events under accounting theory framework and generates output data in the form of statements and reports which helps all the interested parties (internal and external both) in economic decision-making *i.e.* planning and controlling financial activities.

In other words, accounting is book-keeping process which generates information known as accounting information to help all the interested parties (internal and external both) in decision-making *i.e.* planning and controlling financial activities.

Thus, the role of accounting is, information system hereafter referred to Accounting Information System (AIS).

Accounting as information system can be presented as shown below:

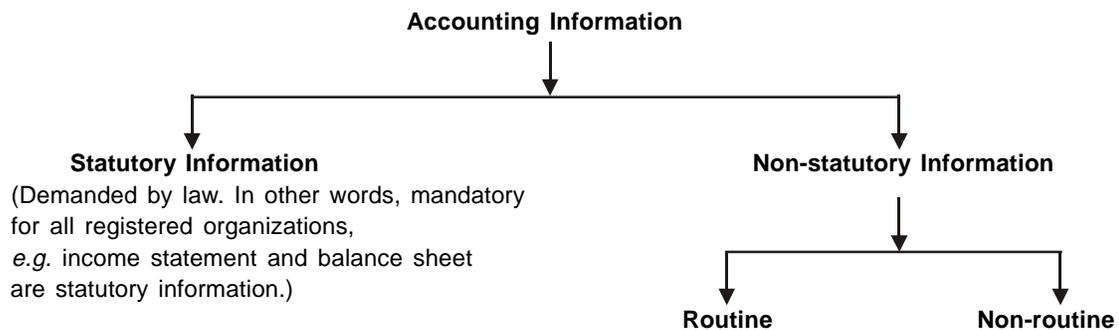


Both the views on accounting have one thing common *i.e.*, book-keeping. In other words, book-keeping is an essential part of accounting process. But before going into the mechanism involved in various stages of book-keeping process, let us have a look on information generated by accounting system known as Accounting Information.

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1.4. ACCOUNTING INFORMATION

The information generated through accounting system can be categorized in two parts.



- Routine information is generated after certain intervals. Examples of routine information are fund flow statement/cash flow statement, annual budget, performance reports, cost sheet etc.
- Non-routine information is need-based information generated by accounting system to help in solving specific problem, e.g., marginal cost sheet, zero-based budgeting etc.

Thus, accounting helps in knowing (say):

- (i) The result of business operation *i.e.* profit/loss through income statement.
 - (ii) The financial position *i.e.* picture of assets and liabilities through balance sheet.
 - (iii) Fund position/cash position through fund flow statement/cash flow statement.
 - (iv) Resource utilization position/financial health through ratio analysis.
 - (v) Cost records for different cost centers through cost sheet.
- And many more things that are required for decision-making process.

1.5. BRANCHES OF ACCOUNTING

On the basis of information generated by accounting system, there are three main branches of accounting:

- (i) Financial accounting system
 - (ii) Cost accounting system
 - (iii) Management accounting system.
- Financial accounting deals with information numbering (i) and (ii) mentioned above.
 - Management accounting deals with information numbering (iii) and (iv). Whereas
 - Cost accounting deals with last information mentioned above.

1.5.1 Financial Accounting (FA)

FA deals with preparation of Final Accounts/Financial Statements viz.

- (i) *Income Statement* to get previous year's result of business operation *i.e.*, Profit/Loss. Income statement is also termed as Profit & Loss Account (P & L A/c).
- (ii) *Balance Sheet* (B/S) to get previous year's financial position *i.e.*, picture of Assets and Liabilities.

1.5.2 Cost Accounting (CA)

Cost accounting deals with present information *i.e.*, determining unit cost at different levels (known as cost centers) of ongoing production. Cost accounting process includes:

- (i) Cost determination *i.e.* costing
- (ii) Cost analysis *i.e.* studying behavior of profit with respect to cost and volume.
- (iii) Cost control *i.e.* comparison of actual cost with predetermined cost/standard cost.

For above-mentioned information, CA system generates:

- (i) *Cost sheet* for cost determination.
- (ii) *Report on CVP (Cost-Volume-Profit) analysis/BE (Break-Even) analysis* for analyzing behaviour of profits with respect to cost and volume.
- (iii) *Report on variance analysis* for determining variances and to take corrective action whenever needed and hence cost control.

Note:

- Both FA and CA takes input data for further processing from book-keeping system.
- In an organization book-keeping system functions as a part of FA system. In other words, it is not in isolation.

