"Ovidius" University Annals, Economic Sciences Series
Volume XVII, Issue 1 /2017

Management Accounting as a Knowledge Based Organization Value Driver for the 21st Century Business

Daraban Marius Costin
"Lucian Blaga" University of Sibiu
marius.daraban@ulbsibiu.ro

Abstract

The 21st century information and information technology revolution has made its mark on classical business functions like business support services. Management accounting, a still young business activity has transformed from reactive cost determination focus to proactive value creating and considerate resource business driver. Management accounting is on the way to asserting itself as a proactive business value driver for the modern 21st century business organizations. The present paper is presenting the arguments that support the transformation of management accounting from the "bean counter" score keeping role to value driver supported by knowledge, the prime commodity of the 21st century business environment. Management accounting is the business partner that delivers reliable and accurate data and information for the business decision process that is more and more influenced globalization, internationalization and accelerating and dynamic markets. Can modern companies afford to disregard the dormant value drivers from within their own business organization?

Key words: management accounting, value, knowledge, support services
J.E.L. Classification: M4, M21, M20

1. Introduction

Accounting is one of the main business support activities that is present in any company. The two major accounting fields that can be found distinct in the business accounting activity are financial accounting and management accounting.

The main activity of financial accounting is the recording, reporting and analysis of financial business transactions. The preparation of financial statements requested and imposed by authorities are the main output of the financial accounting activity. The main stakeholders of the financial statements are shareholders, suppliers, financing organizations, fiscal and tax authorities and other 3rd parties are just some of the interested stakeholders.

Financial accounting is regulated and governed by local and international accounting standards and principles. The local regulations are issued by governments and local tax and fiscal authorities whereas international organizations like IASB (International Accounting Standards Board) have issued, the todays one of the most used accounting framework, the IFRS (International Financial Reporting Standards).

While financial accounting is mainly for non-operational stakeholders that are not involved in the day-to-day activity of the company, management accounting is used for the daily business operations in the management decision process. Management accounting is the operational "business language" that is used mainly by the involved managers and business responsible. Similar to financial accounting, management accounting is regulated by various organizations worldwide, like the UK based CIMA (Chartered Institute of Management Accountants), Australia based ICMA (Institute of Certified Management Accountants) or the US based IMA CMA (Institute of Management Accounting Certified Management Accountant).

The Institute of Certified Management Accountants defines the management accountant as follows: A management accountant applies his or her professional knowledge and skill in the preparation and presentation of financial and other decision oriented information in such a way as to assist management in the formulation of policies and in the planning and control of the operation of the undertaking.

Management Accountants therefore are seen as the "value-creators" amongst the accountants. They are much more interested in forward looking and taking decisions that will affect the future of the organization, than in the historical recording and compliance (scorekeeping) aspects of the profession. Management accounting knowledge and experience can therefore be obtained from varied fields and functions within an organization, such as information management, treasury, efficiency auditing, marketing, valuation, pricing, logistics, etc. (Institute of Certified Management Accountants, 2017)

2. Genesis of management accounting

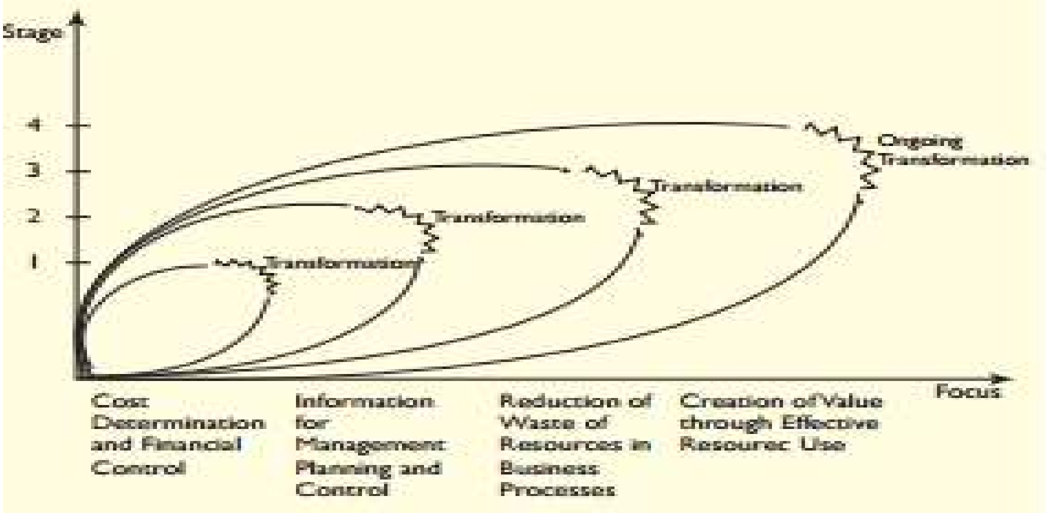
IFAC (The International Federation of Accountants), founded 1977 in Munich, Germany, is one of the major worldwide professional organizations that has a major contribution to the development of the accounting profession and standards.

