A SURVEY OF CHIEF EXECUTIVES' PERCEPTION OF ACCOUNTING FOR MANAGEMENT CONTROL IN GOVERNMENT MINISTRIES AND PARASTATALS

BY

OKO, KANAYO CHIKODINAKA

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DECLARATION

I hereby declare that this project is original and a product of my study.
All materials used have been acknowledged accordingly in the references.

SIGNATURE:______________ DATE: 12/07/96
KANAYO C. OKO

CERTIFICATION

This project report entitled, "**A SURVEY OF CHIEF EXECUTIVES' PERCEPTION OF ACCOUNTING FOR MANAGEMENT CONTROL IN GOVERNMENT MINISTRIES AND PARASTATALS**" By **KANAYO CHIKODINAKA OKO,** meets the regulations governing the award of the degree of Master of Business Administration of Ahmadu Bello University, Zaria and is approved for its contribution to knowledge and literary presentation.

CHAIRMAN, SUPERVISORY COMMITTEE — DATE: 24/12/98

MEMBER, SUPERVISORY COMMITTEE — DATE: __/__/__

MEMBER, SUPERVISORY COMMITTEE — DATE: __/__/__

HEAD OF DEPARTMENT — DATE: 24/12/98

DEAN, POSTGRADUATE SCHOOL — DATE: 02/09/99

DEDICATION

This project is dedicated to my loving, humble and amiable wife, Mrs UZOAMAKA IFEOMA OKO and to my Children - ONYINYE, CHIAMAKA, CHUKWUDI and CHUKWUEMEKA.

ACKNOWLEDGEMENT

I am most grateful to God for giving me the strength, will and ability to write this project. To my wife and children , I find words grossly inadequate to express my gratitude. Your support was immeasurable.

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My late parents - Mr. Samson Nnefe Oko and Mrs. Bessie Nwadika Oko, for all their sacrifice and self-denial to make sure I got the fullness of western-type education, deserve a pat on the back. I wish you a perfect rest in the bosom of God .

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ABSTRACT

The present untoward economic circumstances prevailing in the country today have made employment in the government ministries and parastatals unattractive.

Consequently, there is mass exodus of qualified staff from the public sector of our economy to the more lucrative private sector, leaving the formulation and execution of government policies and programmes in the hands of mediocrities.

Regrettably, some chief executives of government ministries and parastatals have taken advantage of this loop-hole, occasioned by the flight of qualified professionals from the public sector, to manipulate well intended internal control system of the government to suit their whims and caprices.

Many a regime have at one time or the other, harped on probity, accountability, cost consciousness, profligacy and planlessness in the public sector but without success.

The reason is not far fetched. How can you control what you do not know either by definition or causation?

We are therefore of the firm belief that the only sure way to curb the aforesaid seemingly intractable problems in the public sector is the provision of adequate incentives comparable with those in the private sector so as to attract and retain qualified staff. With the presence of trained personnel like accountants, economists e.t.c, in the organization, there is no gain saying that the benefits of accounting for management control will be fully reaped. More so if the chief executives are exposed in this new field of accounting (accounting for management control)through seminars and conferences.

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LIST OF ABBREVIATIONS AND SYMBOLS

1.	BE	- BREAK EVEN
2.	CM%	- CONTRIBUTION MARGIN PERCENT
3.	C-V-P	- COST-VOLUME-PROFIT
4.	II	- PROFIT

CHAPTER ONE

INTRODUCTION

1.1 General introduction

It is a matter of great regret that in this present jet age Government ministries and parastatals are accused of financial impropriety that borders on wasteful expenditure, lack of cost consciousness, and lack of planning. Who is to be blamed?

A survey of Chief Executive perception of accounting for management control in government ministries and parastatals is therefore necessary since they are the chief accounting officers.

Accounting for management control may be defined as the application of accounting techniques to the provision of information designed to assist all levels of management in planning and controlling the activities of the organization.[1]

Due to its newness, relative to financial accounting, many people profess to be applying accounting for management control by mouth. They seem to believe that once accounting is mentioned what is meant just has to be in the area of financial accounting. But accounting for management control goes farther than financial accounting. Financial accounting is concerned with the external requirement of creditors, shareholders, prospective investors, Registrar of Companies, the inspector of Taxes and persons outside the management as well as with the internal requirements of the

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[1] *Sizer,J. (1977) An insight into Management Accounting. Penguin Books, England, P. I.*

management; these objectives are satisfied through the recording of revenue received and expenditure incurred by the Company so that its overall trading position can be ascertained at any point in time.

Accounting for management control on the other hand is concerned with assisting management in planning and decision making presenting accounting information in such a way as to assist management in the creation of policy and in the day-to-day operation of an undertaking.

Many Chief Executives therefore, while saying that they apply accounting for management control still fall back to historical costs generated by the financial accounting system. We are not saying that past records are bad per se. "It is only worth pointing out that the major draw back in using historical data for judging performance is that inefficiencies may be concealed in the past performance; moreover the usefulness of comparisons with the past is also limited by intervening changes in economic conditions, technology, competitive manoeuvre, personnel e.t.c."[2]

Accounting for management control comes in here to help managers keep abreast with current operations by reporting and interpreting information that aid chief executives to focus on operating problems, imperfections, inefficiencies and opportunities.

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2 Hongren, C.T.(1975) Accounting for Management Control Prentice-Hall International, London. P. 139.

1.2 Statement of the problem

There is no gain saying the fact that financial indiscipline culminating in deficit spending, profligacy and planlessness is the bane of government ministries and parastatals today. This is rather surprising, more so for any government that professes to hold probity and accountability in high esteem. This research therefore probes into causes of these untoward circumstances in selected government ministries and parastatals in Kaduna State.

1.3 Purpose and significance of the research

It is an indisputable fact that one cannot control what he neither knows by definition nor causation.

Accounting for management control is the application of accounting techniques to the provision of information designed to assist all levels of management in planning and controlling the activities of the organization.

Tricker (1967) noted that : "The physical resources of an organization may include manpower, money, machines and materials.

To these four is added incoming orders and information." Information is the most valuable resource the organization has. Without it, none of the other resources can be fused into a working system. What cement is to the mason is what information is to Chief executive. And management information stems from the accounting for management control system.

The role of accounting for management control in an organization generally is perceived to be the provision of information for decision making by various elements of the organization's hierarchy. The use of such information in the elevation of performance is a critical aspect of decision making function. The story of the wood-cutter goes to buttress the pervasiveness of accounting for management control.

"A man was watching a wood-cutter working very hard on a hot summer's day. After several trees had been felled, the wood-cutter paused for a few minutes rest during which time the onlooker took the opportunity to say, "I hope you won't mind my mentioning this, but you would get those trees much faster if only you sharpened your axe."

I haven't got time for that, replied the wood-cutter irritably, I have got twelve more trees to fell before I leave today and I am already behind because this axe is so blunt.

"Good information is like a sharp axe. You use less effort in obtaining better reward."[3]

Thus, this study as a matter of fact is intended:

(1) To determine Chief Executives' perception of accounting for management control in government ministries and parastatals in Kaduna state.

(2) To make recommendations on how deficit spending, profligacy and planlessness in government ministries and parastatals can be minimized.

1.4 <u>The scope of the study</u>

This study for effectiveness covers only the Government ministries and parastatals within Kaduna State of Nigeria.

A total of fifty Government Ministries and parastatals where studied and the views of their chief executives in the areas of planning, budgeting and controlling were critically assessed with

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[3] *Pitcher, M.A.(1969) <u>Management Accounting for the lending Banker.</u> The Institute of Bankers London, P. 20*

a view to determine their perception of accounting for management control.

1.5 limitations of the study

The limitations of the study were various and include:-

(i) Time: The time for the submission of this study was very limited as a project of this importance needs considerable time and attention for remarkable impact.

(ii) Finance: Financial constraints were of course a major militating factor considering the poor economic situation in the country presently. Consequently, the ability of this researcher in collecting much needed data and information were curtailed.

1.6 Hypothesis

No doubt you cannot control what you do not know either by definition or causation.

Hence, cost consciousness, frugal spending and proper planing is the result of a chief executive's perception of accounting for management control.

1.7 Plan of the study

This project is divided into five chapters: Chapter one starts with the introduction of the study. This section deals with the background of the study, statement of the problem, limitations of the study, purpose and significance of the research, the scope of the study, hypothesis as well as the definition of terms.

Chapter two focuses on Literature review. Under this chapter is treated the historical background of accounting for management control and its relevance to not for profit making establishments like government ministries and parastatals.

Chapter three deals with the research methodology. It tries to discuss the sources of data as well as the methods of collecting the data.

In chapter four, the data are presented and analysed. In this chapter, efforts are made at measuring the level of Chief executives' perception of accounting for management control. The results of this presentation are analysed.

Chapter five which is the last chapter, draws out the summary, conclusion and the recommendations of the project.

1.8 Definition of terms

Budgeting : A budget is a pre-determined statement of management policy during a given period which provide, a standard for comparison with the results actually achieved.

It is also defined as a formal quantitative expression of management plans.

Controlling : Controlling means the implementation of plans and the use of feed-back so that objectives are optimally obtained.

Planning : Planning is deciding in advance what to do, how to do it, when to do it, and who is to do it. Planning bridges the gap from where we are to where we want to go. It involves selecting from among alternative future courses of action for the enterprise or section within it.

CHAPTER TWO

LITERATURE REVIEW

2.1 Introduction

There is no escaping the linkage of accounting and management, more so internal accounting most often called accounting for management control. The role of accounting for management control in organizations generally is perceived to be the provision of information for decision making by various elements of the organisations hierarchy. The use of such information in the evaluation of performance is a critical aspect of decision making function. Even the chief executives of very small establishment who are often padding so furiously just to keep their heads above water agreed that it aids them in decision making.

It is well established that accounting information should be the most important tool in any management set up. Every organisation has resources which it uses to fulfil its purpose. The physical resources of an organisation may include manpower, money, machines, materials. To these four is added incoming orders and information. Information is the most valuable resource an organisation has without it none of the other resources can be fused into a working system. What cement is to the mason is what information is to chief executives. And management information stems from the accounting for management control system.