1.5.3 Management Accounting (MA)

MA deals with all those information, which helps in decision-making process *i.e.* planning and controlling financial activities. In an organization, MA is common to both FA and CA because all those information, which are generated by FA and CA system are useful in decision-making process and comes under the preview of MA system *e.g.*

- CVP analysis and variance analysis of CA system also form part of MA system.
- Fund Flow Statement (FFS) of FA system also form part of MA system. Because it presents the flow of fund through business organization during financial year and is of great help in assessing fund position.

Apart from above information which are common to both FA system and CA system, there are some information exclusively generated by management accountants *e.g.*

- (i) Projected statements like:
 - A- *Projected income statement* to estimate coming year's target profit.
 - B- *Projected balance sheet* to estimate coming year's target financial position. (*i.e.* assets and liabilities).
 - C- *Projected FFS/CFS* to estimate coming year's target fund/cash position.
- (ii) *Developing budget and budgetary control system* for the purpose of budgeting.
- (iii) *Marginal costing techniques* for short-term decision-making purposes.

1.6 DIFFERENCE BETWEEN FA, MA AND CA SYSTEM

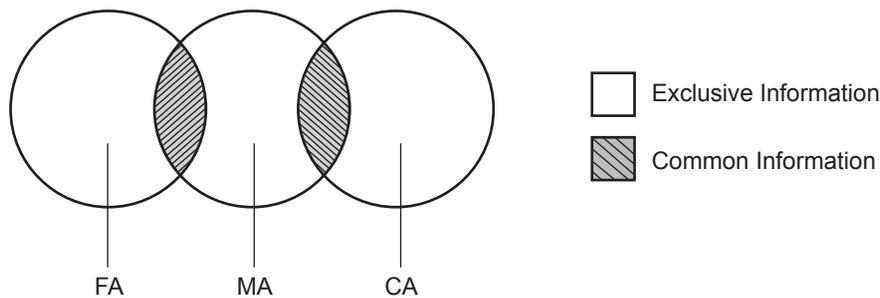
Financial Accounting (FA)	Management Accounting (MA)	Cost Accounting (CA)
1. Financial accounting is concerned with preparation of financial statement <i>i.e.</i> income statement and balance sheet.	1. Management accounting is concerned with accounting done by management itself that help the top-level management in decision-making.	1. Cost accounting is concerned with cost determination <i>i.e.</i> costing, cost analysis and cost control.
2. Financial accounting is governed by certain accounting principles, concepts and accounting standards etc.	2. Management accounting has no such restrictions. The management as per its requirement prepares it. The tools used for	2. Cost accounting is also regulated by certain rules and formats. The techniques used for cost control is standard

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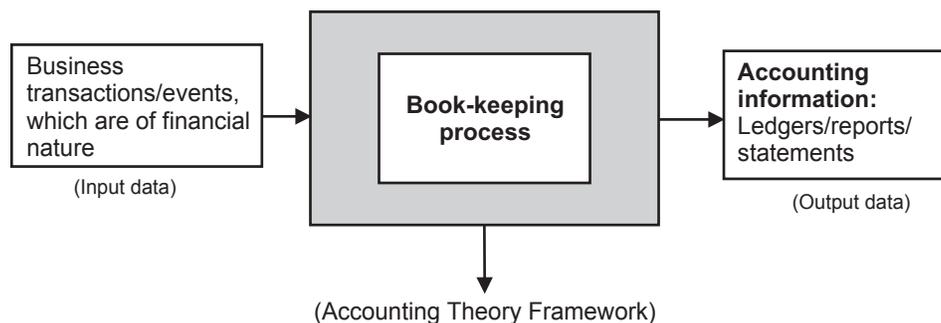
Financial Accounting (FA)	Management Accounting (MA)	Cost Accounting (CA)
<p>3. Financial accounting takes raw information from book-keeping system.</p> <p>4. The auditing power of financial statement rests with public accountant e.g. C.A. in India.</p>	<p>management accounting are—ratio analysis, cash flow and funds flow analysis etc.</p> <p>3. Management accounting takes input data from financial accounting as well as cost accounting system.</p> <p>4. Management accounting does not require auditing but can be reviewed by a senior executive.</p>	<p>costing/variance analysis.</p> <p>3. Cost accounting takes input data from book-keeping system i.e. from the various vouchers.</p> <p>4. Cost accountants, audit cost accounting information.</p>

Note: Position of MA system with respect to FA and CA system: MA system is common to both FA and CA system.



