THE NATURE AND SCOPE OF THE FINANCE FUNCTION

PAST, PRESENT and FUTURE*

By

GURUPRASAD MURTHY

LALA LAJPATRAI RESEARCH CENTRE

*BASED ON THE LECTURE DELIVERED ON 3-9-1981 AT THE LALA LAJPAT RAI COLLEGE OF COMMERCE AND ECONOMICS, BOMBAY.
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THE FINANCE FUNCTION – IN RETROSPECT

A redeeming feature of the twentieth century corporate scene is the emergence of Financial Management, as a distinct discipline at the level of the individual enterprise. In the past, financial management of business was considered as a part of the wider discipline of the economics. As a result it was difficult to identify an independent function of and scope for finance in business. The functions of finance, and therefore the study, were more or less related and restricted to the individuals and institutions contributing 'money' or 'funds' or 'finance' to the business. Thus, the focal point was the financial instruments and institutions which provided the required financial resources and the scope of the finance function was restricted to the procurement and deployment of funds. In this situation financial management was defined as “managing money or cash transactions of a business” or as “raising and administering funds used in the enterprise”.* The external environment like financial markets (money markets and capital markets), financial institutions and agencies and financial instruments dominated the finance function as well as the study of finance. The first few formal works on business finance by Greene, Meade, Dawing and Lyton presented an almost uniform thought. As Archer and D'Ambrosio would put it “All of them ………….. typically use what may be referred to today as the “traditional approach to the study of business finance, emphasizing as they do major episodic financial events** in the life cycle of a firm and institutional factors that bear on them”*. And, the purpose of corporation finance was to “describe and to document the rapidly evolving complex of capital market, institutions, instruments and practices”***. But the traditional school of finance, referred to above, was criticised, even in those days for the undue emphasis placed on the investment bankar and the concomitant conspicuous attention given in text books to the ‘outsiders looking at the inside’. It was also criticised for leaning in favour of long term financing decisions and the consequent neglect of Working Capital management. Further, the episodical approach to finance and the concentration of the studies of finance in favour of corporate forms of organisation to the exclusion of other sectors of the economy also came under heavy attack. Undoubtedly, the traditional

** Promotion, incorporation, merger, consolidation, recapitalisation and reorganisation.
** Ezra Solomon Theory of financial Management.
approach to corporate finance was rather narrow to effectively subserve or meet either the then existing or emerging needs of society at large. It had to give way to an altered recipe of financial management which eventually came to be called as the 'Managerial Approach'. World War I brought in its wake a new cultural pattern which gave prominence to the corporate form of economic organization. Corporate securities were slowly becoming a popular mode of investments. The corporation became an useful avenue for the investor and an effective base for resource mobilisation for the resource mobilisation for the entrepreneur. And out of this emerged a mutually understood financial objective, between the corporate management on the one hand and corporate shareholders on the other, viz. "maximisation of the economic welfare of the shareholders (owners or capital contributors)". Thus, an important function, in fact the cardinal function of finance is to protect and promote the investors (shareholders/owners) stake in business. With the emergence of this accepted objective of financial management, the scope of the finance function within an individual enterprise was enlarged.

The corporate management were vested, as custodians of the assets of the enterprise, with the task of effectively communicating their terms of reference vis-a-vis the shareholders. Stated in a general way the corporate management had to promote the greatest good of the share-holders by producing the best possible results with the resources entrusted to them, or the highest possible output for any given input. So, for the first time, in a limited way though, financial management was to be viewed from "the insider looking out" rather than vice-versa a la traditional approach. In this context, new and broader definitions of finance emerged.