IFAC is the global organization for the accountancy profession dedicated to serving the public interest by strengthening the profession and contributing to the development of strong international economies. IFAC is comprised of over 175 members and associates in more than 130 countries and jurisdictions, representing almost 3 million accountants in public practice, education, government service, industry, and commerce. (International Federation of Accountants, 2017)

1989 the International Federation of Accountants (IFAC) issued a statement summarizing its understanding of the scope and purposes of management accounting and the concepts which underpin it. The statement was revised and released in 1998 as Management Accounting Concepts - Number 1 in the series of International Management Accounting Practice Statements. (Abdel-Kader & Luther, 2006)

IFAC recognizes in their updated statement from 1998, 4 stages of evolution of the management accounting concepts and focus. The 4 development stages, illustrated further in Figure 1, are not exclusive developments stages, they are inclusive stages, one stage includes and does not exclude the previous stage of development.

Figure no. 1 Evolution of Management Accounting



Source: IFAC 1998

The defined development stages of management accounting reflected the economic environment of the time that was synchronized with the shift in management accounting focus.

Stage 1 - cost determination and financial control (pre-1950) has been described as mainly focused on the determination of product cost. The production processes have been simplistic and labor intensive. This allowed an easy direct cost allocation to the production. Its focus was mainly oriented towards the determination of product cost.

Stage 2 - information for management planning and control (by 1965) In the 1950s and 1960s the focus of management accounting has shifted towards the delivery of business information for the business planning and control processes. Management accounting was more reactive than proactive with main interest in operational topics and no involvement in strategic and management issues.

Stage 3 – reduction of waste of resources in business process (by 1985) came as a result to the 1970 world recession and the oil price shock from the 1980. The focus of management accounting shifted towards the reduction of waste of business resources.

Stage 4 – creation of value through effective resources use (by 1995) is a normal and logical continuation of stage 3, the focus of management accounting has shifted to value creation by effective usage of existing business resources.

A critical difference between Stage 2 and Stages 3 and 4 is the change in focus away from information provision and towards resource management, in the form of waste reduction (Stage 3) and value creation (Stage 4). However, the focus on information provision in Stage 2 is not lost, but is re-figured in Stages 3 and 4. Information becomes a resource, along with other organizational resources; there is a clearer focus on reducing waste (in both real and financial terms) and on leveraging resources for value creation. Accordingly, management accounting is seen in Stages 3 and 4 as "an integral part of the management process, as real time information becomes available to management directly and as the distinction between staff and line management becomes blurred." (IFAC, 1998, para 19) The use of resources (including information) to create value is seen to be an integral part of the management process in contemporary organizations (Abdel-Kader & Luther, 2006, p. 5)

3. Management accounting as a knowledge based organization

Even though there is no universally accepted definition of a knowledge based organization it is commonly understood as being the organization whose products and services are knowledge intensive. A knowledge based organization is an organization where workers use processes and infrastructure to produce, change, manage, use and share knowledge based products and services to achieve the organizational goal. (Daraban, 2016, p. 4)

The characteristics of a knowledge based organization, go beyond product to include process, purpose and perspective. Process refers to an organization's knowledge based activities and processes. Purpose refers to its mission and strategy. Perspective refers to the worldview and culture that influences and constrains an organization's decisions and actions. knowledge based organization exhibit knowledge-intensive processes, purpose, and perspective, regardless of their product (Zack, 2003, p. 1)

IFAC has issued 07.2009 an International Good Practice Guide (IGPG) on Evaluating and Improving Costing in Organizations where a clear distinction between financial and management accounting is made and recognized.