Again, although management use of accounting information is not new-some of the techniques of accounting for management control have been used for many decades. But one may be surprised to know that many chief executives have not heard of accounting for management control before. Hence they do not have accounting for management control set up in their organisations. However, this is not unexpected in view of the developing nature of our economy.

The term accounting for management control developed real meaning during the 1950s. The concepts are well tested and have become increasingly fashionable and accepted over the past 40 years.

The National Association of Accountants (1963) had this to say;

> *A broad new field of accounting has evolved since the beginning of the 20th century. While it had its origin in historical financial accounting and cost accounting, it is designed to provide financial data to guide management actions oriented towards the present and future. It serves management at all levels. The term accounting for management control describes this field with accuracy and seems to be gaining rapid and widespread acceptance.*

The lukewarm attitude in the setting up of accounting for management control models may also be attributed to the dearth of knowledgeable people in the field.

In the sections that follow, I shall be discussing accounting for management control in the broad areas of planning, controlling and budgeting.

2.2 **Planning**

In designing an environment for the effective performance of individuals working together in groups, the most essential task is to see that purposes and objectives, and methods of attaining them, are clearly understood. If group effort is to be effective, people must know what they are expected to accomplish and how it can be done. It is fundamentally a technical activity concerned with the problem of choice among alternatives in the resource management process. "Planning provides answers to two questions: What is desired? when and how is it to be accomplished?"[4]

Planning is the formulation of policy in a broad sense, selecting from a number of alternatives the most appropriate cause of action and then obtaining the necessary resources. Plans are sometimes regarded as being inflexible blue print which might be followed to the minute detail, unfortunately, they are followed even though it is clear to everyone that they are outmodeled.

And in serious cases quite suicidal to the organisation. What is required is amended or adopted plan to suit the changed conditions. Because of the dynamic state of business and environment which it operates, no board of directors can afford simply to define objectives and then wait for profit. There is need for a general statement on the policy to pursue.

2.2.1 Functions of planning

Planning is a function that answers four questions

(1) Where are we now

(2) Where do we want to be

(3) What is the difference between where are we now and where do we want to be

(4) How can we get there from here.

Indeed planning looks to the future to determine the direction in which an organisation or its units should be going. To be successful in business over a period of years there must be a goal. So planning and application of strategy are fundamental importance in both

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[4] *Hongren, C.T.(1975) Accounting for Management Control. Prentice-Hall International, London, P.7*

achievement of that goal and control of the business while neonate to it. Note that size of the organisation is immaterial. And that is why some authors advocate for corporate planning for the following reasons:

(1) To reach target set

(2) To avoid failure

(3) To ensure the adoption of common aids by every one in the organisation

(4) To measure achievement on a continuing basis.

An understanding of these reasons inform the basic answer to the question where does planning start? Where does planning end? Which route to get there? and what to do on arrival? Addressing the first question, planning starts on the understanding of the organisation present position considering all aspects of the business particularly financial actors e.g the turnover and profit, marketing and marketing methods e.g range and quality of products. Who are the key personnel in the organisation. The control system employed. All these necessitate a number of strategies like the setting of finance and non financial goals for each aspect of the business and the determination of suitable time scale in the plan. In addition, this defines the need for appropriate yardstick for measuring progress.

The actual means of displacement of corporate position is determined from corporate target and condition. What ever be the position and the condition, it is very necessary to start planning for the next period well before the current one ends, answering the question where the plans start.

2.2.2 **Hierarchy of planning**

There are usually hierarchy of planning:-

(1) Strategic

(2) Tactical

(3) Operational

Strategic planning

This is the process of determining the major objectives of an organisation and policies and strategies that will govern the acquisition, use and disposition of resources to achieve these objectives. This view of strategic planning is shared by a number of authors including sterner. In this conceptualization policies are subsumed to be broad guides to action and strategies are the means to deploy resources. What is important is that although all managers plan, strategic planning takes place primarily habitually at the top level of management and is directed towards attaining a desired position for the organisation in the environment. Such planning determine what should be the overall and continued objective of the organisation. According to Peter Drucker, "Managers must be skilled in making decisions with long futurity on a systematic basis".

Accordingly therefore, management has no choice but to anticipate future to attempt to mould and balance short range and long range goals. But Drucker lamented that it is not given to mortals to do well in all these things so he argued that lacking divine guidance management must make sure that this difficult responsibility is not overlooked or relegated. Therefore, "The present and immediate short range plans require strategic decisions fully as much as the long range". But the long range is the envelop of short range decisions. Unless the long range is built into and based on short range plans and decisions, the most elaborate long range plans will be an exercise in futility. And conversely, unless the short range plans, i.e the decision on the here and now are integrated in one plan of action they will be simply expedient guesses and misdirections.

Planning what is our business, planning what it will be and planning what it should be have to be integrated. What is short range and what is long range is then decided by the time span and futurity of the decisions. Everything that is planned becomes immediate work and commitment.

Peter Drucker listed four things that strategic planning is not:-

(1) Strategic planning is not a box of tricks or a bundle of techniques. It is analytical of thinking and commitment of resources to action. In this conceptualization, many techniques may be used in the process of strategic planning but then again none may be needed e.g strategic planning may need computing but the most important question what is our business or what should it be cannot be quantified on program for the computer. But no matter what it is, cannot answer these questions. So model building or simulation may be helpful but they are not strategic planning. They are outlook for specific purposes and may or may not apply in a given case. What is being said is that quantification is not planning. Strategic planning is the application of scientific planning to business decision. It is the application of thought, analysis, imagination and judgement. It is indeed responsibility rather than technique.

2. Strategic planning is not forecasting. Indeed it is not master minding the future. Peter Drucker says that any attempt to do that is foolish. The future is not predictable. The fact is that you can discredit by attempting to do it.

Peter Drucker therefore observed: "If any one suffers from the illusion that human are able to forecast beyond a very short term span, look at the headline of yesterday paper which of them could possible have predicted a decade ago". He said you must start out with a premise that forecasting is not respectable human activity and not worth while beyond the shortest period.

Strategic planning is necessary precisely because we cannot forecast. Therefore, it is not forecasting. Forecasting attempt to find the most probable cause of event or at best a range of probabilities. But the entrepreneur problem is the unique event that will change the possibility. The entrepreneur universe is not physical but social universe.

In essence, Peter Drucker argued that the central entrepreneur contribution which is rewarded is a profit. It will bring about the unique event or innovation that changes the economic, social or political situation.

3. Strategic planning does not deal with future decisions. It deals with futurity of present decisions. Decisions exist only in the present. The question that faces the strategic decision maker is not what the organisation should do tomorrow, it is what do we have to do today to be ready for an uncertain tomorrow.

What futurity do we have to build into our present thinking and doing what time span do we have to consider and how do we use this information to make a rational decision now.

4. Strategic Planning is not an attempt to eliminate risk. Is not even an attempt to minimize risk. Such an attempt can lead to only irrational and unlimited risk and to certain disorder. Economic activity by definition commit present resources to the future ie to highly uncertain expectations. To take risk is the essence of economic activity so it has been argued that while it is futile to try to eliminate risk and questionable to try to minimize it, it is essential that the risks taken are the right risks. The end result of successful strategic planning must be the capacity to take a greater risk for this is the only

way to improve entrepreneur performance. But to extend this capacity we must understand action rather than plunging into uncertainty on the basis of hear say no matter how carefully quantified.

Peter Drucker sees strategic planning as a continuous process of making present risk taking decisions systematically and with greater knowledge of their futurity, organising systematically the effort to carry these decisions and measuring the results of these decisions against the expectations through organized systematic feedback.

Tactical planning: Tactical Planning or co-ordinating planning involves determining how certain areas of the business will deploy resources to reach objectives by following the policies and strategies that have been established in the strategic planning process. A major characteristic of tactical planning is the co-ordination of the most important function of the organisation in the service of the strategic plans.

Operational planning: This is short term detailed and concentrated primary and functional aspect of production goods and services. It involves e.g the production scheduling of goods and services, the purchase of materials for inventory or simply the development of course outline by the teacher.

2.2.3 **Dimensions of planning**

There are five dimensions of planning. These include

(1) The organisation

(2) Subject

(3) Element

(4) Time

(5) Characteristics

The Organisation: What type of organisation? The nature determines the type of plan. Whether at the level of subsidiary, division, department. These can be looked at conceptually.

Subject: Will it include research, production, financial, facility, manpower etc.

Element: What rule, procedure, charter. what program?

Time: Dealing with a situation that is perpetual, short range, long range.

Characteristics : Economical, flexible or inflexible type of thing. International or national.

Whether you are talking of case of written or unwritten, confidential or public, qualitative or quantitative comprehensive or narrow, complex or simple.

Knowing the characteristics determines how you perform it. Huse in his book, "management" reorganised road block to effective planning in three areas:-

(1) Attitude and value of management
(2) Design of planning systems
(3) Implementations of plans

Examine a situation where top management views systematic long range planning as unimportant. In this situation, lower level managers will exert minimal effort and thoughts.

The design of the planning system can constitute a road block to planning by:-

(1) Lack of rewards
(2) Lack of participation
(3) Lack of specific objectives
(4) Lack of balance between formality and informality.

Four major obstacles in the area of implementation can be recognized:-

(1) Confusion between planning and reality.
(2) Lack of motivation to implement plans.
(3) Lack of orientation
(4) Lack of training.

2.2.4 **The selection of objectives**

The purpose of every plan and all derivative plans is to facilitate the accomplishment of enterprise purpose and objectives. Objectives properly developed and applied, can tell chief executives in what paths, new and old, their total undertakings should be moving. They can guide both the day-to-day activities and personal development of individuals in an organisation. Without clear objectives management is haphazard and random, and no individual, no group can expect to perform effectively or efficiently unless a clear goal is sought.

It has been noted that to be meaningful, objectives must be verifiable. The easiest way to get verifiability is to put goals in quantifiable terms. Instead of saying a goal is to make a profit, we must say that it is to make =N=100,000 in profit after taxes in 1995 by selling =N=2 million worth of products with =N=1 million in product line A, =N=.5 million in line B and C respectively at a gross profit margin of 20%, a net profit taxes of 5% and a return on stockholders equity of 15%.

From the foregoing paragraph it stands to reason that for all information pouring into the accounting system to be useful, it must be quantified.