The episodic approach to finance continued to be increasingly supported by the "managerial approach". However, this blend between the episodic approach (traditional view) and the managerial version (modern finance—say) continued in various proportions till World War II. In fact the managerial approach, identifiable in the post-World war I epoch in the work of Gerstenberg (1915), Lincoln (1921) and W. M. Stevens (1934), gave some emphasis on topics like profit planning and control for the enterprise as a whole and also functional areas like production and sales, budgetary control, cost control and so on. Slowly, the episodical approach was relegated to the background, and the managerial approach was in the forefront. Another notable development in the inter-war period, that is to say in 1930, was the announcement by the Controller's Institute (Financial Executive Institute) in the USA about the bifurcation of the Finance Function into two viz. Controllers' and Treasurers' functions in fairly unequivocal terms. For instance, the controller's functions
included planning for control, reporting and interpreting, evaluating and consulting tax administration, Government reporting, protection of assets and economic appraisal.

And, the treasurer’s function included provision of capital, investor relations, short-term financing, banking and custody, credits and collections, investments and insurance.

Thus while the scope of finance was identified as extensive, it was split into two different roles viz. ‘The Treasurer’ and ‘The Controller’. But, the classified functions of the treasurer, clearly bring out the role of financial institutions, agencies and instruments. It also shows the domination of routine, internal and administrative functions in the office of the treasurer. The managerial dimension of finance was almost conspicuous by its absence. The primary focus was on maintaining relationship with agencies which were potential sources and users of corporate capital.

The functions of finance and, ‘ipso facto’, its scope were restricted to the custodial, stewardship, role. Active involvement of the finance manager in the functional areas of management was almost unheard of. And, the managerial version of finance was either absent or subordinate to the custodial function. But it was only after World War II, as late as 1949, that internal financial problems of enterprise started dominating the study of finance. This new version of managerial finance gathered momentum and acquired its full stature as a sequel to the Keynesian General Theory of Employment. Keynes said that the effective demand for investments depends upon the expected rate of return on incremental investment and the cost of incremental capital. This macro-analysis was systematically conceptualised into a feasible micro-level or enterprise level analysis.

Joel Dean’s Capital Budgeting (1951) was a starting point followed by Ezra Solomon’s Management of Corporate Capital in 1959 and the Theory of Financial Management (1963). Ezra Solomon’s book brought into limelight a frame of thought within which the scope and functions of financial management, were identified at the micro-level or the level of the enterprise. Since then many useful and scholarly works on corporate Finance have been published all over the world, particularly the U. S. A. Ezra Solomon’s work gave a further impetus to refine the corporate financial objective and ipso facto the corporate financial management techniques employed to achieve the said objectives. The Corporate financial objective of maximisation of the shareholders’, results-resource
ratio was defined as "continuous maximisation of the present value of the future benefits of the shareholders" or "continuous maximisation of the present value of the shareholders' wealth." The above phrase is algebraically expressed as follows:

\[ \sum_{i=1}^{N} \frac{B_i}{(1+k)^i} \]

Where \( B_i \) = propospective yields expected over the economic life of a proposal at the end of each year.

\( K \) = discount rate used as the cut-off point.

THE FINANCE FUNCTION – TODAY.

An analysis of the evolution of the changing profile of the scope and content of the Finance Function can be appreciated better if the scope and content of the Finance Function in practice is examined. We may consider a typical corporate form of organization and examine the functions of the Finance Department (say in the Indian context in current times). The functions included broadly categorising, External Reporting (Score-keeping of one sort or the other to meet the farrago laws governing enterprise) and Internal Reporting (Attention Direction and Problem Solving). External Reporting includes Shareholder Reporting (Financial Accounting), Cost Audit Reporting, Tax Reporting, Reporting to Agencies concerned with the pricing and procurement of different sources of finance (financial institutions, controller of capital issues, stock exchange authorities) and Reporting to Government Agencies viz. Foreign Exchange Regulation Act (FERA), Bureau of Public Enterise, Bureau of Industrial Costs and Prices (BIBP), Monopolies and Restrictive Trade Practices Authorities and any other duly appointed Government/Semi Government Agency. Internal Reporting includes providing relevant, quantified and other information, to aid product costing (income determination and inventory valuation), profit planning and control (using techniques like standard costing, budgetary control, marginal costing), decision making relating to quantum and mix of finance, quantum and mix of assets, rate of growth in assets, make or buy, sell or process further and pricing decisions, performance budgeting with a view to practice responsibility accounting, and decision making in functional areas of management like production, marketing, personnel. It is not out of place to mention here that new concepts of cross-functional finance viz. production finance, marketing finance, personnel finance is slowly gaining currency. We will consider the above functions in turn.
EXTERNAL REPORTING (E.R. – I)

