Indicators of Assessing the Effectiveness of the Accounting Information System for Business Organizations

by

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Abstract

The development that occurred in the activities of business organizations recently and continuous complexity facing these organizations, led to appeared a set of challenges for these organizations, the most important of which is the testing of ability for these companies to formulating and building an effective and useful accounting information system in a manner that keep pace with the developments and meets the requirements of parties that depend on the outputs of this system. In fact, it cannot say that, all accounting information systems are considered as successful systems and achieve the goals required of it due to many problems that located within the structure of this system and the accounting staff who responsible for operating this system. In the context of this problem, the study seeks to clarify the most important duties and tasks of the distinguished system and the indicators through which it can judge the level of success of that system in the expected range.

Keywords: Accounting Information System, Accounting Duties, the Activities of Business, Profitability, Making Decisions.

Introduction:

Accounting can be viewed as an information system that communicates the financial and non-financial information of economic entities to interested parties. In fact its own unique terminology means it is often referred to as the language of business. The most important activities that considered as the essential part of accounting system can be categorized into financing, investing and operating activities [11, p.16].

Main Activities of Accounting Information System:

Financing Activities:

These are those which relate to the raising of funds for an economic entity to carry out its operating and investing activities. All companies must start with financing. Simply putting money into the business is needed to start [9, p.31].

A company's financing activities include obtaining the funds necessary to begin and operate business. These funds come from either issuing stock or borrowing money. Most companies not only sell stock to raise money but also borrow money from various sources to finance their operations, in other words most companies use both types of financing to obtain funds[11, p.17].

The discussion of financing activities brings up two important accounting terms" liabilities - is obligations arises when a company borrows money from another entity such as a bank or creditor and must repay the amount borrowed" and "capital stock". A creditor does not provide a permanent form of financing to the company. A common way for a company to obtain cash is to borrow money with the promise to repay the amount borrowed plus interest at a future date. Such borrowings are commonly referred to as note payable. A special form of note payable that is used by companies to obtain large amount of money is called a bond payable.

In addition to borrowing money from creditors, a company may issue shares of stock to investors in exchange for cash. The amount paid to a company for these shares is termed "capital stock" and represents the basic ownership interest in a company. Capital stock is the term used by accountants to indicate the amount of stock sold to the public. The difference between "capital stock" and "liability" is that; those who buy stock in a company are not lending money to the company, as are those who buy bonds in the company or make a loan in some other form to the company. Someone who buys stock in a company is called a stockholder, and provides a permanent form of financing to the company. In other words the company is not obliged to repay the stockholder the amount invested. However, many companies distribute a portion of their earnings to stockholders on a regular basis. This distribution is called dividends [8, p.18].

Therefore, creditors and stockholders have a claim on the assets, or economic resources of a company. However, the claims on these resources differ in the case of financial difficulty or distress, the claim of the creditors (liabilities) must be paid prior to the claims of the stockholders (called stockholders equity). Stockholder's equity is considered a residual interest in the assets of a company that remain after deducting its liabilities. Normally, the only way for a stockholder to get back his or her original investment from buying stock is to sell it to someone else [7, p.26].

Investing activities:

These are those associated with the acquisition and disposal of long-term resources used in the entity's production, selling or administrative functions [9, p.31].

There is a natural progression in a company from financing activities to investing activities, that is, once funds are generated from creditors and stockholders, money is available for investment. In other words, once a company has obtained funds through its financing activities, it invests the funds in productive resources that are necessary to operate the company [10, p.25].

Principally these activities involve investments in long-term tangible and intangible productive resources and financial assets that are needed to operate the company to generate interest-income, dividends, and other returns on investment and selling them when they are no longer need.

The point is that not all assets or resources are tangible in nature. A tangible asset is representing resource that expected to generate a future economic benefit to a company or the right to receive some sort of benefit in the future. The main intangible assets of company include cash, Land, building, and equipment [4, p.6].

Regardless of its form, these assets purchased by a company vary depending on the type of business that the company engages in, and the composition of these assets is likely to vary across different companies and different industries [11, p.17].

Operating activities:

Once funds are obtained from financing activities and investments are made in productive assets, a company is ready to operate .Operating activities are those associated with the provision of goods or services. Some of these operating activities also arise in non-profit making entities, and may be reported in their financial statements [9, p.31].

Every company is organized with a purpose in mind. The purpose of some companies is to sell a product. Some companies are organized to produce and manufacture products while other companies provide services rather than products.

While different companies have different purposes, they all want to generate revenue. Revenue "represents the amount of sales of products and services for a specific period of time or the increase in assets that result from the sale of products or services". It arises from different sources and identified by various names depending on the nature of the company. Sources of revenue common to many companies are sales revenue, service revenue, and interest revenue [5, p.10].

However to earn revenue, a company will incur various costs or expenses. Expenses take many forms and are identified by various names depending on the type of asset consumed or service used. The common types of expenses include: cost of goods sold (such as the cost of ingredients), selling expenses (such as the cost of the salespersons' salaries), marketing expenses (such as the cost of advertising), administrative expenses (such as the salaries of administrative staff, and telephone and heat costs incurred at the company's office), interest expense (amount of interest paid on various debts), and income taxes (company's tax paid to government).

The costs incurred to operate by a company include as follow [8, p.19]:

i. a company must pay its employees' salaries and wages;
ii. Suppliers must be paid for purchase of inventory, and the utility company has to be paid for heat and electricity;
iii. a company must pay the government tax.

