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RESPONSIBILITY ACCOUNTING: AN APPROACH TO COST CONTROL

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ABSTRACT

Responsibility accounting is an approach to cost control whereby every item of expenditure is made the responsibility of that individual who can best influence it by his actions. Responsibility centre is a personalized group of control centre under the control of a responsible individual. Responsibility accounting is a concept aims to help achieve a fit between planning and control systems and managerial responsibilities. It is system of accumulating and reporting both actual and budgeted costs and revenues by individuals responsible for them. In responsibility accounting concept persons are made responsible for the execution of plans and the evaluation of actual performance for determining whether actual operations have gone according to what was planned and if the actuals are not according to plan, what is the extent of deviation, what is the reason for the deviation what action can be taken to bring in the future actions more in line with the plan. However, managers should avoid over emphasizing controllability. Responsibility accounting is more far-reaching. It focuses on information and knowledge, not on control. It helps managers to first focus on whom they should ask to obtain information and not on whom they should blame.

KEY WORD: *Cost Centres, Cost Control, Management by Exception, Management Control System, Responsibility Accounting.*

INTRODUCTION

Responsibility accounting is a system of accounting that segregates revenues and costs into areas of personal responsibility in order to assess the performance attained by persons to whom authority has been assigned. Responsibility accounting is a method of accounting in which costs and revenues are identified with persons assigned to their control rather than with products or functions. It classifies costs and revenues according to the responsibility centres that are responsible for incurring the cost and generating the revenues. Responsibility accounting also classifies the cost assigned to each responsibility centre according to whether they are controllable or non-controllable. Controllable costs are classified by items. The aim is to show up the results of operation by each section or division having control over resources and their use.
Briefly speaking, Responsibility accounting requires that costs be classified:

- By the responsibility centres,
- Within each responsibility centre whether controllable or non-controllable, and within the controllable classification by cost elements in sufficient details to provide useful basis for analysis.

The American Accounting Association has recommended the following:

- ✓ If the person has authority over both the acquisition and the use of the service, he should be charged with the cost of such services.
- ✓ If the person significantly influences the amount of costs through his own action, he may be charged with such costs.
- ✓ Even if the person cannot significantly influence the amount of cost through his own direct action, he may be charged with those elements with which the management desires him to be concerned, so that he will help to influence those who are responsible.

Under the conventional system of cost accounting, overheads accumulated are allocated to different 'cost centres' defined for the purpose. A cost centre, as we know is the organisation's unit in which the individual incharge administers his activities directly. Obviously this definition of cost centres seems necessary from the point of view of cost control and to determine responsibility. Cost allocation at best in loaded with assumption and in many cases highly arbitrary methods of apportionment are employed in practice.

Products is not an appropriate unit for cost control. Through this system an individual in charge of a 'cost centre' is burdened by a large number of overheads over which he has little control. Hence, a system of responsibility accounting is recommended whereby the person controlling on initiating a particular cost should be held responsible for it. The problem becomes particularly acute in the allocation of service department costs, especially where responsibilities overlap. This problem can be circumvented by the use of standard costs. Responsibility accounting follows the basic principles as for any system of cost control like budgets and standard costs, with the difference that it has a bias towards fixation of responsibility of individuals, departments or machines.

BASES OF RESPONSIBILITY ACCOUNTING

The following principles should be considered in implementation of control through responsibility centres:

- The organisation structure must be clearly defined, and responsibility delegated so that each person knows his role.
- The extent and limits of functional control must be determined.
- The responsible individuals should be fully involved in preparing plans if they are to be held responsible for results.
- Responsible individuals must be served with regular performance reports.
- Means must be established to enable plans to be revised in line with actual performance in such a way that responsible individuals are involved.
- Every item should be the responsibility of some individual within the organisation.

Responsibility accounting is based on four basic principles:

Objectives-The overall objectives of the business are divided and subdivided into the objectives of each of its constituent parts, expressed as profit, contribution or cost.

Controllable Costs- Responsibility accounting excludes or segregates costs which are not controlled directly by the manager. For example, in a machine shop the level of waste is directly controllable but the rent is not.