FINANCIAL ACCOUNTING AND AUDIT

Financial Accounting refers to the score-keeping or stewardship or custodial function of the Finance Department. It includes the maintenance of the books like journals, ledgers etc which lead to the preparation of the final accounts comprising 'Trading or Manufacturing and Profit and Loss Account' OR 'Income and Other Statements (statement showing Factory Cost of Sales and Statements showing Non-Manufacturing Expenses)' and Balance Sheet'. The function of financial accounting includes debtors and creditors accounting, fixed assets accounting, billig, and payroll accounting.

All the above functions, in the ultimate aid in preparing the financial reports relevant to fulfill the statutory obligations under the Indian Company Law. The reports are prepared in accordance with directives in Schedule VI of S211 of the Companies Act a prescribed format for the Balance Sheet and Notes to Profit and Loss Account. Thus, "every business in incorporated under the provisions of Companies Act (1956) is required to maintain books of account as stipulated in S209. S. 210 requires that at every annual general meeting held in pursuance of S.166, the Board of Directors shall lay before the share-holders a balance sheet and a profit and loss account. The primary objective is communication to the shareholders about the state of affairs of the business. S. 211 dictates the form and contents of balance sheet and profit and loss account.

S. 211 Schedule VI (Companies Act) comprises three parts vis. Part I which till recently prescribed a Balance Sheet format popularly known as the Horizontal Format. Now it is no longer necessary to adhere to the horizontal format*. Since then a company may, choose to present the balance sheet data either in a 'Horizontal Format' or 'Vertical Format. Earlier to the above referred Government resolution deviation from the horizontal format was possible only if prior permission of the Company Law Authorities was obtained; Part II of Schedule VI provides a list of the instructions to be followed while preparing the Profit and Loss Account, known as 'Requirements as to Profit and Loss Account'. The Companies Act does not prescribe any format, for the Profit and Loss Account, perse. Part III of Schedule VI entitled 'Interpretation' gives instructions relating to the treatment to be accorded to Provisions and reserves and clarifies the meaning of certain expressions used in Parts I & II of Schedule VI.

* As per Government Special Resolution. 220 (E) of 12-3-1979.
It is interesting to note that the data used to meet the statutory obligation under S. 211 of the Companies Act is predominantly, possibly exclusively historic accounting data i.e. actual costs and actual revenues based on ex post accounting analysis of actual transactions (events).

It is not out of place to mention that shareholders reporting transcends much beyond the bounds of the three parts of Schedule VI of the Companies Act in much as

a) in terms of S. 217 (2A) of the Companies Act 1956 vis-a-vis the Companies (Particulars of Employee) Rules 1975 the company has to provide particulars of all employees drawing Rs. 3000 or more per month;

b) in pursuant of S. 212 of the Companies Act a Statement relating to the subsidiary companies has to be issued

c) in accordance with S.277 of the Companies Act the Companies are obliged to provide auditors report as per the Manufacturing and other Companies Auditors Report order (1975) (with effect from 1-1-1976)


COST ACCOUNTING AND AUDIT (E.R. – II)

Cost Accounting includes maintenance of cost records to fulfill the following functions:

a) Cost book-keeping which means recording costs according to readymade cost classification scheme

b) Cost control which includes a comparison of actual costs with predetermined costs

c) Cost analysis which includes variance analysis and pinpointing responsibilities for variances, and

d) Cost comparison which includes providing comparative cost data regarding alternative activities, products, methods in the functional areas of production and marketing.
The functions of cost book-keeping, cost control and to some extent cost analysis is obligatory if an enterprise or any segment thereof is within purview of S. 209 (1) (d) of the Companies Act which makes Cost Accounting a compulsory proposition and Cost Audit a statutory requirement. S. 209 (1) (d) says "in the case of a company pertaining to any class of companies engaged in production, processing, manufacturing or mining activities, such particulars relating to utilisation of material or labour or to other items of cost as may be prescribed, if such class of companies is required by the Central Government to include such particulars in the books of account".