2.2.5 **Application of cost volume analysis in decision making.**

Broadly, accounting for management control branches naturally into two major branches: decision accounting and control accounting.

Decision accounting is essentially planning which is in itself an attempt to provide information that will enable management to take decisions between alternatives and to measure the profitability of various allocations of resources in the organisation. The key relationships between costs, volume and profit need to be understood by chief executives and rational decision making can be helped by providing data to reveal these relationships.

If we make the assumption that organisational objectives are towards profit maximisation then attention must be paid to the monitoring and understanding of the relationship between these elements that go to make up profit, namely: costs and revenues at different levels of production.

Among the several tools available to management in its process of decision - making is the cost - volume - profit (C - V - P) analysis. C-V-P analysis is the study of the inter-relationships of he volume of sales, elements of costs, and profit. The analysis has often been narrowly described as "break-even" analysis, which is merely its starting point.

The focus in the C-V-P analysis goes beyond the break-even point to the impact which various decisions that affect sales and costs have upon net income. The break-even point is the point of zero profit and zero loss, and it is only incidental to the C-V-P analysis.

A review of the accounting literature reveals that the C-V-P analysis was for a long time, until about two decades ago, considered under the assumptions of deterministic variables alone. As a result of this type of analysis (which is now usually referred to as the traditional model of C-V-P analysis), the solutions developed to the C-V-P relationship are deterministic as well.

But recently, uncertainty has been introduced into the analysis and its application to mult-product or mult-process companies has been delved into.

However, in this paper, only the traditional model shall be discussed.

Traditional Model: linear function: This model is built on certain assumptions, the major ones of which shall be briefly mentioned here.

Within a specified range of production or sales volume (usually referred to as the relevant range), Fixed costs and selling prices are assumed constant, variable costs and total revenue are assumed as changing proportionally with volume. All costs are assumed to be resolvable into fixed and variable elements. Thus costs and revenue are assumed to have a deterministic behaviour and to be linear over the relevant range.

C-V-P analysis is generally prepared from annual or monthly budget figures. Alternatively, the historical data of the company are used to draw the lines of best fit, though the company must be careful to avoid the possible distortion that may arise out of historical data covering either too short or too long a period of time.

The shorter the period of time covered by the historical data, the relatively greater will the random fluctuations resulting from the inherent inaccuracies of profit measurement.

Conversely, the longer the period of time covered, the further away from the current profit - volume relations will be the result derived from the analysis because of significant changes which might have taken place.

C-V-P relationships can simply be stated as:

$R = PX$

where

R = total revenues

P = unit selling price

X = number of units produced and sold in the case of a service organisation, X would refer to the number of units of service produced, such as meals served or insurance policies sold.

The total cost for firm is:

$T = a+bx$

where

T = total costs

a = fixed costs

b = variable costs per unit

x = number of unit produced and sold.

Profit is the difference between total revenues and total costs:

$\Pi = R - T$

where

Π = profit

R and T are as previously defined.

Contribution margin: The difference between the unit selling price, P and the unit variable cost, b is the unit contribution margin. In manufacturing organizations, the unit contribution margin is the amount that each unit produced and sold contributes toward covering fixed costs and providing a profit. Profit is the amount by which the total contribution margin exceeds the fixed costs. Total contribution margin is computed as the unit contribution margin multiplied by the number of units produced and sold. Total contribution margin can also be calculated as the difference between total revenues and total variable costs.

<u>Illustration:</u> The DICON Furniture Company manufactured and sold 20,000 units of a standard model furniture during 1994. The unit selling price was =N=60. Variable manufacturing costs of =N=40 consisted of direct materials, direct labour, and variable factory overhead of =N=20, =N=15 and =N=5 respectively. Fixed factory overhead was =N=250,000. Selling and administrative costs included a variable element of =N=5 per unit manufactured and sold and a fixed element of =N=50,000.

To determine DICON Furniture's unit contribution margin, all variable costs must be added together and deducted from the unit selling price.

Unit variable costs	=N=
Direct materials	20
Direct labour	15
Variable factory overhead	5
Variable selling and administrative	5
Total	45

The unit contribution margin is =N=60 - =N=45, or =N=15. Note that variable selling and administrative costs as well as the variable manufacturing costs were included in the computation.

The total contribution margin at 1994 volume is the unit contribution margin multiplied by the number of units produced and sold or =N=300,000 (=N=15 x 20,000 units). The total contribution margin can also be computed by deducting the total variable costs from the total sales:

	=N=
Total sales (20,000 x =N=60)	1,200,000
Total variable costs:	
Direct materials (20,000 x =N=20)	400,000
Direct Labour (20,000 x =N=15)	300,000
Variable factory overhead (20,000 x =N=5)	100,000
Variable selling and administrative (20,000 x =N=5)	100,000
	900,000
Total Contribution Margin	=N= 300,000

Contribution margin percent: The contribution margin concept is sometimes expressed as a percentage of sales. The contribution margin percent (CM%), also called the contribution margin ratio, is the portion of each sales Naira that goes to covering fixed costs and to profits. This percentage can be calculated using either :

(1) Unit contribution margin and unit selling price or

(2) Total contribution margin and total sales.

If unit data are used, the contribution margin percentage is equal to the unit contribution margin divided by the unit sales price:

$$CM\% = \frac{\text{unit contribution margin}}{\text{unit sales price}}$$

$$CM\% = \frac{(p - b)}{p}$$

If total sales and variable costs are used, the contribution margin percentage is equal to total contribution margin divided by total sales:

$$CM\% = \frac{\text{Total sales - Total variable costs}}{\text{Total sales}}$$

$$CM\% = \frac{(px - bx)}{px}$$

DICON Furniture Company has a 25 percent contribution margin. Using unit data:

$$CM\% = \frac{(N60 - N45)}{N60} = \frac{N15}{N60} = \underline{\underline{0.25}}$$

Using total data:

$$CM\% = \frac{(N1,200,000 - N900,000)}{N1,200,000} = \frac{N300,000}{N1,200,000} = \underline{\underline{0.25}}$$

From each Naira of sales, 25kobo went to covering fixed costs and to profits. Note that the percentage is the same regardless of whether unit data or total sales and variable costs are used.

Break-even point: The break-even point is the unit or Naira sales volume at which total revenues equal total costs. The break-even unit sales volume can be determined by setting profit equal to zero and solving for X in this equation:

$$(p - b)X_{BE} - a = o$$

$$X_{BE} = \frac{a}{(p - b)}$$

Where

X_{BE} = break-even unit sales volume.

a,b, and p as previously defined.

In words:

$$\text{Break-even unit sales volume} = \frac{\text{Fixed costs}}{\text{unit contribution margin.}}$$

Note the importance of the unit contribution margin. The break-even point is where the total contribution margin of all units produced and sold equals the fixed costs. The break-even unit sales volume tells us the number of unit that are required to cover the fixed costs.

The 1994 break-even unit sales volume for DICON Furniture Company was 20,000 units.

$$X_{BE} = \frac{N300{,}000}{(N60 - N45)} = \frac{N300{,}000}{N15} = 20{,}000 \text{ units}$$

We can determine the break-even Naira sales volume by multiplying the unit selling price by the break-even unit sales volume, $p(X_{BE})$. It can also be determined as the fixed costs divided by the contribution margin percentage.

$$PX_{BE} = \frac{a}{(p-b)/p}$$

In words:

$$\text{Break-even Naira sales volume} = \frac{\text{Fixed Costs}}{\text{Contribution Margin Percentage}}$$

In 1994, N1,200,000 of sales were required for DICON Furniture Company to break -even:

$$PX_{BE} = \frac{N300{,}000}{(N60 - N45)/N60} = \frac{N300{,}000}{0.25} = N1{,}200{,}000$$

Note that with sales of 20,000 units, or N1,200,000, DICON Furniture Company merely broke even in 1994.

Since the contribution margin percentage is the same regardless of whether unit sales price and unit variable costs or total sales and total variable costs are used, the break-even Naira sales volume can be calculated even if per unit data are not available. This becomes important for multiple product firms such as department stores and restaurants. Multiple product firms sell different products with different unit contribution margins. The break-even unit sales volume for multiple product firms is expressed in terms of a mix of products. This unit volume may be difficult to compute if many products are produced and sold. However, we can easily calculate the break-even Naira sale volume using total amounts without having data on individual products of the product mix.

Illustration: Assume that DICON Furniture began producing two additional furniture, a glass furniture and a cane furniture in 1995. Further assume that sales of the standard furniture and total fixed costs of N300,000 remain the same as in 1994. The 1995 sales and variable costs of each model were:

Model	sales	Total variable costs
Standard	N1,200,000	N900,000
Glass	500,000	300,000
Cane	300,000	200,000
	2,000,000	1,400,000

DICON now has a 30 percent contribution margin:

$$CM\% = \frac{N2{,}000{,}000 - N1{,}400{,}000}{N2{,}000{,}00} = \frac{N600{,}000}{N2{,}000{,}00} = \underline{\underline{0.30}}$$

and their break-even sales volume is N1,000,000:

$$PX_{BE} = \frac{N300{,}000}{0.30} = \underline{\underline{N1{,}000{,}000}}$$

Given the total level of fixed costs and the 1995 mix products, sales of at least N1,000,000 are needed to break-even. The 1995 break-even point is lower than the 1994 break-even point of N1,200,000 because the 1995 contribution margin percentage is greater than the 1994 contribution margin percentage (0.30 versus 0.35). The addition of the new models increased DICON overall contribution percentage.

Cost - volume - profit graphs: Cost - volume - profit relationships are frequently presented in a cost - volume - profit graph illustrating revenues, costs and profits or losses at various sales volumes. In a cost-volume-profit graph, the revenue lines has a vertical - axis intercept equal to zero and a slope equal to the unit selling price. The total cost line has a vertical-axis intercept equal to the fixed costs and a slope equal to the unit variable costs. The difference between the slope of the revenue line and the slope of the total cost line is the unit contribution margin.

DICON cost-volume-profit graph for 1994, when only standard furniture were produced and sold, is presented below. As shown, the revenue line intersects the vertical-axis at =N=0 and increases at a rate of N60 per unit. The total cost line intersects the vertical-axis at N300,000 and increases at a rate of N45 per unit. Note that fixed costs are layered on top of variable costs allowing us to see how the total contribution margin, the difference between total revenues and total variable costs goes first to cover fixed costs and then to provide a profit. The break-even point of 20,000 units is the level where the total revenue and total cost lines intersect.