1.7 ACCOUNTING INFORMATION SYSTEM (AIS)

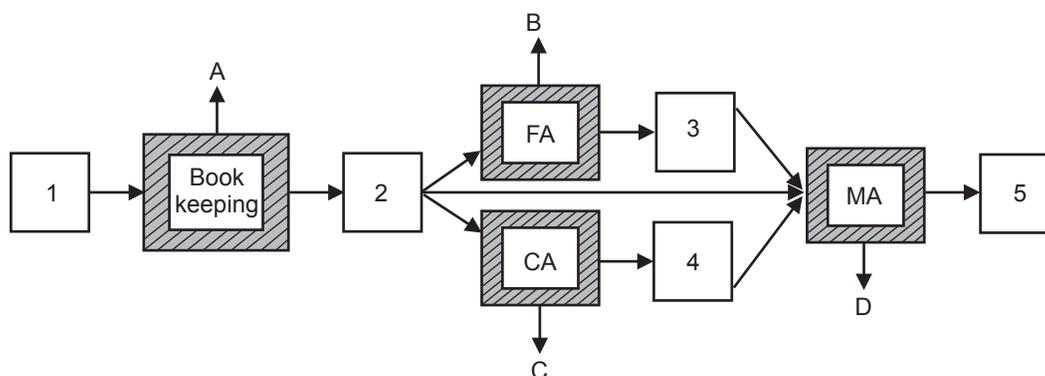
1.7.1 Information Flow Chart (Level 1)



1.7.2 Information Flow Chart (Level 2)

There are 4 sub-fields/components of accounting:

- (i) Book-keeping system
- (ii) FA system
- (iii) CA system
- (iv) MA system



Explanation to above-mentioned symbols

- 1** – Business transactions/events, which are of financial nature (must be supported by source documents like cash memo, invoice etc), which acts as input data for book-keeping system.
 - 2** – Output generated by book-keeping system which acts as input data for all the main branches of accounting viz. FA system, CA system and MA system. This output consists of different ledger books and trial balance.
 - 3** – Statutory financial accounting reports generated by FA system, which acts as input data for MA system. Statutory financial accounting reports consists of financial statements *i.e.* income statement and balance sheet.
 - 4** – Cost accounting reports like various cost sheets showing unit cost at different level of production, which in turn acts as input data for MA system.
 - 5** – Output information generated by MA system fulfilling needs of internal, as well as external users having direct/indirect interest in the organization concerned *e.g.* statement of ratios, fund flow statement/cash flow statement.
- A** – Accounting theory framework for processing of book-keeping consists of accounting standards, conventions and concepts.
- B** – Framework of statutory laws and acts like company law, partnership act, SEBI act etc. under which processing of FA system takes place.
- C** – Framework of predetermined formats, procedures and assumptions under which processing of CA system takes place.
- D** – Framework of relevant factors (external as well as internal factors) within which processing of management accounting system takes place.

Processing of book-keeping, FA, CA and MA systems are as follows:

- Processing of book-keeping system includes identifying, recording, classifying and summarizing (trial balance only) the business transactions/events, which are of financial nature.
- Processing of FA system includes preparation of financial statements *i.e.* income statement and balance sheet.
- Processing of CA system includes classification, allocation, recording, summarizing and reporting current and prospective costs *i.e.* preparation of various cost sheets showing unit cost at different level of production *i.e.*
 - (i) Cost determination
 - (ii) Cost analysis
 - (iii) Cost control

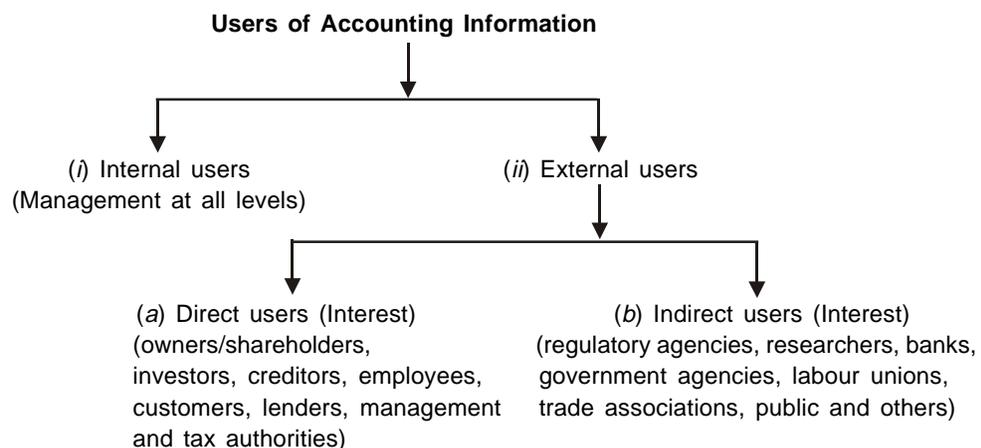
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- Processing of MA system includes:
 - (a) Analysis and interpretation of financial statements generated by FA system
 - (b) Analysis of cost records/cost sheet in the light of financial statements
 - (c) Analysis and interpretation of variance analysis
 - (d) Developing cost control techniques.
 - (e) Developing different budgets
 - (f) Developing short-term decision-making techniques etc.