The objects of the introduction of the clause was to ensure the maintenance of proper cost records relating to the utilisation of material and labour with a view to facilitate efficiency audit. The Government are of the firm opinion that efficiency audit is possible only when a system of cost accounting is adopted and costing records maintained. Further, cost accounting is a continuous process, and the maintenance of cost records will permit the evolution of standard costs (scientifically predetermined costs) thus making periodic cost comparisons (actual costs vis-à-vis standard costs) a plausible proposition. With the above ideas in view section 209 (1) (d) was made applicable, with effect from October 1968. For instance the said section applies to companies manufacturing the following products viz. cement and clinker, cycles and components thereof, rubber tyres and tubes caustic soda, room air-conditioners, refrigerators, storage batteries used in automobiles, electric lamp or fluroscent tubes or both, electric fans, electrical motors, motor vehicles and tractors. The kind of cost data used to fulfill the statute governing cost audit will be a curious mixture of predetermined costs and actual costs. The intention of the statute is to encourage the development of a cost data bank which can provide target costs or standard costs. However, in business units which have started the practice of or cost accounting only after the insertion of S. 209 (1) (d), it will be difficult to identify predetermined costs. Hence, at least for a few years, in the initial instance, only actual costs or historic costs will be available. But in units which have been practising cost accounting, regardless of S. 209 (1) (d), standard cost information should be readily available.

TAX ACCOUNTING (E.R. - III)

Tax Accounting, also known as 'Tax Management', 'Tax Planning', etc includes planning the profits to minimise tax liability; liason with tax authorities levying corporate income tax, central sales tax, excise duties, state levies and imposts; indentifying the tax impact of alternatives
open to operating managers in their decision making; and computing taxable income, assessing tax liability and filing the tax returns.

The Income Tax Act (1961) has a specific requirement which relates to 'Advance Tax' or 'Pay as You Earn' Scheme S. 211 of the Income Tax Act (1961) says that "Subject to the provisions of this section and of sections 209A and 212 advance tax shall be payable in three equal instalments on the following dates during the financial year, namely:

(i) the 15th day of June, the 15th day of September and the 15th day of December if the year ends on or before 31st day of December.

(ii) the 15th day of September, the 15th day of December and the 15th day if March in any other case.

Thus, even before the expiry of an accounting year a Company has to have knowledge about 'likely revenues, 'likely costs' and 'likely profits'. Hence the inadequacy of the historic accounting data of an accounting period which presents actual costs, actual revenues and actual profits and the inevitability of predetermined or projected information relating to the parameters cited above.

AGENCIES CONCERNED WITH PROCUREMENT AND PRICING OF FUNDS

The agencies involved in the above function, include, inter alia, financial institutions (development banks and commercial banks), Stock Exchange Authorities, Controller of Capital Issues, Reserve Bank of India, Foreign Exchange Regulation Act, Authorities Monitoring the Companies (Acceptance of Deposits) Rules, 1975.

Financial institutions appear in corporate situations where there is a negotiation for loans between the company (borrower) and the institutions (lender). The financial institutions seek data, past, present and future, from the concerns seeking assistance with a view to assess the credit-worthiness in terms of liquidity, profitability and integrity. In explicit terms, the lender would like to

(a) ensure periodic receipt of interest;

(b) ensure timely amortisation or repayment of loans by the assisted units; and

(c) improve their status in the enterprise by invoking their right to convert their loans into equity share capital.
Again negotiation of loans with commercial banks for bank overdraft, cash credit, and in some cases bridge loans and term loans takes place within the framework of the overall Government fiscal and monetary policy, Tandon Committee and now the Chore Committee Recommendations. Hence the enterprise intending to negotiate with development or commercial banks has to provide all historic/futuristic data called for by the lending agencies.