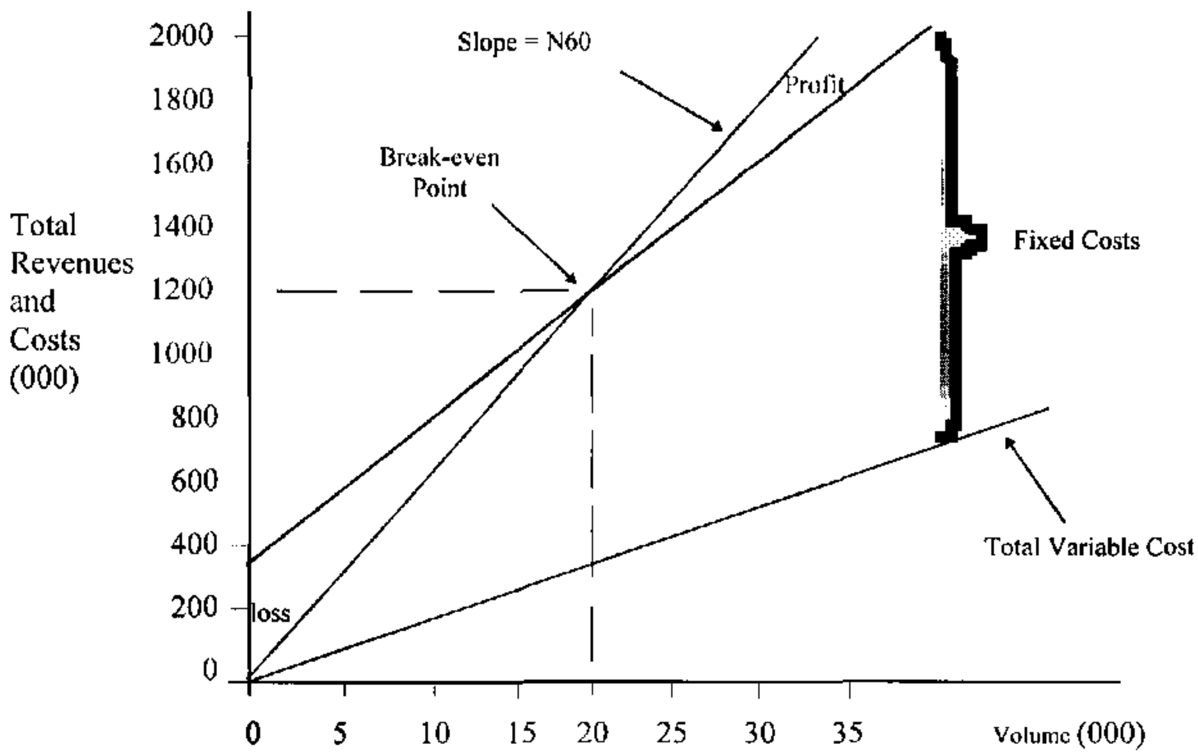

Figure 2.1 Cost-Volume-Profit graph

Another way of showing cost-volume-profit relationships is to layer the variable costs on top of the fixed costs as is shown below for DICON 1994 data. Although the same data as above is used, it does not show the total contribution margin at all volumes. As indicated above, the vertical difference between the total revenue line and the total variable costs line represents the total contribution margin. This information is not readily available as shown below.

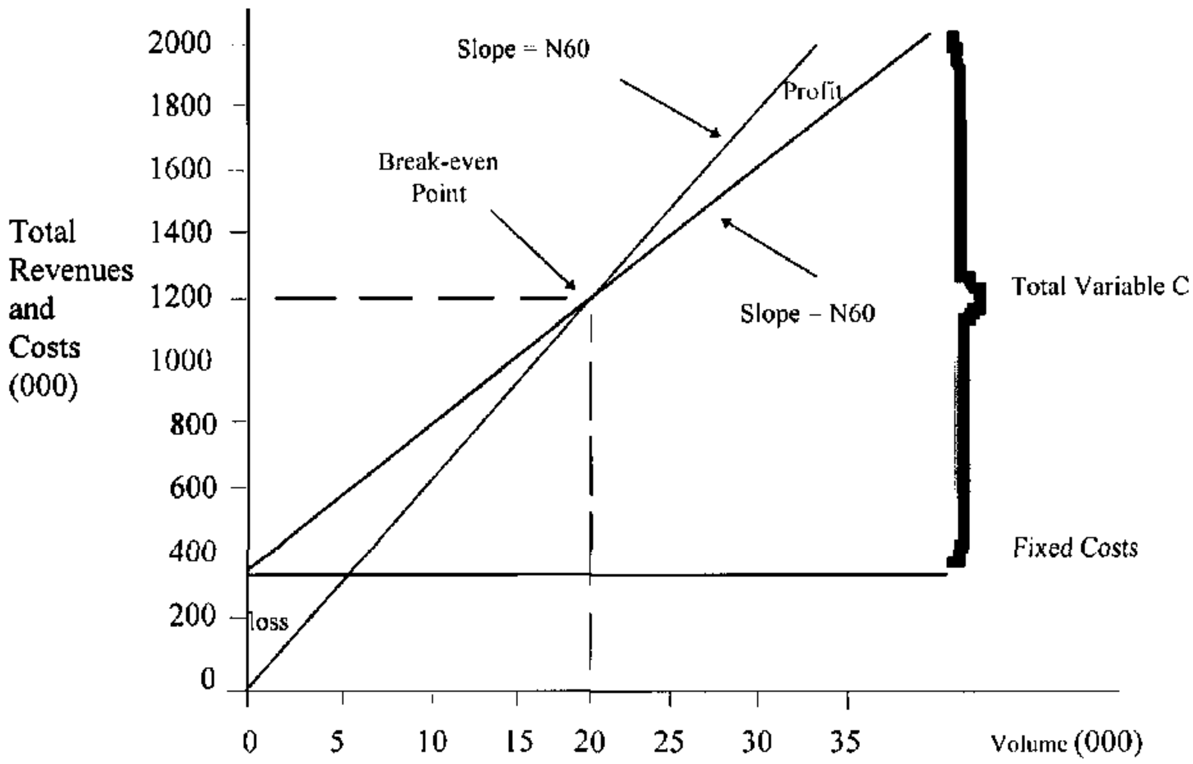

Figure 2.2 Cost-Volume-Profit graph

<u>Margin of safety</u>: The margin of safety is the excess of actual or budgeted sales over break - even sales. The margin of safety can be expressed in units or sales Naira. Management may want to know the margin of safety in actual or planned activity because it indicates the amount by which sales could decrease before losses occur.

As previously illustrated, DICON's 1994 break-even unit sales volume was 20,000 units. Assume DICON's management was contemplating a return to the exclusive production of standard furniture in 1996 with an expected sales volume of 25,000 units. This planned sales volume would provide a margin of safety of 5,000 units or N300,000.

	Units	Sales Naira
Expected sales	25,000	N1,500,000
Break-even sales	20,000	N1,200,000
Margin of safety	5,000	300,000

Profit planning: The unit sales volume that will cover all fixed expenses and provide a desired profit can be determined by setting profit equal to the desired profit and solving for x:

$$\Pi = (p-b)\,x - a$$

$$x = \frac{a+\Pi}{p-b}$$

Where:

x = volume required to earn a profit of II

a,b and p are as previously defined.

In words,

$$\text{Unit sales volume for desired profits} = \frac{\text{Fixed costs + desired profit}}{\text{Unit contribution margin}}$$

The unit sales volume for desired profit tells us the number of unit contributions required to cover the fixed costs and provide the desired profit.

Illustration: DICON's management desires to know the 1996 unit sales volume necessary to earn a profit of N150,000 from the standard model furniture. Recall that fixed costs are N300,000; the unit selling price is N60; and the unit variable costs are N45. The required volume is 30,000 unit:

$$x = \frac{N300{,}000 + N150{,}000}{(N60 - N45)} = \frac{450{,}000}{N15} = \underline{\underline{30{,}000 \text{ unit}}}$$

2.2.6 **Usefulness of C-V-P and conclusion**

The traditional model of C-V-P analysis is useful to management in various ways. It is an area of accounting for management with costs and profit data required for profit planning, policy formulating and pricing decision-making.

Because of their inherent visual advantage, break-even and profit - volume charts are easy for management to understand and use.

The analysis offers management a wide application for testing proposed actions, for considering alternatives, and for deciding the sales volume required to attain a given level of profits. Its formula is useful in projecting the sales volume necessary to realise a given profit or minimize a calculated loss.

Information developed from the traditional model of a C-V-P analysis offers additional useful control data such as the margin of safety figure, which is the excess of the selected sales figure over the sales figure at the break-even point.

However, it is always important that a break-even chart be interpreted in the light of the limitations of its underlying assumptions, especially with respect to the price and sales mix factors.

The analysis is applicable to one product or process at a time (when more than one product or process is involved, a constant product mix is assumed) and consequently, different sets of charts are required for the different products or processes.

The analysis under the traditional model is static, whereas business is dynamic. As a result of this," Hongren (1977) said "the user of C-V-P analysis must constantly challenge and re-examine his assumption in the light of changes in business conditions, prices, cost factors, sales mixes, cost mixes, and the like".

A comparison between the break-even charts of two products (X and Y), showing that product X needs a larger Naira amount of sales or a greater number of units sold to break-even than does product Y should not be taken as a conclusive evidence of product Y's higher profitability than product X's.

A knowledge of the expected number of units that can be sold of each product and the contribution margin are needed in order to determine the expected level of profitability of each.

2.3 <u>Budgeting and budgetary control</u>

Brown and Harward (1975) defined budget as "a pre-determined statement of management policy during a given period which provides a standard for comparison with the results actually achieved "And the good definition of a budget given by Hongren, (1975)in his book "Accounting for management and control", is that a budget is a formal quantitative expression of management plans. Time is a fundamental factor in any budget hence Harper (1969) has defined a budget as a" cost plan relating to a period of time".