1.7.3 Information Flow Chart (Level 3) (See on next page)

1.8 USERS OF ACCOUNTING INFORMATION

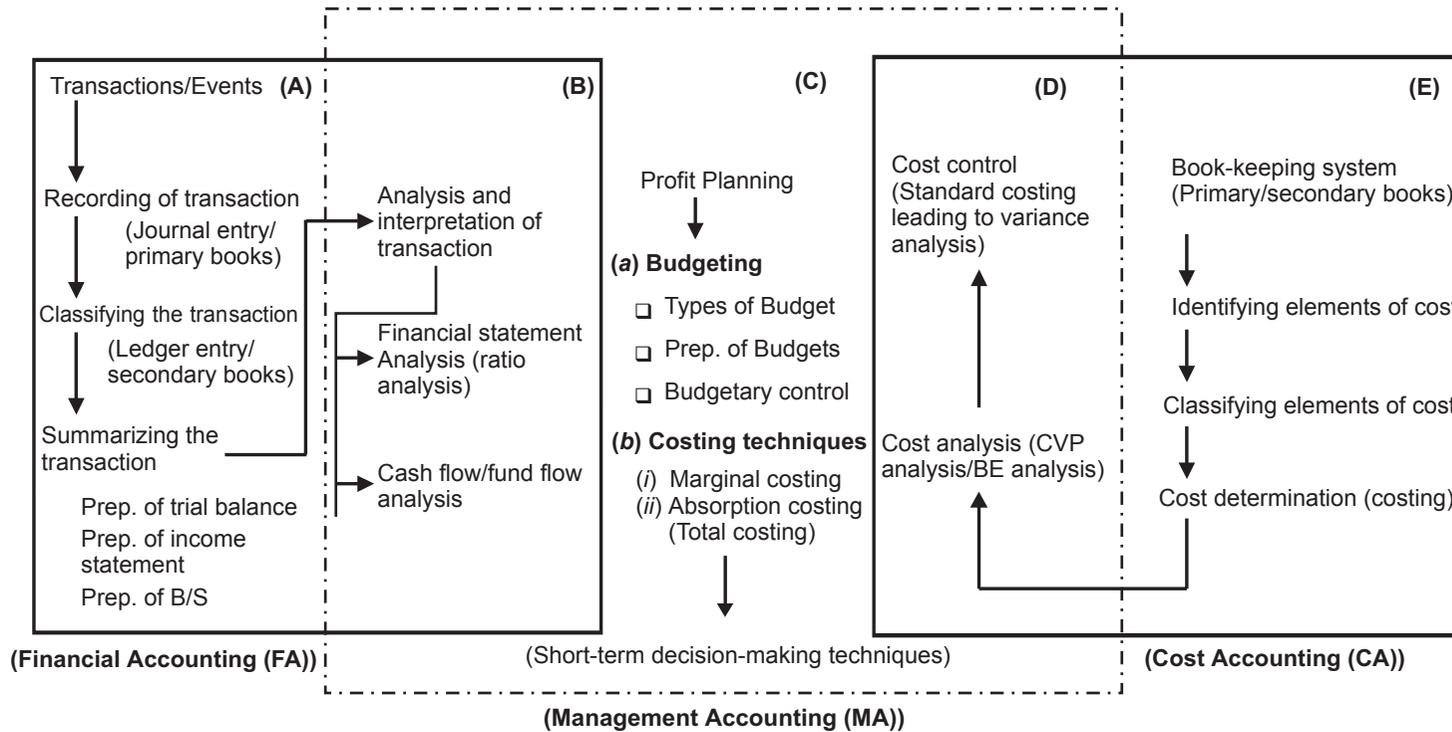
Different users, for making their decisions require accounting information. These users may be classified as:



- (i) Internal users:** Top, middle and bottom level of management executives are the internal users of accounting information. They need it for making decisions. These users are interested in the profitability, operational efficiency and financial soundness of the business. The top-level management is concerned with accounting information related to planning, the middle level is interested in planning and controlling and the lower level with operational affairs.
- (ii) External users:** External users may have direct interest or indirect interest.
 - (a) External users having direct interest:** The existing and the prospective creditors and investors have direct interest in the accounting information. The sources of information for external users are financial statements and reports of Directors and Auditors.

