The Importance of An Accounting Information System in the Strategic Management Process

Aaron Caillouet and Bill Lapeyre, *Nicholls State University*

Information systems provide essential data about the activities of a firm to managers at all levels. Managers can use this information to make rational and intelligent judgments in the decision-making process. One of the most useful types of information provided is financial data. Optimal decisions require the use of effective, efficient, and timely financial data. The financial data are supplied to management from the accounting function to be used as a decision-making tool (Warren & Fess, 1989).

The accounting process is responsible for information of all types throughout the organization. However, one of its most important roles is reporting activities in the evaluation stage of the strategic management process (SMP). The evaluation stage is the fifth and final stage of the SMP. The SMP consists of defining a mission, setting goals, formulating strategy, implementing the strategic plan, and evaluating the plan. Evaluating involves more than just evaluating performance against a predetermined plan. It also involves reviewing the entire situation and initiating corrective adjustments (Thompson, 1990).

Financial vs. Managerial Accounting

Financial reports prepared for users are based on what is known as Generally Accepted Accounting Principles (GAAP). GAAP represents widely accepted agreement on the guidelines for accounting theory and practice. Several groups have a role in the establishment of GAAP. The Financial Accounting Standards Board (FASB), the American Institute of Certified Public Accountants (AICPA), and the Securities and Exchange Commission (SEC) are three of the major groups. The FASB has the primary responsibility for developing and issuing rules. The AICPA has some indirect influence through its senior technical committees. The SEC is an agency of the federal government with legal power to set and enforce accounting practices for companies whose securities are offered for sale to the general public. SEC actions become legal reporting requirements.

Although the SEC's major focus is somewhat different from that of the other groups, it has enjoyed a good working relationship over the years with the FASB and FASB's predecessor, the Accounting Principles Board (APB). Other groups that affect accounting standards are the Internal Revenue Service (IRS), the International Accounting Standards Committee (IASC), the National Association of Accountants (NAA), and the American Accounting Association (AAA). The NAA is composed mainly of managerial accountants working in private firms while the AAA takes an academic and theoretical point of view. The AAA is composed mostly of instructors of accounting in universities.

Financial reports prepared in accordance with GAAP are called general-purpose because they are prepared for all users, both internally and externally. They provide decision-making information for company managers as well as creditors, stockholders, potential investors, and the IRS and others. Consequently, they need to be uniform.

Managerial reports are prepared for internal purposes to aid the manager in decision-making. They are not restricted to GAAP, hence firms can be innovative in the type of information necessary for their particular firm or situation. This article is specifically concerned with the reporting of managerial information and how it can be used to facilitate the SMP through the evaluation stage.

Identification of Users

To understand the complexity of the accounting information system one need only look at the constituency of financial data. Accounting has diverse user needs because it is a service activity acting as an information system for business decisions at all levels. It measures business activities by recording data about them for future use. Through data processing, the data are stored until needed. Then data are processed to provide useful information and communicated through reports (Needles et al., 1990).

The process of using accounting to provide information to users involves more than gathering, processing, and communicating information. It also involves identifying user groups and their needs. Users can be classified in three categories: internal; external with direct financial interest; and external with indirect financial interest.

Internal users include owners and managers at all levels. Management consists of the board of directors, officers, department heads and supervisors. External users having direct financial interest include potential investors and creditors such as suppliers and banks. The third category of users, external with indirect interest, is far reaching and includes taxing agencies, regulatory agencies, economic planners, employees, the Federal Reserve, labor unions, financial advisors, customers, and the public in general. A system to satisfy the needs of these diverse categories of users is very complex.

Role of Managerial Accounting

Although managerial accounting is the area of accounting that provides information for the entire management process (planning, organizing, directing, and controlling), our concentration will be on the functions of strategic planning and controlling. Strategic planning involves the development of a long-range course of action to achieve desired results. A strategic plan often encompasses periods of five to ten years and is a function of the highest levels of management.

Controlling involves attempting to achieve goals identified in the plan, in our case the strategic plan. The process includes the monitoring of results by comparing the expected with the actual. Through this feedback, management can investigate significant variations from the plan. Another common term for this process is "management by exception" (Warren & Fess, 1989).

Achieving An Adequate Accounting Information System

Achieving effective, efficient, and timely financial data for evaluating the SMP is not easy and involves the complex pitfalls of any information system. One of several keys to providing the proper data for management is adequate executive support. Any system needs support from the top. Since executives are directly involved in the SMP, support is perhaps more prevalent than in other information systems. However, if they are simply going through the motions in the SMP, chances are they won't support the system sufficiently for proper evaluation.

Well-defined system objectives and information requirements are also key to a successful information system. Financial data systems are not exceptions to this premise. Any successful system needs objectives that are defined. A system with specific goals will accomplish more for an organization than one with no goals, few goals, or ambiguous goals. An important factor in setting objectives is to make them challenging yet attainable. A financial goal of simply achieving a dollar volume of sales might be easily met, but will do very little by itself toward making adequate profit or solving complex management problems.

Effective information execution requires an organization to develop a number of support systems. Hiring a competent and adequate staff is perhaps the most important. Huge investments in hardware, software, and other support is certainly important, but without the competent human resources to coordinate the system, the result will be inaccurate, untimely, and insufficient information (Watson, 1990).

The Strategic Management Process

An accounting information system is necessary to gain the full advantage of the SMP in an organization. Without the proper financial information the SMP will not have the feedback system so essential to the correcting adjustment phase in strategic planning (Warren & Fess, 1989).