Explanation-The results achieved in a profit centre are not all directly controllable by the profit centre manager. External factors will affect both revenues and expenditures. But responsibility accounting requires managers to explain why the actual results obtained differ from those in the forecast or budget. Even if these are a result of changes in the external environment, managers are still expected to predict and measure the behaviour of relevant parts of that environment and to act appropriately. It is the job of the manager of a responsibility centre to explain outcomes regardless of his or her personal influence over the results.

Management by Exception- The feedback of information on actual revenues and costs to the responsibility centres manager concentrates on the important deviations from the budget. This is the principle of management by exception where by the attention of managers is focussed on exceptions to the norm so that they do not waste time on those parts of the reports that reflect smoothly running phases of operations.

Responsibility Accounting: An Important Component of Management Control System

Responsibility accounting is an important component of management control system. It is an invaluable support to modern management. The more complex and decentralized the operations of an enterprise, the more the significance of responsibility accounting. It contributes to the firm's management by providing relevant information on a continuous basis. Besides being an information system, responsibility accounting, when implemented, accomplishes many other benefits. It necessitates the need of clearly defining and communicating the corporate objectives and individual goals. It compels management to set realistic plans and budgets.

Responsibility accounting facilitates the delegation of decision taking. Responsibility centre managers can be given an appropriate and controlled degree of authority over their units in the knowledge of what they are expected to achieve and what they can do. Exception reporting, built into any fully developed responsibility accounting system, enables manager to concentrate on the key issues which need their attention. It provides as system of closer control. Responsibility accounting measures the performance of individuals in an objective manner. Responsibility accounting provides individual managers with incentive through performance reports, and top management with a quantitative basis for evaluating each manager's performance. It facilitates decentralization of decision making. It fosters a sense of cost consciousness among managers and their subordinates.

Implementation Process

The basic process underlying implementation of responsibility accounting are:

- Responsibility centres within the organisation are identified.
- A plan of objectives is set up in terms of a target, budget, standard or estimate. The plan is broken up for allocation of each responsibility area of centre and is communicated to the concerned level of management.
- For each responsibility centre the extent of responsibility is defined.
- Controllable and non-controllable activities at various levels of responsibility are specified.
- Accounting system accumulate information by area of responsibility is specified.
- Performance reports are prepared to provide information to those who will use them.
- The performance is evaluated i.e., the results of actual operation by each responsibility are ascertained.
- The variances from the plan are analyzed as to fix responsibility on the responsibility area or centre. The variances are reported to higher management.
- Corrective action is taken and communicated to the individual responsible.

In order to implement this system the lines of authority of each manager is clearly defined, with the result that each manager knows exactly what his responsibilities are and precisely what is expected of him, then it is possible to plan and control costs in order that the performance of each individual may be evaluated and improved.

Proper reporting system should be designed to fit into the responsibility accounting concept. The concept suggests that the manager incharge of responsibility centres should receive information relevant to his area of operation and his performance should be judge only by reference to events within his control. Responsibility accounting requires that costs be classified by degree of controllability within the responsibility centre and the nature of costs. For successful implementation of the system the manager incharge of responsibility centre must:

- ✓ Know what is expected of him to achieve,
- ✓ Knows the result of his performance,
- ✓ Be within his power to influence what is happeing

Difficulties in Implementation

The difficulties that may be encountered in introducing responsibility accounting are as follows:

- The management may find it difficult to fix responsibility.
- The traditional way of classification of expenses should be subjected to a further analysis which becomes difficult.
- Certain managers may need additional clarification because of the design of responsibility reports being different from routine reports.

CONCLUSION

Responsibility accounting is a system of accounting that recognizes various responsibility centres throughout the organization and reflects the plans and actions of these centres by assigning particular revenues and costs to the one having he pertinent responsibility. It is a system that generates information on the basis of managerial responsibility, allowing that information to be used directly in motivating and controlling each manager's actions. Responsibility accounting is specially designed according to the organization structure and no tailor-made system could be recommended for an individual firm. It is introduced. One of the difficult tasks is the assignment of responsibility for each activity and for each corresponding item of expense, income, capital expenditure and asst investment. It establishing responsibility accounting system, the management should decide on certain guidelines for assigning costs to individuals for reporting.

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