Investors assess the financial soundness and net worth of the business so that they may decide about buying, selling or holding investment in the business. Creditors, such as banks, lenders, debenture holders and financial institutions assess the risk involved in granting loans, servicing of the existing loans to the business.
 - (b) External users having indirect interest:** These users such as department of company affairs, registrar of joint stock companies, sales tax and income tax authorities, labour unions, prospective customers, creditors, stock exchange's trade associations and others who are interested in the affairs of the business. They have to make their own decision on the basis of the financial reports of the business.

1.7-3 Information Flow Chart (Level 3)



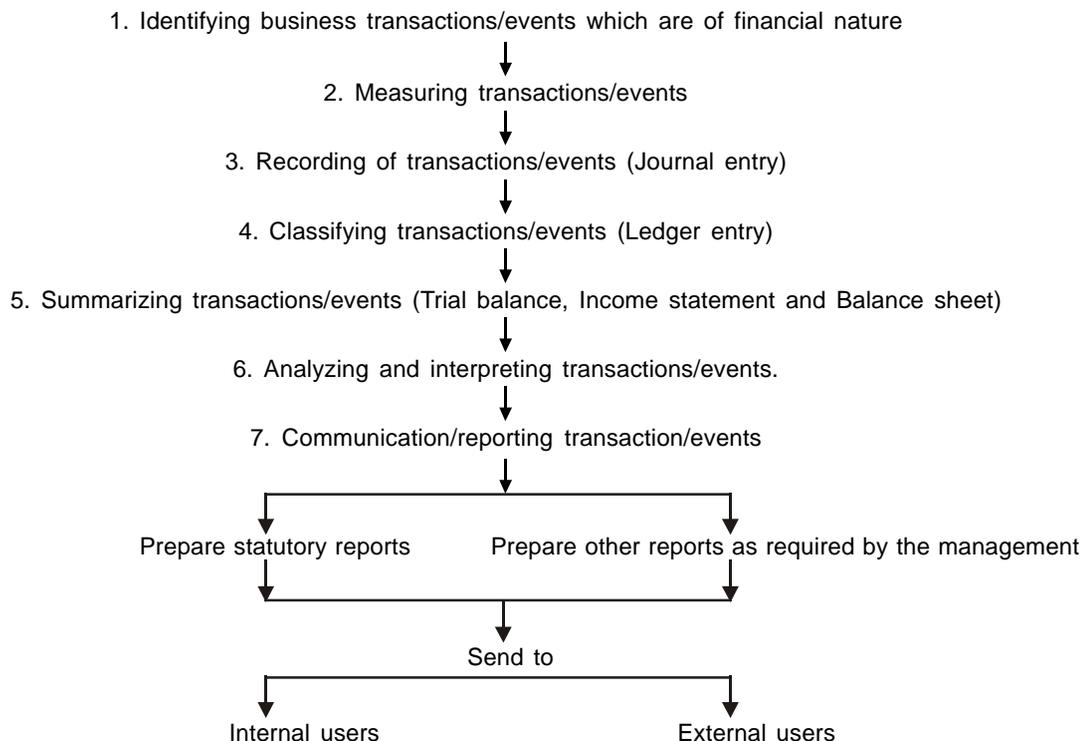
- (A): Information flow exclusive to financial accounting
- (B): Information flow common to both financial accounting and management accounting
- (C): Information flow exclusive to management accounting
- (D): Information flow common to both management accounting and cost accounting
- (E): Information flow exclusive to cost accounting

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A brief description of some users having direct interest is as follows