A budget which is a plan or target in quantities and/or money values prepared for a future period of time, attempts to "look over the hill "into the future to plan (i) where the business wants to be in a future period of time and (ii) how it intends to get there.

Budgets and budgetary control help to provide information for:

(a) Planning (b) Control

(c) Decision Making

They are rarely 100 percent but if business management attempts to budget for the future they are looking at tomorrow's business world and are forced to think about tomorrow, plan for tomorrow and thus see some of tomorrow's opportunities.

The system should be designed to meet the needs of the business and not try to fit the business into some preconceived system.

It is essential that budgeted targets can be only attained with effortso that motivation becomes part of the budgeting process.

Easily achieved targets become meaningless exercises and the system is sometimes treated with scorn and loses its effectiveness, while impossible targets can cause people to give up before the budgeting system really gets started. It is thus essential that the setting of targets be thoroughly thought through by the person or persons responsible, as the system can be a non-starter because of a slip-shod approach to budgeted targets.

If the budgeting system is to be meaningful and effective it is necessary:

(1) To create budgets which are realistic and can be achieved with some effort.

(2) To measure actual performance as and when it occurs

(3) To compare actual performance against budget and spotlight adverse performances.

(4) To take management action on those adverse performances which can be controlled.

It is important that the manpower required to operate the system is adequate and it is normally better for a very small business to have only one or two easy to operate budgets rather than several budgets.

2.3.1 **Budgeting for who?**

All human aspects need budgeting and essential controls. As we go about the business of living, we are surrounded by organisations. We have jumbo ones, mini types, formal and informal ones, groups that are primarily economic in nature, religious, military, governmental, education, social, or political. These multiple human institutions need to be budgeted for. The budgets could be ones that cover a short period of time or they could be very long term plans. All these are designed to achieve specific objectives. In the case of a company a form of economic forecast is paramount to estimate the general trend of business tempo within the industry. This forecast becomes the basis for establishing single-use operating plans or budgets to be used to guide production, personnel, cost, profit, cash flow, etc. They must be co-ordinated and properly synchronised if the organisational effort is to be a united one. It should be clear that objective plays a dominant role and a unifying one for that matter, if the goals of the organisation are to be achieved.

In the case of a government a budget will equally provide for the general welfare of its citizens.

They need clothing, food, shelter, education, infrastructures, health, defence and various other things that make life complete. Human lives cannot be left to the conflicting variables or the stresses and strains of our modern economic systems. Human being are not chairs, stones, stables; they have hopes and aspirations. This therefore calls for some control or grass root planning which are drawn up in efficiently pre-determined network plans. Such plans ensure availability of regular food supplies to the cities, constant flow of water from the pipe holes and steady electricity supply from the power stations.

2.3.2 <u>Preparing the budget - how ?</u>

A budget is an important aspect of a company's life. At the national level the important cannot be over-stressed. It is one thing to prepare a budget at all but it is another to prepare a workable one; one that could best serve the company in general or the national at large, not a selected privileged few. In preparing a company's budget the opinion of functional managers cannot be side tracked. Production executive can best give information on output and cost, and sales managers and sales men can gather invaluable records from their dealings with the public who purchase the company's services or manufactures. The Accountant can best give the information about the sources of finance after due consideration of alternatives such as decision on leasing or outright purchases. At the national level too, short services of university professors/professionals could be hired or enlisted in the preparation of national budgets. Since the budget will affect both top and lower management alike there is therefore the need for a type of grass root planning process whereby the senior executives or super executives first collect information from below to be delivered to the central planning committee. The times are past, infact, gone, when a single manager should plan for the welfare of any organisation alone. Two heads are better than one and where many people are involved in a planning process they are surely going to think differently - otherwise they could hardly be said to be thinking at all. These multi thinking has the effect of bringing new values, new orientations and a synthesised form of group goal. A budget, therefore must be prepared by a committee in the case of a company or a selected group of experts in the case of a national level plan. For a budget to work well, therefore the estimates submitted to the committee must be real and not faked-up and that they are in consonance with the company's wide objective. Thus the real values of participation at all management levels apart from better planning are the psychological values that accrue as the result of participation.

2.3.3 Preparing the budget - when ?

There is no fast and hard rule about the period when a budget should be prepared. Expenditures fall into various categories - some are capital in nature while others are recurrent. A capital expenditure requires long term planning, balancing against alternatives and choice. This therefore requires careful and protracted planning. Such expenditures command billion Naira and therefore need distant planning. In the case of recurrent, revenue or out-of-pocket expenditures, of which life spans are very short and intermittent, they could be planned more regularly so as not to over-shoot the target plan. There are so many variations in business cycles, and as such, plans often go wrong if the timing are excessively long or short. Planners are therefore advised to use the best of judgement and to consider the cyclical trend of the economy in fixing their plans. In general therefore, one is tempted to say that short term plans are better than long term plans but this qualification could still be wrong because of the unstableness of our modern economic world plagued with economic inflationary spirals.

2.3.4 Budgeting - why ?

Budgeting are excellent tools for both planning and control. They are social accounting norms which can be translated both qualitatively and quantitatively into roles, values and responsibility performances. Psychologists hate to explain question of "why" but even then there is no justification for putting off or postponing the study of a problem and since the affairs of men rest still uncertain there is good intelligence in reasoning with the worst that may befall.

Budgeting therefore, are plans instituted to help control uncertainties in human institutions.

2.3.5 Kinds of budgets

A company's budget could safely be divided into the following headlines.

These are by no means exhaustive but could include:

1. Sales budget
2. Production budget
3. Production cost budget
4. Plant utilisation budget
5. Capital Expenditure budget
6. Selling and distribution budget
7. Purchasing budget
8. Cash budget
9. Profit and loss budget
10. Balance sheet budget, etc

In the case of a nation, they could be all or more of the following:

1. Educational budget
2. Health budget
3. Defence budget
4. Infrastructure budget
5. Agricultural budget, etc.

In particular, budgets are a tool for controlling both the use of the company's or national funds and its individual managers or super executives.

In the case of a company it is not clear what budget to prepare first sales or production. Essentially, cash budget should be the central core of any budgeting exercise since nothing can be done without cash.

Availability of cash as desired is what gives the company or nation command over all the other terms of budget. But in securing cash, sales must be made. But before sales are made constraint is usually existent by way of production capacity. If a company intends a big sales after a thorough market research it may not be able to achieve this because production plans have to be executed from receipts from sales. For production in particular managers' services have to be hired, materials purchased, labour have to be recruited, equipment have to be bought and so many other exercises have to be performed and all there siphon the company's resources.

Budgeting is tiring exercise indeed but human beings do not have to resign their responsibilities in the face of problems. To forecast sales is not an easy task. Companies often get defected by their inability to make accurate forecasts. Essentially, forecasting is a hypothesis and its importance is only when it explains much by little. In forecasting it is important to ask at the onset whether there are any feature of form or structure which most organisation have in common. We find that such actually exist and that it is safer to construct a general model of an organisational budget which embodies in some what "abstract" form the essential feature of all organisations.

In constructing a sales budget therefore, the actions of customers should be properly viewed since they are sometimes irrational and over them the company has no grip or control in a competitive economy. Really, this seems a problem but the use of extrapolations, economic and marketing research techniques, sales could be correctly forged. By extrapolation mean the projection of past trend by way of added percentages to past results and by economic forecast of mean a diligent study of the business cycles taking into accounts population changes, income changes, taste and competitive struggles between manufacturers. Market research itself involves the attempt to finding new market for an ending and lasting industrial trend.

For cash budget adequate plans should be made to secure the company the desired funds. This deals with the time lag in receipts and payments of expenditures, securing loans when company funds are dried up and investing in profitable securities when surpluses exist in the company.

This also includes the planning for capital expenditure and the weighting of various capital projects against their alternatives for purpose of profitability.

In the case of a nation budget cash too is the nerve center and could constitute a big constraint in the case of poor countries.

Usually, government plans by first deciding on all the projects it has to execute for the planned period and after this the sources of revenue are sought. This could be through revenue from natural resources generated internally, or from foreign aid by richer countries or it could be through taxation and the like, such as gifts, donations, etc. It is quite painful that here in Nigeria the cart is always put before the horse and hence our citizens pay various forms of taxes to generate revenue for the government. Here our sources of revenue are balanced against expenditure and the government generally makes profit on its own citizens - a very abnormal planning process, and this indeed gives room to greater degree of inequality and the persistence of poverty disease and ignorance.

2.3.6 Budgetary control

Brown and Harward (1975) said "Budgetary control is a system of controlling costs which includes the preparation of budgets, co-ordinating of the departments and establishing responsibilities, comparing actual performances with that budgeted and acting upon results to achieve maximum profitability"· There are certain established principles of budgetary control and these can be outlined as follows:

1. Establish a plan or target of performance which co-ordinates all the activities of the business.
2. Record the actual performance.
3. Compare the actual performance with that planned.
4. Calculate the differences, or variances, and analyse the reasons for them.
5. Act immediately if necessary to remedy the situation.

It may also be necessary to state that there should be an efficient organisation if budgetary control is to be operated effectively since budgetary control is not an accounting exercise but a tool of management at all levels. Thus, although financially oriented, it requires full recognition to be given to the fact that participation by directors and managers is essential. It therefore, follows that pre-determination is a cardinal feature, co-ordination is essential and the monitoring of results indispensable. Pre-planning is a cardinal feature of budgetary control and in many organisations, the overall plan is represented by the master budget.

Each segment of the master budget is covered by a functional budget.

There is therefore, a series of budgets all co-ordinated together into a plan of action. Behind each budget are the actions of people, their performances and the costs they incur. All are measured in financial terms, but the physical efforts and quantities involved should not be overlooked.

Great care has to be taken to ensure that all budgets are co-ordinated. This may be quite a difficult matter. The aim of doing this is to achieve optimum profitability. Unfortunately, it is not always easy to achieve, profit earning being determined by a number of factors such as prices, and costs. Restrictions imposed on demand, on the volume of production or on any other aspect which affects profit maximisation are known as "limiting factors". Unless due attention is paid to any limiting factors which may be present, the necessary co-ordination will not be achieved.