Liaison with financial institutions to provide relevant historic and future data to aid project appraisal is another dimension of funds procurement exercises to be performed by the Finance Manager in our country. The development banks conduct project appraisal on a professional basis employing scientific management tools concerning capital expenditure decisions viz. 'Payback Method', the 'Discounted Cash Flow Techniques' and in many cases sensitivity analysis and 'Simulation Techniques'. Projects proposed by enterprise have to surpass the target rate or hurdle rate, prescribed by the financial institutions, to justify the use of capital. Project Management transcends beyond the initial liaison for getting loans sanctioned. The relationship between the assisted concerns and the financial institutions is a continuous one, once a project is sanctioned, and there is a constant, periodic, dialogue between the lender and the borrower. The borrowing enterprise has to keep the lending institutions informed about the project progress in particular and the enterprise health in general. Thus, in our environment today 'Project Management and Bank and Funds Management' are interrelated functions to be taken care of by the enterprise interested in short term/long term funds procurement—particularly procurement of borrowed funds.

The Controller of Capital Issues is another important agency with which enterprise has to keep constant touch to:

(a) implement the existing and emerging legislation governing capital issues;

(b) seek permission for procurement and pricing of additional funds; and

(c) seek sanction for the issue of bonus shares and also for the making of a 'rights issue'.

The relevant legislation in this regard include The Capital Issues (Application for Consent) Rules 1966, Application for Guidelines for Bonus Shares, Conditions for the Issue of Rights Share, Issue of Securities at Premium or Discount.
It is a well known fact that an important function of the finance manager is wise management of the sources and uses of funds which include procurement of funds at the right time from the appropriate source at the lowest possible cost within the constraints imposed by statute and Government notifications in this regard. In our country the volume of funds and its mix is influenced by the Government whose policy on debt : equity ratio reads as follows "To Finance the capital cost of project, the capital structure should be such that an equity-debt ratio of 1:2 is considered fair and reasonable. In case of capital intensive industries a higher equity-debt ratio can be considered on merits of each case". 

The cost of funds is monitored again by legislation and notifications from time to time. Thus, interest rate on debentures is regulated in terms of notifications in pursuance of sub-clause (ix) of clause 5 of the Capital Issues (Exemption) Order. In September 1974 the interest rate on debentures and bond was raised to 10 per cent for a term upto and including seven years and 10.5 per cent for a longer period. Again in 1980 the Government revised the interest rate of debentures and jacked it to 12 per cent with an explicit proviso that the companies can offer suitable incentives to attract investors by issuing debentures at discount paying an additional interest of upto one percent for any year if in that year the company declares a dividend on its equity at a rate exceeding a previously established rate (for example the highest rate of dividend declared in the three years preceding the debenture issue). Further, in March 1981, the Finance Minister has proposed "to raise the interest rate ceiling on debentures from 12 percent at present to 13.5 per cent".

The Stock Exchange Authorities represent yet another body with which association of the enterprise is necessary to -

(a) ensure compliance of the Securities Contracts Regulation Act.

(b) ensure fulfillment of directives issued by the Stock Exchange Authorities to companies intending to list their securities and offer the same for public subscription.

Thus, Rule 16 (2) (b) of the Securities Contracts (Regulation) Rules 1957 required, till March 1981, that at least forty-nine per cent of each class or kind of securities issued by the company should be offered to the public for subscription. It also provided that the stock exchange authorities could relax the above rule with the previous approval of the

* Guidelines for ISSUE of fresh capital issued by the Office of the Controller of Capital Issues (14-5-1975)
** Finance Minister’s Speech, Budget, PART A, Para 31, P. 10
Central Government. However, in his budget speech of 28-2-1981 the Finance Minister Mr. R. Venkataraman said... "We have decided to relax the requirement under the Stock Exchange guidelines that promoters can hold only a maximum of forty per cent of the equity of a new company". Further he said... "promoters will be allowed to hold higher equity than the forty percent limit during the initial stages of a project". The Companies intending to place new issues with listing facilities have to reckon with the new situation which says that.