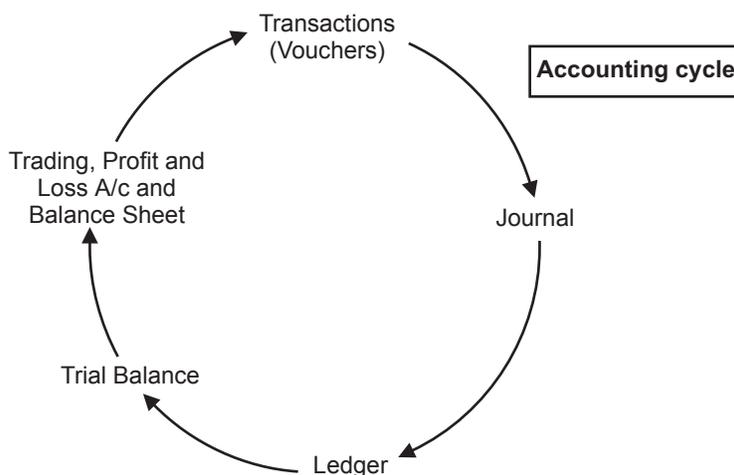
- 1. Shareholders (owners):** Shareholders have direct interest in the affairs of organization and therefore they are interested in accounting information, because rate and amount of dividend depends on residual income. Residual income is reported in income statement.
- 2. Long-term creditors:** The examples of long-term creditors are banks, financial institutions and debenture holders who provide long-term funds to the organization. They are concerned with the debt servicing and interest payment as and when due.
Thus, they are interested in accounting information as accounting information reveals financial health of the organization.
- 3. Government:** Government is interested in collection of the tax revenue and tax is computed on the basis of income, generated by the organization. Thus, government is interested in income statement.
- 4. Short-term creditors:** The example of short-term creditors is suppliers; banks and banks providing overdraft facility etc. Short-term creditors *e.g.* suppliers are interested in their bills. Timely payment of bills depends upon liquidity position of the organization and liquidity position is represented by the accounting information and thus, accounting information is important for short-term creditors.
- 5. Employees:** Receive the benefits in the forms of salaries, perks, allowances etc. which in turn is dependent on profit position which is represented by income statement.
- 6. Management:** Utilizes the available resources [5M *i.e.* man, money, material, machine, method + time + I.T.] of the organization. The prime responsibility of management is optimum utilization of resources. The position of resources utilized is calculated using accounting information and therefore, management uses accounting information for the purpose of performance evaluation.

1.9 STEPS IN ACCOUNTING PROCESS



Note:

- **Accounting Cycle:** Step 1 to step 5 constitutes accounting cycle. Put differently, accounting cycle starts from identifying and recording of transaction and ends with summarizing transactions *i.e.*, preparation of financial statements (Income statement and B/S).



- **Accounting Period:** The time period in completing accounting cycle is known as accounting period and in India it is of one-year duration (1st April to 31st March of next year).

1.10 LIMITATIONS OF ACCOUNTING

Accounting is helpful for business in assessing its worth *i.e.*, profit or loss, assets and liabilities. It enables the business in deciding its future line of action on the basis of information supplied. Though logical conclusions can be derived from accounting, it can never be taken as granted that the facts supplied by accounting are cent percent true. They may be false, biased and manipulated. Accounting has the following limitations:

1. **Record-keeping:** Accounting records only those transactions/events, which are financial in nature. Transactions/events of non-financial nature do not find place in accounting. Certain very important information such as competency of the management, exit of top-level executive, change in consumers preferences etc. are not recorded in accounting, though they affect the financial soundness of the business.
2. **Accuracy of information generated by accounting system:** Accounting assesses profit or loss and financial position (picture of asset and liability) of the organization concerned on the basis of both the real and assumed estimates. Accountants make the valuation of stock, determine the method of depreciation and maintain various reserves and provisions. Different firms have their own different methods of making provisions, so the results of the business will change with the change in the practice.
3. **Value of assets:** The balance sheet does not show the market value of the assets in the ordinary sense of the word. It usually shows assets, costs adjusted according to the conventional rules of accounting. Again there are certain assets, which do not have real value, but they are shown in our

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balance sheet. These assets are like goodwill, patents, preliminary expenses, discount on issue of shares etc. Showing these assets in the book of accounts make the results doubtful.

4. **Window dressing:** Window dressing practices that will improve profitability in the short run may be utilized by the management. Such practices may take the form of postponing the maintenance of plant and machinery, which will decrease costs and increase profitability in the short run, but which would affect the company severely when machine breakdown occurs and production is interrupted.
5. **Changing price levels:** Changing price levels and changes in the current values of assets can produce distortions in accounting measures of performance and financial position. It is desirable that additional information on the basis of current replacement values be provided.

1.11 ACCOUNTING AND FINANCIAL MANAGEMENT—INTER-RELATIONSHIP

1.11.1 Defining Financial Management

Financial management is concerned with management of fund.

It may be defined as “acquisition of fund at optimum cost and its utilization with minimum financial risk.”