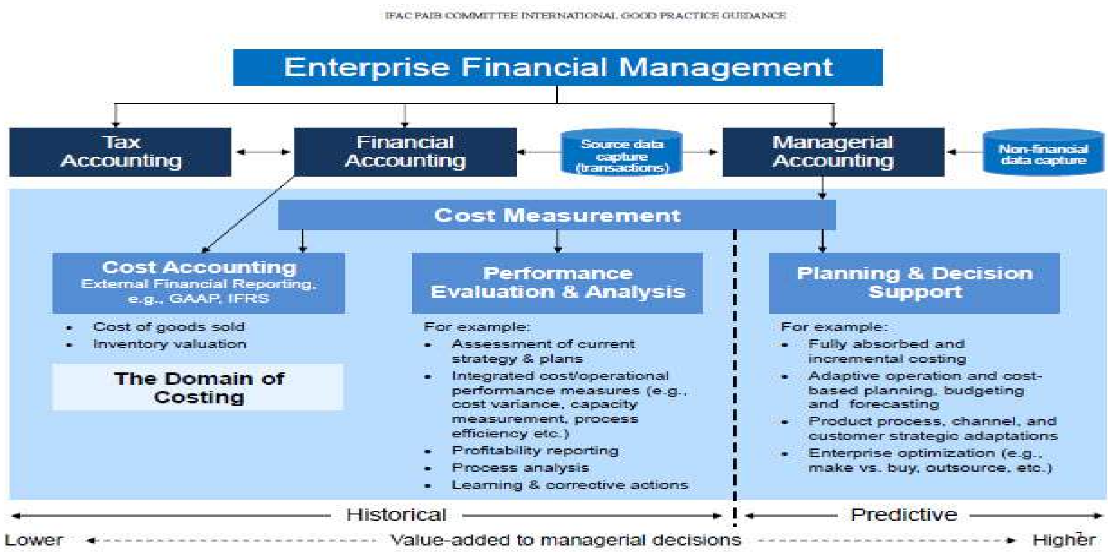
Also in the IGPG the recommendation is made to distinguish between cost accounting for external reporting, where historical performance is reported within certain prescriptive guidelines, and costing for decisions to drive improved organizational performance. (IFAC PAIB Committee, 2009)

The positioning and participation of management accounting within the context of cost measurement, as one of the main pillars of management accounting activity, is illustrated in Figure 2. Per IFAC IGPG management accounting is a part of the enterprise financial management, involved in cost measurement, with contributions to the performance evaluation and analysis and a driver role in the business planning and decision support by adding value by providing useful and relevant business information and knowledge. In this view management accounting is defined as being inclined towards higher value added information for the business management decision process.

A knowledge based organization could be shortly defined as an entity, where knowledge workers are making use of business resources, like systems and processes, to generate, alter, use and transfer knowledge intensive products and services to achieve the organizational goals. The key defining characteristics of a knowledge based organization are at the core of the role definition and meaning of management accounting. Business and financial data are used as input, data are analyzed, put into specific business context and disseminated through the organization as business support data and information. Management accounting is a data-driven business information provider for the business decision process.

Management accounting is using the historical data analysis as a foundation for the predictive higher value business data generation and dissemination that is needed for the business planning and decision support. The management accounting system is leveraged and driven forward by the knowledge worker, the management accountant that is the enabling factor for the learning ability of the knowledge based organization. The learning ability adds to the management accounting activity the knowledge aggregation ability that results in wisdom, the highest and most valuable form of knowledge. The business and financial data transformation into valuable business knowledge is driven by the management accountant that is the knowledge worker as a 21st century "new" type of worker. The knowledge worker raises and deepens the challenges of the 21st century modern data and information driven business where knowledge is the prime commodity. The learning aspect of the knowledge based organization, the management accounting activity, is the key element in the generation of business support data driven conclusions and recommendations that enable a more clear and efficient, risk minimizing planning and decision support. Management accounting encompasses elements of a knowledge based organization, it operates and develops business systems and processes to use, generate, transform and disseminate business information with increased economic value added through its knowledge workers, the management accountant.

Figure no. 2 Enterprise Financial Management IFAC PAIB



Source: IFAC 2009

4. Management accounting as a business value driver

Business value creation is the ultimate goal of any business organization and can also be defined as being the sum of the value created by all business activities and processes from the specific organization. The todays business organizations must compete in the globalized, dynamic and information driven markets. The competitive advantage that assures the future of the business organization can be gained by coping with the 21st century market requirements, understanding and managing the available data and information that are business relevant.

Competitive advantage cannot be understood by looking at a firm as a whole. It stems from the many discrete activities a firm performs in designing, producing, marketing, delivering and supporting its product. (Porter, 1985, p. 33)

Porter, in his book "Competitive Advantage" has identified that support activities have a contribution to the business margin at the beginning of the information age, that has made its mark on the existing economic and business processes.

In the quest for more reliable, quicker and actual business information business organizations have invested and made maximum use of the new information technology features and possibilities in data processing, storage and distribution. Management accounting has become a driver for the usage and adoption of modern IT systems that allowed and eased the data acquisition, transformation and dissemination process.