Control follows planning and co-ordination. Deviations from the pre-determined plans are brought to light by comparing actual and budgeted performances and costs. Subsequently, the differences between the actual and the budgeted figures (the variances) are analysed. Great emphasis should be placed on the location of responsibilities. Recognition that performances and costs can be traced to employed - Managers, Supervisors, and Workers - is an integral part of budgetary control. There should be a clear distinction between "Controllable and "Uncontrollable" costs so as to be able to trace responsibilities.

Budgets are concerned with people, in that they delegate responsibilities to one person, whether he is head of a government department, a company or a small budget centre. A budget is a means to an end and not an end in itself. It covers the area of responsibility of one specified person, so that his performance can be measured at the end of a budget period. It follows therefore, that the budget should be prepared in conjunction with those who are to be responsible for achieving the budget performance. In this way a head of department knows his goal, which tends to induce precision and confidence. This technique due to its stress on personal responsibility, differs from standard costing.

Argyris (1968) noted that "The necessity for constantly increasing efficiency is a basic fact of business life. Budgets are utilized as a pressure device for that purpose. But because of the effect of budgets on people, they tend to generate forces which in the long run decrease efficiency"

Many organisations make capital budgeting decisions. Such decisions may include any or all of the following lines of action - should an equipment be replaced ? should a product line be added ? should a component be made or bought? and should the component be leased or bought ? The list of such decisions is in no way exhaustive. In making such decisions, the analyst should consider only the relevant costs or relevant information which will differ among alternatives. Historical, or past data have no direct effect on the decision, but may only be helpful in the formulation of predictions. The accountant's role in problem solving decision as in the above is primarily that of a technical expert on cost analysis. His responsibility is to be certain that the manager, hence the chief executive is guided by relevant data, information that will lead him to the best decision. Thus, bringing in the irrelevant information will blur the whole picture and make it look like a mass of rumbled data. In using the relevant cost approach, the contribution made by each data or information should be the guiding principle. Where any particular data does not change with changes in alternative lines of action, then it is not a relevant information. Also, qualitative and quantitative factors should be considered in making such problem solving decisions Quantitative factors can be more easily reduced to Naira and kobo such as future costs of alternative materials, or direct Labour. The qualitative factors cannot be easily be reduced to Naira and Kobo, and an example is the opposition of a trade union to a labour saving device.

Today many companies are in a serious profit squeeze. Budgetary control reduces cost, eliminates waste and increases productivity.

Budgets as evaluation instrument of the conduct of people are often attacked because it gives room for punishment, success and rewards. They are a form of pressure devices to get the best out of human beings who are by nature lazy. Once a budget has been set, a standard must be equally put up so as to measure variances.

Variances or deviations from plans afford management an effective grip on the company's operation since it is always better to manage by variances than devoting total efforts to the entire plan. Exceptions from plans afford management the ability to take quick and determined step for rectifying errors.

Comparison of performance against budget is therefore one of the best methods of determining whether or not the company is spending more or less than it had planned to and of tracing the reasons for "overages" and "underages" and making any correction necessary.

The value of the budget as a control factor depends to a large extent on how quickly actual expenditure can be reported to those responsible for them and on the break down within the subject. If the manager sends the figure several weeks after the money has been spent, there is little or nothing he can do about an overrun. Over spending or under-spending are dangerous and should be queried since they make plans falter.

In general, therefore, a good network plan must be set up to control budgets. A net work plan consists of arrows and circles.

The arrows denote activities, that is job to be done, involving the expenditure of resources and time. They link together the circles which represent events, which are distinct stages in the development of the project. Network planning therefore afford good control over projects and prevents pitfalls to a reasonable degree if well exercised. For instance, a plan could be set out in such a way, say, in the construction of a bridge as follows:

TIME IN WEEKS	EVENTS
Week 1	Drawing the plan
Week 2	Visit bridge site and determine volume water at bloom.
Week 3	Laying the foundation
Week 4	Building the walls
Week 5	Casting the concrete
Week 6	Opening the bridge to traffic use.

In all these events so many activities could take place in between like the purchase of materials such as rods, cement, planks or the hire of labour. For instance when the bridge is to be roofed so much work could be involved because it is at this stage that the head beams have to be fixed and this requires the work of other professional of the materials used to see whether they agree generally with tolerance requirements etc.

We have now seen what a budget is, how it is prepared, executed and controlled. But why does it go astray ? A budget is like a drama. All participants must act in concert. The refusal to act as pre-determined lead to budget failures.

2.3.7 Why budgets go wrong

Budgets as I have said are tools for controlling both the use of the company's Naira or the nation's income. But it is no secret that, in practice, they seldom accomplish either of these objectives. Infact, far from attaining these aids they all too often degenerate into ends in themselves, with the results that may well be the direct opposite of what the budgeting process was intended to achieve.

Almost invariably, the fault lies in higher management's failure to recognise the human relations problems inherent in this as in any other control function. Controls, obviously are necessary; but they must not be used as pressure device because they are sure to be resisted by employees since they are not stones, sticks or houses; they have hopes, aspirations and family back grounds. Employees believe that pressures from above are ingenuous devices to deny them their fundamental human freedom. It should be noted that a man as a pleasure seeking animal, gregarious in nature, may agree to mix but could resist every move to loose his self identity. This self "ego" is an important aspect of modern human relations in industry or government. This very aspect leads to budget defeats and this explains the thought without action by top management and the action without thought by lower management. They lead to grudging acceptance and deterioration in human relations.

Budgets go wrong too due to the way they are prepared. A house cannot stand on a faulty foundation; it will crumble. When a budget is based on historical past, pasts that are gone and sunk, such plans must crumble in the light of present circumstances. It is true that experiences are useful but when the weak fibres of old experiences are used in constructing new "citadels" and when they are so near the flames of past ruins they must themselves give way and lead to disaster and ruins.

Also the budget in the final stage may be the result, not of examination of the probable effect in the light of pure reason but on faith and a good deal of negotiation and self protective manoeuvre among the super executives involved.

It is a general practice too that some senior executives use under-spending in one year as justifications for cutting budgets in the next year which leads to lower management's increased spending ability.

Also budgets go wrong because where only top managers have to take the decisions lower managers may refuse to co-operate since they have a say in what may eventually affect them adversely or otherwise.

Some times too, top managers mask the tool of control and it results in communication blocks to lower managers and less effective "feed backs". Some times too, top managers may punish lower managers for overspending and this results in such devices as the creation of contingencies which inflate total budget figures and their concomitant evil effects.

In companies as well as governments, corruption is a vice. It is now an established practice that people steal money allocated for budgets. Apart from this, where a contractor has to bribe even he government or company before he wins a contract for work and having regards he too has to make his own profit, it should not be surprising to find bad quality jobs which are aspects of failures in budgeting.

There is some times what we call control pressure from top management and inflexibility of lower management to control which lead to collapse of administrative procedures. To resolve this control - inflexibility handicapped lower managers must be allowed to participate in the planning process since they do not have to be directed towards a common purpose if they have had the chance to write them. Instead of engaging in a running battle over externally imposed limits, top and lower management can search for other means of control useful to both.

In conclusion, we must accept that an aspect of budgeting and budgetary control is a series of network plan which must be designed to translate a company's or a government's intention into a series of assignment which provide the money to carry them out. Since budgets extend over a period of time it must be normally designed to represent a flow of assignment rather than a stationary exercise. Organisers of budgets should aim at what budgets will do for the many that the budget is being made and not for the few who organise the budget. As budgets are responsibility assignments they must be executed on a standard that conform with social norms.

2.4 Controlling

Top management set their company objectives and must see that plans are executed and that such plans are followed up with an appraisal of how actual performance have conformed to plans.

Thus, controlling (involving) action and evaluation) means the implementation of plans and the use of feed - backs so that objectives are optimally obtained. But accounting formalises control as performance reports which compare results with plans and which spotlight deviations (i.e. exceptions).

In controlling therefore, the chief executives visualization of cost behavioural patterns, the influences of quantitative techniques on management accounting, his perception of attention directing through reports or feed - backs and the significance of deviations, affect materially the control function of management accounting. Moreover, do the chief executives have regard to obtaining optimal results through motivation?

CHAPTER THREE

RESEARCH METHODOLOGY

3.1 Introduction

This study is to determine chief executives perception of accounting for management control in government ministries and parastatals in Kaduna state.

In undertaking this study a random sample of 50 government establishments were selected from government ministries and parastatals in Kaduna. In order to obtain the views of the chief executives of accounting for management control questionnaires were sent to each of the 50 establishments. Hence the data for this study were obtained mainly by means of a questionnaire.[5] The items included in the questionnaire were randomly arranged but are presented below according to four general categories or classifications:-

1. General
2. Planning
3. Budgeting
4. Controlling.

The respondents were provided with the following instructions: "checkmarks may be used to answer the following questions about your perception of accounting for management control.
Feel free to make additional comments on your answers to any or all questions".

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[5] *The Questionnaire used in the survey was adapted from a format used by Porter to measure the perceived deficiencies in the need fulfilment of managers. see Lyman W Porter: "A study of Perceived Need Satisfaction in Bottom and middle management jobs" Journal of Applied Psychology vol. 45,1961 PP1-10 .*

3.2 Sources of data

This study aims to draw its data from both primary and secondary sources.

3.2.1 Primary data

Primary data were collected from both chief executives and from other personnel of the selected government establishments in Kaduna.

3.2.2 Secondary data

The secondary data were collected from both state and federal budget offices. Others include, the financial Guardian newspaper, the Business Times.

3.3 Method of data collection

The methods adopted in collecting data for this research were as follows:

3.3.1 Personal interview

Personal interviews were held with chief executives and other key staff of ministries and parastatals based on the questionnaire in Appendix I. The interviews were largely structured.

3.3.2 **Questionnaire**

The data for this study were obtained by means of a questionnaire. The items included in the questionnaire were randomly arranged to cover:

1. General
2. Planning
3. Budgeting
4. Controlling.

This questionnaire covered twenty five issues, the answers to which we considered essential to this study.

3.4 **Summary**

Chapter three deals with the types and sources of data, as well as the methods of data collection. Two types of data the primary and secondary data] are involved in this project. whereas the secondary data were sourced from state and federal annual budgets the primary data were got through a combination of a questionnaire and from a largely structured personal interview.