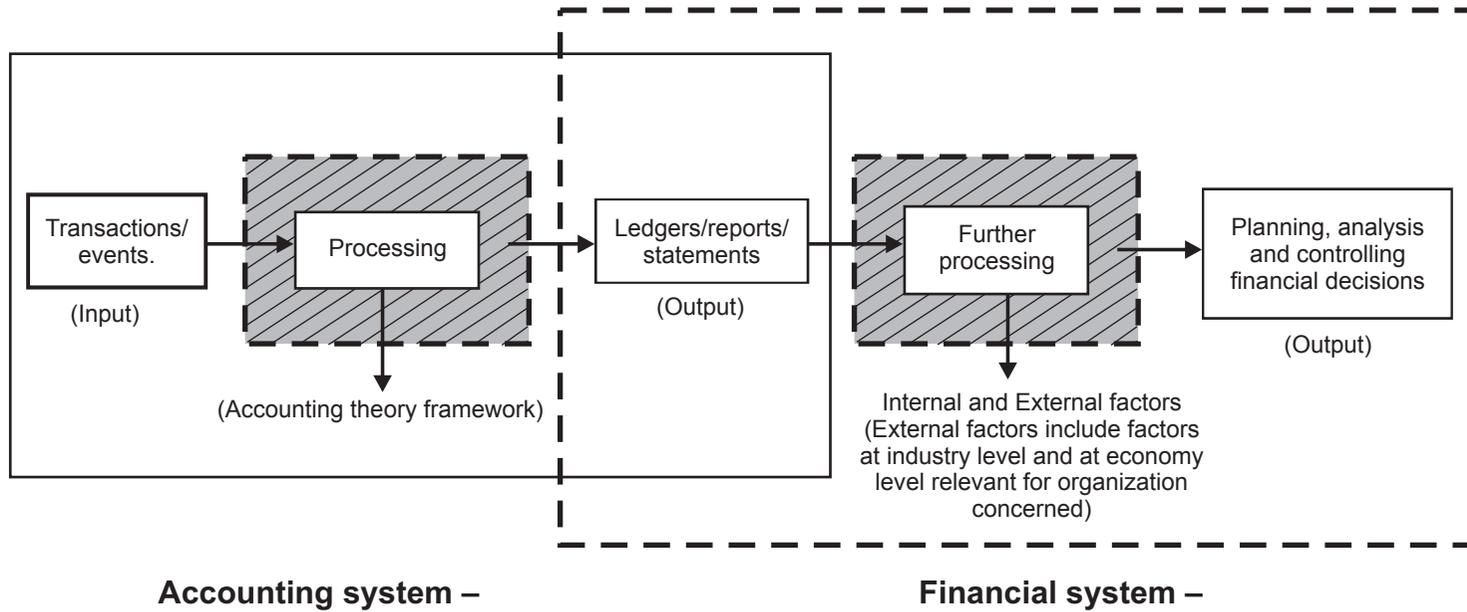
1.11.2 Accounting and Financial Management—Inter-relationship

(See diagrammatic presentation on next page)

1.11.3 Difference between Accounting System and Financial System

<i>Accounting system</i>	<i>Financial system</i>
(i) It is information generating system.	(i) It is decision-making system.
(ii) It is governed by certain laws and Accounting theory framework	(ii) It is governed by external factors relevant to organization concerned.
(iii) The role of accounting system is: (a) Score-keeping (b) Attention directing (c) Problem solving	(iii) The role of financial system is planning and controlling financial decision viz: (a) Financing decision (b) Investment decision (c) Dividend decision.
(iv) It takes input data from business transactions/event, which are of financial character.	(iv) It takes input data from information generated by different branches of accounting incorporating relevant industrial and economic factors.

Accounting and Financial Management—Inter-relationship



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1.11.4 Financial Decisions and Management Accounting

- Financial decisions are of two types *viz.*:
 - (i) Short-term decision, also known as working capital decision.
 - (ii) Long-term decision, also known as capital budgeting decision/project decision/capital expenditure decision.
- Difference between S.T. decision and L.T. decision are as follows:

S.T. Decision (W.C. decision)	L.T. Decision (Capital budgeting decision)
(i) Do not involve substantial capital outlay.	(i) Involve substantial capital outlay.
(ii) Operating profit/short term-sources are sufficient to meet financing requirement.	(ii) Separate/special financing is required.
(iii) Reversible in nature	(iii) Irreversible in nature.
(iv) Short-term effect <i>i.e.</i> benefits are realized immediately/within short period (Revenue nature).	(iv) Long-term effect <i>i.e.</i> benefits are realized over a period of time <i>i.e.</i> up to the life of the project (Capital nature).
(v) No time lag between cost and benefits and hence time value of money concept is not required for cost-benefit analysis.	(v) L.T. decisions involve time lag between cost and benefits and hence time value of money concept is required for cost-benefit analysis.

Note: Time value of money concept refers to change in value of money due to change in time.