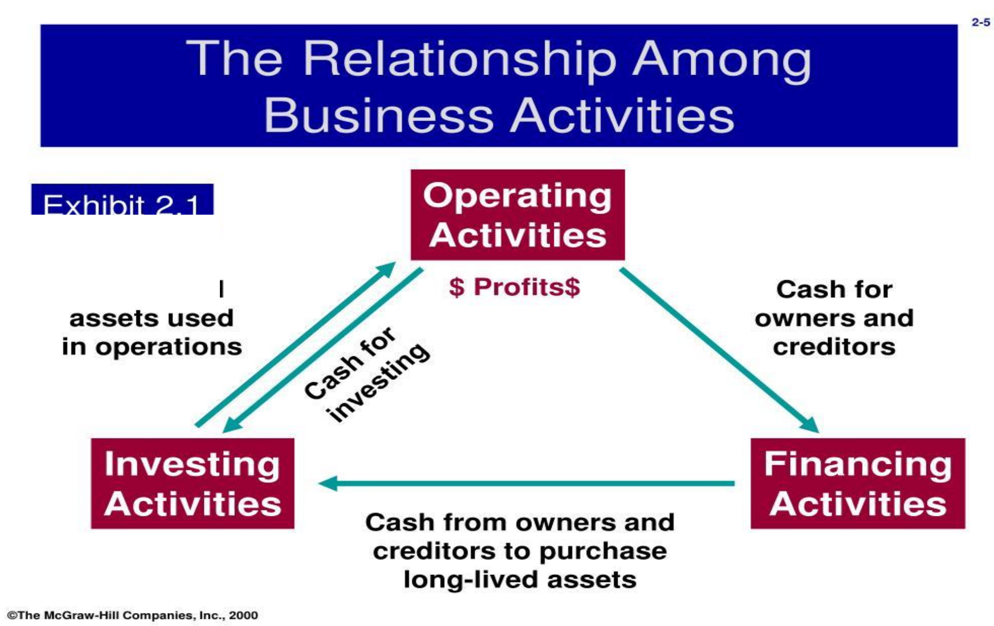

Fig 1 main activities of accounting information system

The results of a company's operating activities can be determined by comparing revenue to expenses. If revenue is greater than expenses, then a company has earned a net income. If expenses are greater than revenue, a company has incurred a net loss [11, p.17]. Figure 1 summarizes the three types of activities conducted by an economic entity and considered as essential parts of accounting information system

Basic Functions of An Effective Accounting Information System:

The effective accounting information system entails a number of tasks and duties that can help the management of business organizations to achieve their goals and the success of strategies outlined for them. The most important of these tasks can be summarized as follows [1, p.15; 3, p. 345]:

i. Facilitate The Process of Making Decisions:

The primary function of accounting system is to help in providing a basis for planning and control of future activities that enables management to make decisions to run the business organization. Also it helps to facilitates corporate and investment decisions, a major part of corporate and investment decisions relies on analyzing all of the companies accounting information system.

ii. Evaluating Financial Position of Business:

The financial position of an entity, deals with the economic resources controlled by an entity, its financial structure, its capacity to adapt to changes in its environment, and its liquidity and solvency .In addition to profit, management of business must evaluate financial position, accounting information system helps to achieve this goal in a right manner.

iii. Predicting Potential Cash Flows:

Accounting information is useful in predicting the ability of the entity to generate cash flows in the future, and to meet its financial commitments as, and when they fall due. The accounting information system that would help to assess these aspects includes the different types of assets held by the business, the amount of money borrowed from other entities, the amount of cash or other assets supplied by the owner of the business, the time needed to repay borrowed money, the current state of repair of the entities assets ,the selling price of these assets , and the possible source of finance available to the business in an emergency . All this information is desirable to help users make informed economic decisions about an entity.

iv. Fulfill the Legal Requirement:

One way ensure that entities are indeed meeting their legal requirements is to examine their accounting information system. Auditing is compulsory in case of registered firms. Auditing is not possible without accounting system, thus its becomes compulsory to comply with legal requirements.

Indicators of Evaluating Successful Accounting Information System:

Despite the functions and tasks that can accomplish by an effective accounting information system, there are some indicators through which it can measure the level of success of this system, the most important of which are:

i. Profitability:

The financing, investing and operating activities of a company as detailed transactions within AIS to effectively communicate the company's financial information to decision-makers. These detailed transactions are summarized and reported in a set of standardized reports called *financial statements* that represent the final result of AIS. The role of financial statements is to measure and report the financial activities of a company's performance for a period of time (profit and loss), usually a quarter or a year, in order to provide accounting information that will help investors, creditors and others make judgments and predictions that serve as the basis for the various decisions they make [2, p. 40; 10, p.24].

ii. Liquidity:

It is the ability to have enough cash to pay debts when they are due. All economic entities pursue their goals by formulating an effective accounting system engaging in financing, investing and operating activities [6, p.5].

Conclusions:

1. Business organizations must seek to study the environmental factors that may surround business, whether internal or external, before starting the process of formulating an accounting information system in order to ensure the accuracy and objectivity of this system.
2. The functions of a useful accounting information system are not limited to earn profitability only, but rather expand to achieving other goals that serve the requirements of many users. Among those goals is to meet the social requirements of the public that depends on the results of the accounting work in one way or another.
3. The necessity to adding other indicators by which can assess the effectiveness of the accounting information. One of the most important of these indicators is the practice of cost benefit analysis, which requires a comprehensive analysis of the cost relating of building this system and an estimate the expected benefits from this system in order to ensure that total costs do not exceed the future benefits that can be obtained.
4. The importance to achieve an acceptable level of compatibility between management goals and external users requirement before operating this system in order to avoiding the conflict of interest amongst multiple parties, which represents one of the most important challenges in building an excellent information system for business organizations.

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