(a) the minimum public offer of equity should not fall below 20 per cent.

(b) promoters will be allowed to hold a higher equity than the present 40 per cent limit, subject to an upper ceiling of 70 per cent.

(c) the 70 per cent ceiling is permitted only to enable the promoters to meet the requirements of the MRTP Act which requires promoters to contribute 20 per cent of the total project cost.

Now, given the cost of the different sources, the finance manager has to use his conceptual skills and managerial judgement to decide the "price tag" to be attached to each source of finance. The relevant concept is the tax adjusted cost of capital adjusted further for the proportion which each source bears to the total composition by a process of 'weighting'. Thus, the costing exercise in this regard will finally result in a concept called 'weighted Average Cost of Capital'. So if K is the cost of capital and K1 = cost of debt, Kp = cost of preference shares and Ko = cost of equity capital and W1, W2, W3 represent the weights of debt, preference share capital and owners funds respectively the tax adjusted, weighted average cost of capital is given by the equation

\[ K = K1 W1 + Ko W2 + Kp W3 \] and \[ W1 + W2 + W3 = 1 \]

In this frame of analysis the finance manager has to provide answers to three critical questions. What should be the sources of funds and the mix of the sources to enable the composite cost of capital to be the lowest possible?

What should be the uses of funds and the mix of the uses of funds to yield the highest possible return on the resources committed in different uses (assets)?

How large should the enterprise be and how fast should it grow that is to say what should be the pace of change in the volume of the sources and uses of funds?
In fact, the above three aspects are a critical set of functions and even the traditional school did not really exclude it. Dewing in defining finance had said "All business problems centre about three essentially different activities. These are production, the sale of the products and finally the disposition of the proceeds from this sale. All these possibilities comprise problems which concern themselves directly with one central theme – the wise disposition of the money proceeds of the business. This is finance".

GOVERNMENT REPORTING

In addition to constant interaction and continuous compliance with the different statutes, independent bodies, Government agencies and Semi-Government institutions companies have to interact from time to time with Government to implement certain specific objectives underlying Government policy manifest in a statute form or otherwise viz. Monopolies and Restrictive Trade Practices Act, Foreign Exchange Regulation Act, Bureau of Industrial Costs and Prices. In fact S.615(1) of the Companies Act reads as follows:

"The Central Government may by order require companies generally or any class of companies or any company, to furnish such information or statistics with regards to their or its constitution or working and within such time as may be specified in the order".

Thus, the tentacles of Government are rather widespread and the finance department (in fact the corporate enterprise) is in the firm grip, if not clutches, of the State. Hence, the Finance Manager in current times in India has to develop an appropriate kind of skills, attitudes and competence to grapple with the ever increasing external, bureaucratic, mandatory pressures for disclosure.

INTERNAL REPORTING (I.R.)

I.R. includes the provision of relevant, quantified and non-quantified data to aid different levels of management in routine day to day operations and long run decisions. IR subserves the functions of ‘Product Costing’, Profit Planning and Control, Responsibility Budgeting and Decision Making. The tool which is made use of by most Companies to make IR a success is now universally known as ‘Management Accounting’. Management Accounting refers to the process which provides, analysis, reports and discusses accounting and related information with a view to aid management in the day to day running and future planning of an enterprises. The general objective of management accounting can best
be described as responsibility accounting i.e. to report information suited to their responsibilities to varying levels of management and supervisors who can take action on that information. It may not be out of place to mention that in providing relevant information to different levels of management an effective management accounting system is one which strikes a balance between speed, accuracy, timeliness and cost of the information provided. Management Accounting thus implies provision of relevant, quantified, varifiable, timely, accounting and other related data to different levels of management to aid product costing, profit planning and control and decision making. In other words, Management Accounting aims at fulfilling the functions of 'Attention Direction' and 'Problem Solving'. Attention Direction refers to the process which provides data relating to the act all events accruing vis-a-vis the intended events in different segments of business. Within a segment the actual inputs (costs) / outputs (revenues) are assayed against the target costs and revenues. A comparison of actual events with the intended events represents the process of control in action. Such comparison is possible only if a fast feed back relating to actual events are available. The comparison aims at identifying the strong segments enjoying favourable per-formance (actual costs being less than intended costs OR actual revenues being greater than intended revenues) and weak segments with unfavourable performance. The focus of attention will however be on the weak segments which need the attention of the management. The situation demands remedial actual (corrective measure) to prevent the recurrence of the unfavourable events. In fact the principal merit of the above exercise is the possibility of the practise of 'Management by Exception'.