The business data used as inputs and outputs by management accounting are matching the knowledge value chain. Raw data are acquired, aggregated into information that is transformed into business knowledge to gain more and more and reliable business wisdom that is used for the business management and decision process to assure the much-needed competitive advantage and to create sustainable business value for its shareholder. The more aggregated data is the more value it creates for its users.

The knowledge value chain represents the conceptual basis for the development of a more prescriptive model for the definition and the implementation of knowledge management projects oriented to improve the value-generating capability of a company. (Carluci, et al., 2004, p. 13)

Knowledge value chain has been defined by Powell as being a process model of how data becomes intelligence, and eventually becomes part of a business result or benefit. The knowledge value chain (KVC) comprises two major sets of activities, knowledge acquisition and knowledge application. This reflects the division of labor in knowledge work that has evolved in large, complex organizations. Here, knowledge workers are primarily tasked with knowledge acquisition and development, and decision-makers apply the resulting knowledge to make better business decisions, plan and execute actions, and thereby achieve business results. (Powell, 2001, p. 3)

Powell has defined the knowledge value chain (KVC) as a shared process between knowledge worker and decision maker. The KVC starts with a joint shared understanding and ends with results. Powell's KVC is illustrated in Figure 3. The KVC includes 7 steps, each being considered and opportunity and a potential point of failure where quality control is required and needed.

5. Conclusions

In the context of an information and data driven economy and business environment, business support activities, like management accounting, have been transformed by the influence and requirements of the information revolution. The classical approach of business support activities as non-productive, resources consuming and unproductive needs to be reconsidered.

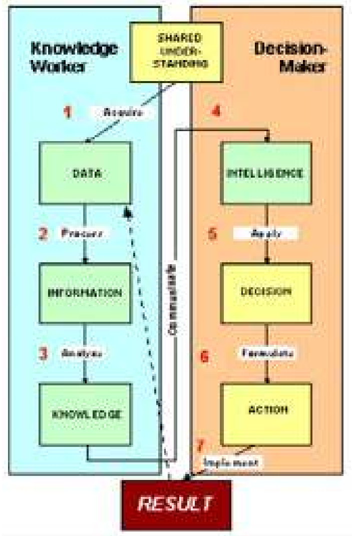
Management accounting, as a science, still in its early ages, has morphed from the more simplistic cost calculation and financial control focus to business value creating activity by the most efficient use of existing resources.

The modern 21st century business organizations must adopt and accept that management accounting is a data-driven business partner that is providing the needed information and data by the business planning and decision activities.

Strategic management accounting will become part of the new business model and business organizations that is supporting the strategic plans and management of the future businesses.

The present paper has shown that management accounting is a knowledge organization that is generating value for the business organizations that are looking for the sustainable competitive advantage, advantage that allows them to compete, adapt and survive in a dynamic and demanding 21st century business environment.

Figure no. 3 Knowledge Value Chain



Source: Powell 2001

6. References

- Abdel-Kader, M. & Luther, R., 2006. IFAC's Conception of the Evolution of Management Accounting. *Advances in Management Accounting,* Volume 15, pp. 229-247.
- Carluci, D., Marr, B. & Schiuma, G., 2004. The knowledge value chain: how intellectual capital. *Int. J. Technology Management,* 27(6/7), pp. 575-590.
- Daraban, M., 2016. *EMPIRICAL APPROACH TO KNOWLEDGE, KNOWLEDGE ECONOMY AND KNOWLEDGE BASED ORGANIZATIONS.* Paltinis, Editura Tehnica, pp. 209-215.
- IFAC PAIB Committee, 2009. *International Good Practice Guide - Evaluating and Improving Costing in Organizations,* New York: International Federation of Accountants.
- Institute of Certified Management Accountants, 2017. *Institute of Certified Management Accountants, Australia.* [Online] Available at: http://www.cmawebline.org/about-icma.html [Accessed 23 03 2017].
- International Federation of Accountants, 2017. *About IFAC.* [Online] Available at: https://www.ifac.org/about-ifac [Accessed 04 04 2017].
- Porter, M. E., 1985. *Competitive Advantage.* New York : The Free Press.
- Powell, T., 2001. *The Knowledge Value Chain (KVC): How to Fix It When It Breaks.* New York, M.E. Williams.
- Zack, M. H., 2003. *What is a Knowledge Based Organization ?.* [Online] Available at: http://www2.warwick.ac.uk/fac/soc/wbs/conf/olkc/archive/olk5/papers/paper62.pdf [Accessed 06 04 2016].