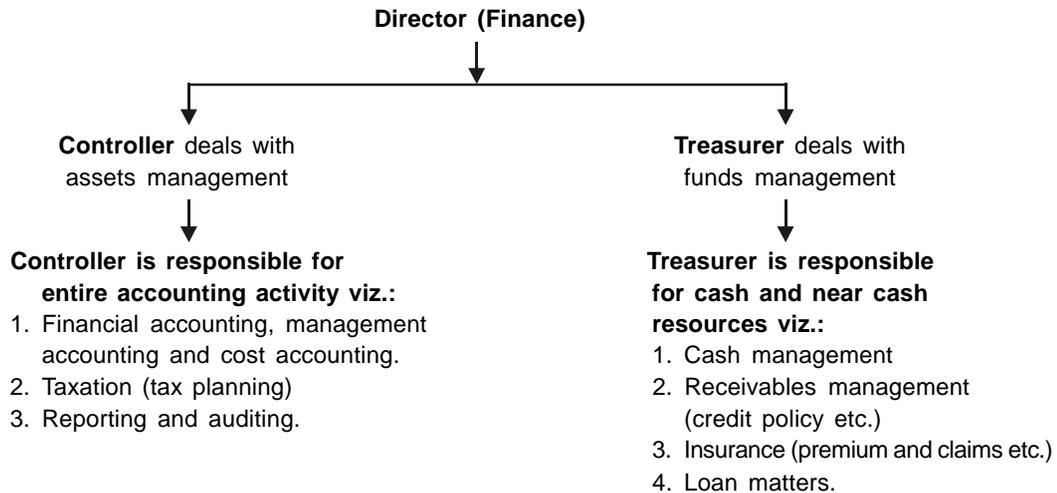
- Planning and controlling financial decisions are complex in nature.
- The management accounting provides tools/techniques for planning and controlling financial decisions. Few examples are listed below: -
 - (i) Projected statements of final accounts
 - (ii) Cash flow/fund flow analysis
 - (iii) Ratio analysis
 - (iv) Variance analysis
 - (v) Budgeting etc.

1.12 ORGANIZATION STRUCTURE FOR ACCOUNTING AND FINANCE ACTIVITY

In an organization, accounting and finance activity is divided into two categories *viz.*:

- Assets management
- Funds management

In case of joint stock companies, the organization structure for accounting and finance activity is as follows:



Note: In case of medium and small-sized organization, financial controller cum chief accountant is responsible for the entire activities of finance and accounts department.

1.13 UTILITY OF ACCOUNTING AND FINANCIAL MANAGEMENT FOR I.T. PROFESSIONALS

I.T. professionals interact with two things *viz.*

1. **Hardware**—which includes computer and telecommunication media like phone, V-SAT etc.
2. **Software**—which includes customized software developed as per management’s requirement and existing software to manage database of the concerned organization using appropriate package. Thus, the problem, from software point of view, before every I.T. professional at business organizations is two fold *viz.*
 - Developing application software for different functional areas like production, marketing, purchase, finance, MIS etc. as per requirement of management.
 - Managing database of the concerned organization and make them available to right person at right time.

Needless to say for both type of problems stated above, I.T. professionals at work must have at least basic knowledge of accounting and financial management because accounting and financial management are language of business, which makes communication possible. It is important to note that without an understanding of accounting and financial management, one cannot understand the complexities associated with business organization. IT professionals, therefore, equipped with knowledge of accounting and financial management can understand not only the complexities associated with business organization but can recognize the problem which helps in developing Data Flow Diagram (DFD) and Entity Relation Diagram (ER-Diagram) easily, which are essential to software development.

Furthermore, clear understanding of database of the concerned organization leads to efficient management of database, which is possible only when I.T. professionals at work have proper knowledge of accounting and financial management because all the financial database rests with accounts and finance department using definite format and terminology.

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Exercises

- Q. 1. Explain the term Management Accounting and state what you understand to be its main objectives.
- Q. 2. Distinguish between:
 - Financial Accounting
 - Cost Accounting
 - Management Accounting
- Q. 3. How does the accounting information assists management in the solution of strategic business problems?
- Q. 4. “Accounting as an aid to management in solving tactical business problems”. Comment.
- Q. 5. Financial accounting has the basic objective of providing financial information to the parties outside the business. Parties inside the business also need information of monetary character and otherwise. Which system of accounting provides this information, and what information is generated for the guidance of the managers to take decisions?
- Q. 6. Distinguish between:
 - Accounting system and
 - Financial system.
- Q. 7. Explain the limitations of accounting information.
- Q. 8. Describe the users of accounting information.
- Q. 9. Describe the utility of Accounting and Financial Management for Information Technology (I.T.) professionals.