CHAPTER FOUR

DATA PRESENTATION AND ANALYSIS

4.1 Introduction

In this chapter, we shall discuss the chief executives perception of accounting for management control in the broad areas of planning, controlling and budgeting. This is to be done through the interpretation of answers obtained from questionnaires distributed to a sample of chief executives of government ministries and parastatals in Kaduna State. We shall then be in a position to say how much impact this important and interesting field of study has made so far on our chief executives.

In order to determine the chief executive's perception of accounting for management control, a random sample of 50 organisations were selected from Kaduna State. In order to obtain the views of the chief executive of accounting for management control, questionnaires were sent to each of the 50 organisations. Of the 50 individuals thus selected, a total of 19 usable responses were received for a response rate of 38%.

4.2 General

It is well established that accounting information should be the most important tool in any management set up. Attempt was therefore made to find out whether our respondents have this view. A 100% positive reply was got. And this was expected because it would have been a contradiction in terms for somebody who professes to be applying accounting for management control to disregard accounting information for that purpose.

Again, although management use of accounting information is not new - some of the techniques of accounting for management control have been used for many decades, yet up to 32% of chief executives replied in the questionnaires that they have not heard of accounting for management control before. The same percentage also agreed that they do not have accounting for management control set up in their organisations. However, this is not unexpected in view of the developing nature of our economy.

The lukewarm attitude in the setting up of accounting for management control models may also be attributed to the dearth of knowledgeable people in the field. This view is given credence by the response of 68% of the chief executives of the 19 organisations surveyed.

It is also to note that about 89.5% of the chief executives agreed that they are aware of the existence in Nigeria of professional accounting bodies. But a follow - up question asking them to name the bodies revealed that up to 38% of the chief executives could not give the correct answer. Ridiculously a good number of the chief executives mentioned their external auditors like Akintola Williams, Peat Marwick etc.

4.3 Planning

In designing an environment for the effective performance of individuals working together in groups, the most essential task is to see that purposes and objectives, and methods of attaining them, are clearly understood. If group effort is to be effective, people must know what they are expected to accomplish and how it can be done.

It is an indubitable fact that the exact future can seldom be predicted and factors beyond control may interfere with the best-laid plans, unless there is planning, events are left to chance.

From the replies got from the establishments surveyed, 100% of the chief executives are seriously aware of the importance of planning. This is very encouraging especially now that we are in an economic, technological, social and political era in which planning has become requisite for organisational survival.

4.3.1 The selection of objectives

The purpose of every plan and all derivative plans is to facilitate the accomplishment of enterprise purpose and objectives. They can guide both the day-to-day activities and the personal development of individuals in an organisation. "We plan to achieve objectives and our objectives are clearly selected" said one chief executive. From the results of the survey, 100% of the chief executives have clearly selected objectives. This is not surprising, for without clear objectives managing is haphazard and random, and no individual, no group can expect to perform effectively or efficiently unless a clear goal is sought. One author, Huse, made one important point that "people who do not have a good idea of where they are going will not know when they get there and would not be able to plan efficiently to get there".

Put succinctly, good management requires clear organisational objectives.

It is pertinent to mention here that for objectives to be meaningful they must be verifiable. The easiest way to get verifiability is to put goals in quantifiable terms.

It was observed from the survey that 84% of the chief executives affirmed that objectives set are quantifiable.

A response from one of the government establishments randomly selected for this survey opined that objectives are not quantifiable as far as his organisation is concerned. One is inclined to believe him since his objective is not profit making. It may be difficult if not impossible to quantify the amount of social services rendered to the public.

But who are involved in the selection of objectives? In a reply to the questionnaire, 63% of the respondents indicated the involvement of top cadre workers while 37% indicated otherwise ie either involving middle level and lower cadre workers , or all cadres. The question aimed at finding the responsibility for the selection of overall objectives of the organisation.

The conclusion that can be drawn from this survey is that some organisations still fail to realise that the selection of overall organisational objectives rests with the top cadre workers while the middle and lower cadre workers should be concerned with the sub-units of objectives which put together make up the overall objectives. The concern of top management should be to select these objectives, sell them to middle and lower cadre workers in such a way as to attain goal congruence optimally.

4.3.2 Application of cost volume analysis in decision making

If we make the assumption that organisational objectives are towards profit maximisation then attention must be paid to the monitoring and understanding of the relationship between these elements that go to make up profit, namely: costs and revenues at different levels of production. In our attempt to find the chief executives perception in this area of accounting for management control 74% of our respondents appreciated the importance of predetermining activity or volume where their organisation makes neither profits nor losses.

Predetermination of activity levels is planning because the levels need planning to work out, while they are also looked upon as objectives as far as the period is concerned.

As a follow-up we wanted to know which method the establishments were using: 68% were either using the Break-even analysis or the profit volume-chart while 32% either were not using them or indicated their application of guess work . We then concluded that a good attempt is being made by the chief executives in this aspect of accounting for management control.

It is however, important to note here that the cost volume profit analysis can be a most useful tool for management. Impacts on profits of changes in the volume of sales or costs can enable management to take decisions on pricing, production levels, cost control and so forth.

4.3.3 Budgeting and budgetary control

A budget is a predetermined statement of management policy during a given period which provides a standard for comparison with the results actually achieved.

There are many quantifiable and unquantifiable benefits which arise from budgeting.

In the survey carried out it was happily noted that some form of budgeting is carried on in all the establishments that were interviewed. They answered in the affirmative to the question "do you endeavour to make your staff affected by the budget accept the notion that the budget is designed to help them and not to hinder them?" The practice by these organisations of making their members of staff to be aware of the nature and advantages of a budget is really commendable. Of even greater importance is the fact that the members of staff contribute in making the budget successful.

However, it was regrettable to note that although all the organisations studied make some form of budgeting most depend on hunches and do not make proper forecasts in order to concretize their figures. Reasons given by these chief executives range from lack of budget experts, high costs associated with budgeting to the uncertainty of the future.

A careful analysis of these reasons shows that actually, they do not fully understand the reasons for budgeting, they still have hazy ideas about reasons for budgeting.

Budget experts are not a pre-requisite for budgeting and in any case, not every organisation can afford to have budget experts. It is worthy to note that budgeting can be done in any organisation no matter the size and since the smaller establishments may not afford to have budget experts who should prepare elaborate estimates, they can settle for very simple budgets. Some chief executives do not yet understand that the benefits from budgets far out weigh their costs.

They do not yet realize that budgeting is designed to eliminate the future uncertainties associated with business transactions. It is unfortunate to note that only 25% of the establishments surveyed know the reasons for budgeting, showing that planning occupies the back sit in government establishments.

This also indicates that chief executives of government establishments are not sufficiently knowledgeable in accounting for management control, which should not be the case.

In the course of the survey, the chief executives perception of the effects of budgetary control on the workers was also ascertained.

Regrettably, most of the establishments surveyed never bother to know the feelings of their workers who are appraised based on the budget performance reports. In answer to a question which reads: what do you think are the feelings of these workers by this method of appraisal ? Almost all the chief executives could not answer this question showing that they do not know that the human aspect of budgetary control is of utmost importance.

The necessity for constantly increasing efficiency is a basic fact of business life. Budgets are utilized as a pressure device for that purpose. But because of the effect of budgets on people, they tend to generate forces which in the long run decrease efficiency.

Having analysed the use of budgeting and budgetary control methods in the organisations studied, we feel that in comparison with other developed countries our chief executives in Kaduna may be said to be still uninformed. We feel that the essence of budgeting and budgetary control is not yet understood. In many developed economics of the world, management seminars are organized by the government for the top echelon of the management of many organisations. Recently, the practice was introduced in Nigeria and is very commendable because the actions or decisions of these chief executives affect not only their particular organisations, but the macro-economy in general. For example, the best decision may be to lease an equipment so as to reap the benefits of flexibility in financing, avoid the risk of obsolescence of the equipment and may be take advantage of tax savings from rental payments which are deductible expenses. But because the chief executives is uninformed, he may take the decision to buy the equipment from say Canada. The country's balance of payment position is affected by many of such decisions and later the chief executive may notice that instead of a decrease in costs earlier anticipated, there is an increase in costs and also the equipment becomes obsolete soon after purchase.

In the meantime, the bank which gave the loan for the loan for the purchase. In the meantime, the bank which gave the loan for the purchase presses for the repayment of the loan which is not forthcoming. All these may result in the eventual winding up of the company with its accompanying effects on the society and the country in general.

It would also be recommended that radio and television programmes include some management accounting topics such as budgeting, budgeting control and the like. This will go a long way to solving some of these problems of ignorance exhibited by some of the chief executives.

4.4 <u>Controlling</u>

Top management set their company objectives and must see that plans are executed and that such plans are followed up with an appraisal of how actual performance have conformed to plans. Thus, controlling (involving action and evaluation) means the implementation of plans and the use of feed-backs so that objectives are optimally obtained.

4.4.1 <u>Cost behaviour patterns</u>

In investigating chief executives perception of the relationship between total costs and volume of business activity attention was directed on cost behaviour patterns. The question is, are chief executives aware that certain costs remain fixed while others change as activity levels are altered ? If chief executives perceive of this cost behavioural pattern then they can better make predictions and evaluations as accurately as is feasible.

Our survey showed that out of the nineteen chief executives eight are aware of the fixity or variability of costs. However, eleven chief executives, while subscribing to the fixity of certain costs could not say for sure whether some or all costs will increase with increase in activity. Probably they have the correct opinion that the distinction between fixed and variable cost are valid only in the short run and within relevant range. All costs are variable in the long-run.

"A fixed cost is fixed only in relationship to a given period of time - the budget period - and a given, though wide, range of activity called the relevant range." [6]

Thus, it is encouraging that at least some chief executives know their costs and how such costs behave. It is hoped therefore, that with this perception and with the use of such tools of cost-profit-volume relationship, the chief executives will better direct managerial attention to controllable areas. But it is regrettable that majority of the chief executives are least cost conscious. The cause may be that they are not motivated to make profit. If they were, then they should have sought operation at the minimum possible cost.

4.4.2 Management accounting and quantitative techniques

Most of the information needed to control activities are quantifiable. Our survey revealed that of the chief executives questioned only 15% would, in controlling the business rely on the quantitative and statistical data supplied by the management accountant.