The SMP determines the long-run competitive performance of the organization. It provides a systematic blueprint to plot the future for the organization in terms of goals, activities, and methods to accomplish these goals. The SMP also links the goals of the organization and the environment, and identifies and develops responses to important trends for greater organizational effectiveness.

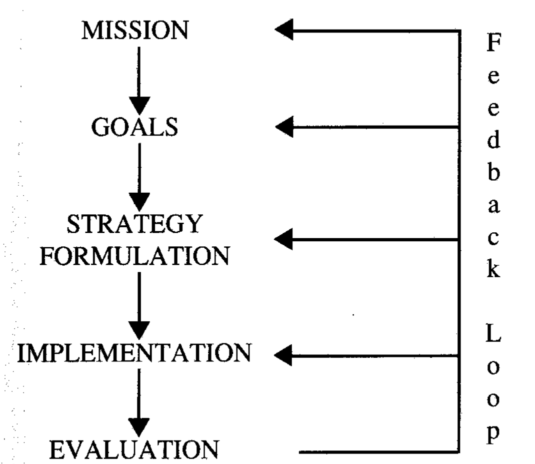
An organization's SMP consists of the following five components: (1) defining a mission; (2) setting goals; (3) formulating the strategic plan; (4) implementing the strategic plan; and (5) evaluating the strategic plan. The evaluation process is an accounting function requiring a sophisticated financial data information system not only to review negative variances from goals but also to subsequently review the entire process to achieve maximization of purpose.

Components of the SMP

The evaluation process provides feedback for

FIGURE 1

THE STRATEGIC MANAGEMENT PROCESS



evaluating the mission goals, the plan, and its implementation (see Figure 1).

Determining the mission for an organization is, in essence, the process of defining the purpose of the organization. The mission should accomplish the following:

1. Define the business of the organization.
2. Identify the markets and products in which the organization intends to be successful.
3. Identify the environmental domain.
4. Provide motivation to the organization.
5. Provide for resource allocation.
6. Provide communication to every member of the organization.
7. Facilitate the consideration of appropriate and timely changes.
8. Establish a mechanism to convert the mission into clear objectives designed to fulfill the mission.

The mission should be stated in broad enough terms to allow the organization to express creativity but be specific enough to define a path to success.

Organizational goals designed to carry out the purpose and mission are long-run and short-run in nature and intended for managers at all levels. Total goals can be achieved only if everyone does his or her part. Goals provide managers a base for strategy formulation and selection of alternatives.

Once the mission is established and goals are set, the strategic plan should be formulated. This involves establishing a game plan to produce desired objectives. An assessment of prior performance, current position, and desired future position is necessary to formulate an adequate plan. The assessment should include a review of the organization's strengths, weaknesses, opportunities, and potential threats to the achievement of its mission.

Implementing the strategic plan involves the entire management function to assure that all aspects of the operation stay on track to achieve organizational goals. It involves the functions of finance, research, production, marketing and human resources. All aspects of the organization — structure, resources, skills, motivation, financial support, and culture — should be optimized (Aldag & Stearns, 1991).

Evaluation of the SMP

The last major step in the SMP is to control the organization's performance through an evaluation process. The accounting information system is critical to this process. Not only does management need to determine the control standards but it must measure performance, compare standards to performance, determine reasons for variances, and take necessary actions to correct problems. Without an efficient system to accomplish this, the organization will function at a less than acceptable level. Only with a detailed comprehensive information system can adequate performance be achieved in the long run.

As illustrated by the SMP with the feedback network, the first four steps in the SMP are not merely one-time steps. Continually changing circumstances make corrective adjustments desirable during the life of an organization. Changing circumstances could cause the business to be redefined, altering long-term direction, and narrowing or broadening management vision. Performance targets may need adjustments as a result of past experience or future prospects. Therefore, the SMP and the search for excellence is a continuous process (Thompson &

Strickland, 1990).

The accounting information system aids the continuous SMP through the following functions:

1. Planning reports that estimate the effects of alternative actions.
2. Designing and implementing procedures for the accumulation of data to all interested users.
3. Preparing budgets and budget analyses to focus on the comparison of the actual results to those planned.
4. Providing performance reports of these variances.
5. Providing special reports as needed in analyzing current problems and their effect on future operations (Warren & Fess, 1989).

The complex maze of coordinated reports generated by the accounting information system is designed specifically to determine what to control, set control standards, measure performance, compare performance to standards, determine the reasons for deviations, and take corrective action. They are designed to provide management with information to use in planning, organizing, directing, and controlling in the SMP (Smith et al., 1988).

Summary and Conclusions

Managers at all levels are provided vital information for their respective areas. The responsibility of providing this information lies with the accounting information system. The particular functions of planning and controlling are directly served by these data. The other functions are served through the evaluation and feedback of the strategic management process as a result of the data produced by the accounting information system.

The SMP involves five steps: defining a mission; setting goals; formulating strategy; implementing the strategic plan; and evaluating the entire process. Without the evaluation stage, which is a responsibility of the accounting information system, the process would not be continuous and would function improperly.

The accounting information system accomplishes its evaluation task by planning reports which estimate the effects of alternative actions, by designing and implementing procedures for the accumulation of data to all interested users, and by preparing budgets and budget analyses to focus on the comparison of the actual results to the plan. In addition, it provides performance reports of the variances and provides special reports to analyze problem areas. The strategic management process, which is so vital to success, is only as strong as the feedback provided by the accounting information system.

Dr. Caillouet, who specializes in strategic management, has published numerous articles in a variety of publications; Mr. Lapeyre has extensive experience in strategy formulation and is currently researching long-term planning for his MBA.

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