



(i) **Financial Accounting.** It is the original form of accounting. It is mainly confined to the preparation of financial statements for the use of outsiders like shareholders, debenture holders, creditors, banks and financial institutions. The financial statements, i.e., the Profit and Loss Account and the Balance Sheet, show them the manner in which operations of the business have been conducted during a specified period.

(ii) **Management Accounting.** It is accounting for the management, i.e., accounting which provides necessary information to the management for discharging its functions. According to the Chartered Institute of Management Accountants, London, "management accounting is 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." It covers all arrangements and combinations or adjustments of the orthodox information to provide the Chief Executive with the information from which he can control the business, e.g., information about funds, costs, profits, etc.

Management accounting covers various areas such as cost accounting, budgetary control, inventory control, statistical methods, internal auditing etc.

### 1.11 DIFFERENCE BETWEEN MANAGEMENT ACCOUNTING AND FINANCIAL ACCOUNTING

Financial accounting and management accounting are closely interrelated since management accounting is to a large extent the rearrangement of the data provided by financial accounting. Moreover, all accounting is financial in the sense that all accounting systems are in monetary terms and the management is responsible for the contents of the financial accounting statements. In spite of such a close relationship between the two, there are certain fundamental differences. These differences can be laid down as follows:

1. **Objectives.** Financial accounting is designed to supply information in the form of Profit and Loss Account and Balance Sheet to external parties like shareholders, creditors, banks, investors and Government. Information is supplied periodically and is usually such in which the management is not much interested. Management accounting is designed principally for internal use by the management.

2. **Analysing performance.** Financial accounting portrays the position of business as a whole. Financial statements like income statement and balance sheet report on the overall performance or status of the business. On the other hand management accounting directs its attention to the various divisions, departments of the business and reports about the profitability, performance etc., of each of them. Financial accounting deals with the aggregates and therefore cannot reveal what part of the management action is going wrong and why. Management accounting provides detailed analytical data for these purposes.

3. **Data used.** Financial accounting is concerned with the monetary record of past events. It is a post-mortem analysis of past activity and therefore out of date for management action. Management accounting is an accounting for future and, therefore, it supplies detailed and analysed data both for the present and the future in "management language", so that it becomes a basis for management action.

4. **Monetary measurement.** In financial accounting only such economic events find a place which can be described in money. However the management is equally interested in non-monetary economic events, viz. technical innovations, personnel in the organization, changes in the value of money, etc. These events affect the management's decision and therefore management accounting cannot afford to ignore them. For example, a change in the value of money may not find a place in financial accounting on account of "growing concern concept", but while effecting an insurance policy on an asset or providing for replacement of an asset, the management will have to take this factor into account.

5. **Periodicity of reporting.** The period of reporting is much longer in financial accounting as compared to management accounting. The Income Statement and the Balance Sheet are usually prepared yearly or in some cases half-yearly. Management requires information at frequent intervals, and, therefore, financial accounting fails to cater to the needs of the management. In management accounting there is more emphasis on furnishing information quickly and at comparatively short intervals as per the requirements of the management.

6. **Precision.** There is less emphasis on precision in case of management accounting as compared to financial accounting since the information is meant for internal consumption.

7. **Nature.** Financial accounting is more objective while management accounting is more subjective. This is because management accounting is fundamentally based on judgement rather than on measurement.

8. **Legal compulsion.** Financial accounting has more or less become compulsory for every business on account of the legal provisions of one or the other Act. However, a business is free to install or not to install, a system of management accounting.

The above points of difference between financial accounting and management accounting prove that management accounting has a flexible approach as compared to the rigid approach in the case of financial accounting. In brief, financial accounting simply shows how the business has moved in the past while management accounting shows how the business has to