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[6] *Hongren, C.T. (1975)* *Accounting for Management Control*. *Prentice-Hall inter. London,P.217*

We are therefore of the opinion that the chief executives selected at random do not fall back on the management accountant for information, and as such unaware of the controllership function of the management accountant in planning for control, reporting and interpreting and evaluating and consulting.

4.4.3 Timing of feed-backs

Management accounting provides, among other information, attention directing information. That take the form of reports and the interpretation of information that help managers to focus on operating problems, imperfections and inefficiencies promptly. Attention directing concerns feedbacks which are commonly associated with current planning and control as well as assisting in the analysis and investigations of current operations.

The question was, do you (as chief executives) have ways of getting feed-back from current operations ? The survey showed that all the nineteen the importance of feed backs and have ways of getting them. But although such feed back should be normally got during the course of operations so that current activities could be geared to pre-determined goals, not all chief executives are of the view that feed backs be better received during operations. Only four out of the nineteen chief executives followed the course of obtaining feed backs during operations. All the other chiefs get feed backs either after the operations, or before or a combination of before, during and after operations. Such a perception is bound to create problems. It is a clear indication that not much use is made of the ready information that should normally by supplied by the management accounting function. As such, early deviations which should have been corrected are neglected. Also it tells that most chief executives concern themselves with past costs. Past costs are down the drain as nothing can be done about them. But with feed backs during the course of operations current costs can be reduced through current planning and control.

4.4.4 Variance analysis

In further probing the chief executives perception of operations control through variance analysis, which presupposes the existence of predetermined standards, our mind was directed also to the possibility of "management by exception" through analysis of variances. Such questions touching on the comparison of actual with budgeted plans, the reconciliation of deviations and the concentration on significant deviations were raised. My survey revealed that at times, but not always, the chief executives perceive that actual performance may deviate from standard.

On the possibility of "management by exception" whereby the executives' attention and effort are concentrated on the significant deviations from expected results, all chief executives agree and would advocate the practice of the principle of management by exception.

On whether deviations call for the evaluation of the whole plan, 63% of the executives would not subscribe to necessity for overhauling the whole plan simply because of a deviation. such is the right perception since only very significant and very adverse deviations should call for total review. It could be that standards have been wrongly set ab initio.

However, 37% of the chief executives did not have this perception. Probably, they are overly concerned about all deviations. But management should not ordinarily be concerned with results that conform closely to plans.

4.4.5 <u>Achieving objectives through goal congruence</u>

The setting of company goals and objectives means that efforts both human and material must be geared toward achieving the objectives. But in the over all problem of management control and the design of control systems, do chief executives perceive the behavioural factors of managers? That is, do they consider it necessary to involve managers in finding means for achieving desired goals ? Hence, does the system specify goals and sub-goals which encourage behaviour that blends with top-management goals ? Are the goals as specified by top-management and through the system accepted by managers as their personal goals ?

In this aspect of goal setting and controls, all the chief executives interviewed subscribed to the motivational aspect of management and control. Again, all the chief executives believe that objectives are subject to review from time to time. This indicates that they (the executives) seek goal congruence whereby goals and sub-goals are specified to induce (or at least not discourage) decisions that will blend with top-management goals.

CHAPTER FIVE

SUMMARY, CONCLUSION AND RECOMMENDATIONS

5.1 Summary

This study has been to highlight the causes of financial indiscipline in our government ministries and parastatals. The attendant repercussions of deficit spending, profligacy and planlessness are so enormous that the issue cannot be treated with levity.

5.2 Conclusion

In concluding this work let us again draw our minds to the National Association of Accountants (1963) who said :

> *A broad new field of accounting has evolved since the beginning of the 20th century. While it had its origin in historical financial accounting and cost accounting, it is designed to provide financial data to guide management actions oriented towards the present and future. It serves management at all levels. The term management accounting describes this field with accuracy and seems to be gaining rapid and widespread acceptance.*

From the survey the chief executives really perceive the importance of management accounting as a guide to managerial actions. They believe that management accounting information is the most important tool in any management set up. In fact all the chief executives do profess to be applying management accounting in making decisions. But while agreeing with the chief executives on the importance of this field of study we are of the opinion that they (the chief executives) are yet to understand in every perspective the great work accounting for management control can do.

No doubt, they apply certain principles of accounting for management control without taking the full benefits derivable. For instance, it is encouraging from the result of the survey that 100% of the chief executives are quite aware of the importance of planning. But one does not have to be a chief executive before one perceives the importance of planning in achieving company goals.

In this connection, despite the chief executives' perception of the planning function of accounting for management control, not all seem to understand and use such accounting for management control tools as the break-even chart, among other tools, for profit planning. Only 74% of the chief executives do use such technique. Again, in budgeting, which by formalizing responsibilities for planning compels managers to think ahead, it is regrettable that the chief executives' ideas are still hazy. Most do not really understand the reason for budgeting. Some are of the opinion that since they would always take advantage of every profitable opportunities available to them, what then is the need for budgeting ? Some who say that they do not have budget experts fail to see that budgeting can be done in any organisation -big or small. Small companies can make do with simple budgets provided it compels managers to think ahead.

In the field of control the chief executives fared relatively well. Reflect on a presidential electioneering campaign.

A presidential aspirant promised his electorate that if voted into power, he would arrest and control inflation within tolerable limits. To ridicule him, his more learned opponent asked him, "How can you control what you don't know either by definition or causation ?" Coming back to our subject matter, the chief executives, generally speaking, know their costs and are aware of how such behave.

By knowing fixed and variable costs, they perceive the controllability and non-controllability of costs. Consequently, if feed backs are properly timed then controllable costs can be controlled. Yet, and alarmingly too, only as few as 32% of the chief executives correctly receive feed backs during operations. Clearly, therefore, such view if taken, means that most excesses in costs are not controlled because feed backs are got after operations. According to Charles T. Hongren, "ALL past costs are down the drain. Nothing can change what has already happened".

5.3 Recommendations of the study

This researcher is fully convinced that government ministries and parastatals are amenable to financial discipline despite their present state of lack of probity and accountability. It is therefore hoped that if the following recommendations are adapted and applied, they could produce results.

1. ***Improved condition of service:*** Government should improve the condition of service in the public sector so as to be able to attract and retain trained professionals.
2. ***Seminars and conferences:*** Lectures and seminars should be organized for the chief executives to better their knowledge on Accounting for management control. The universities, through teaching and research are better placed in this regard.
3. ***Organisational structure:*** The public service should be restructured so as to enhance its internal control system. Presently, the structure tend to give the chief executives blanket authority.

4. ***Budget monitoring committee:*** Both federal and state establishment should set up budgetary monitoring committees to ensure strict compliance with budget proposals.
5. ***Use of experts:*** Financial experts should be employed to draft budgets to achieve realistic estimates.
6. ***Halt to staff exodus:*** The adverse economic condition has resulted to high labour turnover in the public service. The seemingly attractive private sector has attracted high quality staff leaving mediocrity to fashion out policies in the public sector. In this circumstance the internal control system becomes weak and vulnerable to manipulations by the chief executive. To reduce the labour turnover, adequate incentives, comparable to those in the private sector are necessary.

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QUESTIONNAIRE

Checkmarks may be used to answer the following questions about your perception of Accounting for Management Control. Feel free to make additional comments on your answers to any or all questions.

1. Have you heard of Accounting for Management Control ?

   Yes ( )No ( )

2. Accounting for management control:

   a. is not very important in most organisations. ( )
   b. is not important at all in Nigeria. ( )
   c. is not yet understood by many people. ( )
   d. is very important in every organisation. ( )

3. Do you have an accounting for management control set up in your establishment ?

   Yes ( )No ( )

4. Do you think accounting for management control aids you in decision making ?

   Yes ( )No ( )

5. As the Chief Executive, are you involved in the major decision-making processes of the organisation ?

   Yes ( )No ( )

6. Do you think accounting information is necessary as a guide to decision making ?

   Yes ( )No ( )

7. Are there clearly selected objectives in your organisation ?

   Yes ( )No ( )

8. If the answer to the above is yes, are the objectives quantifiable ?

   Yes ( )No ( )

9. Who are involved in selecting these objectives ?

   a. Top cadre workers ( )
   b. Middle cadre workers ( )
   c. Lower cadre workers ( )
   d. All the above ( )

10. How do you view the planning function of your organisation?

   a. Very seriously ( )
   b. Not so serious ( )
   c. Nothing to worry about ( )

11. Do you know that some of the costs you incur in your organisation within a relevant range do not change e.g Rent, Insurance and salaries of key personnel remain the same at various levels of output within that relevant range ?

   Yes ( )No ( )

12. Are there ways of reviewing the objectives set ?

   Yes ( )No ( )

13. Do you have ways of getting feed backs from current operations ?

   Yes ( )No ( )

14. Feedbacks are got

   a. Before operations ( )
   b. During operations ( )
   c. After operations ( )
   d. All the above ( )

15. Does actual performance conform with original plans ?

   a. At times ( )
   b. Always ( )
   c. Not at all ( )

16. Is it wise in your opinion to concentrate on the significant deviation from expected results ?

    Yes ( )No ( )

17. Or does deviation from set objectives in your opinion entail evaluation of the whole plan ?

    Yes ( )No ( )

18. Is there a way of predetermining activity or volume where your organisation makes neither profits nor losses?

    Yes ( )No ( )

19. If yes, which of these do you employ ?

    a. Break-even analysis ( )
    b. Guess work ( )
    c. Profit volume chart ( )

20. Budget is not necessary in my organisation because it is time wasting and puts one in a straight jacket

    Yes ( )No ( )

21. In designing a budget

    a. Only the Chief Executive is involved ( )
    b. It is the business of the Accountant ( )
    c. All heads of departments are involved ( )

22. Monitoring is not necessary in budget

    Yes ( )No ( )

23. In making major decisions on capital expenditure, do you consider these:

    a. Should an equipment be replaced ?
    b. Should a project line be added ?
    c. Should a component part be made or bought ?

    Yes ( )No ( )

24. Do you know of the existence in Nigeria of any recognized professional Accounting bodies ?

    Yes (   )No (   )

25. If yes, name them:

    a. ---

    b. ---

    c. ---

    d. ---