Again problem solving refers to the different day to day as well as long range problems needing scientific processing before a decision is taken one-way or the other. Thus, in the short run the company has to take tactical decisions viz. 'make-or-buy' 'sell or process further' 'product mix', 'operation versus shutdown', 'pricing for a special order in domestic or export markets' and 'long range decisions which include capital expenditure decisions'. Management Accounting provides scientific cost and other data to process and evaluate the alternative available. The scientific processing of situations posit with alternatives aids scientific decision making.

Another important function of the Finance Department is 'Audit and Systems Management which includes –

(a) internal audit to check the conformance of the accounting and other activities of the enterprise with prescribed criteria;
(b) audit of the planning and control systems like data providing system, financial control system and management control system;

(c) management services which is supposed to sell the idea of professional approach to decision making and management of an enterprise. It includes guiding various segments of business and operating managers in different functional areas viz. production, marketing, personnel and purchase, in matters relating to scientific business management or even personal tax matters which requires a professional approach today.

And last, but not the least, the function gaining currency is 'Electronic Data Processing'. It includes the interaction of the finance personnel with the computer. Today, in business, computer is made full use of to provide relevant ready made information to fulfill the functions of financial accounting, cost accounting, management accounting, project management banking and funds management and tax management. This function continues to be in increasing vogue and to reiterate is gathering momentum more than ever before.

The Finance Departments Functions, presented in Exhibit Two, and discussed in the foregoing paragraphs are broad-based and fairly exhaustive. However, certain unique features of the Finance Department of an enterprise in the Indian situation, today, merit special mention.

1. The priorities attached to certain segments of the Finance Department will vary from enterprise to enterprise and within an enterprise from time to time. For instance, if external finance (additional share capital and borrowed capital) is dominant, liason with the capital markets and the financial institutions assumes due importance. However, if additional finance is forthcoming primarily on account of ploughed back funds the function of maintaining liason with external contributors of funds is of auxiliary importance.

Again, if a new project is being launched, project management assumes added significance while in the normal course project management may be one of the several functions. Further, if working capital procurement is difficult, because of the stringent restrictions imposed by banks, management of working capital, monitoring inventory levels and cash flow and liason with banks and other short term financing agencies assume importance. Thus, if the problems encountered by an enterprise vary from time to time the importance of a particular function vis a vis the other functions also tends to vary. And, the changes in policy
(external versus internal sources) regarding method of financing and variation in environmental pressures can alter the importance of one function as against another within the same enterprise. Further in the Indian situation, tax management assumes serious importance because of the complexity of tax laws, variety of intricate tax incentives and also progressive tax rates. Many companies in the private sector in India attach great importance to the function of tax management. And the idea of a separate office of the ‘Tax Accountant’ or ‘Tax Planning Manager’ is increasingly in vogue.

2. In any companies because of the changeover from manual accounting methods to computer based accounting the function of electronic data processing is given a special importance. The difference in the importance given to this function depends on the environmental pressures and the local problems of the company concerned. In some Indian companies the function of the head of the finance department is restricted to the professional skill and capabilities of the head. The modern ‘Management Accounting’ and ‘Financial Management’ functions are vested in a separate office called ‘SYSTEM MANAGER or ‘BUDGET OFFICERS; ‘MANAGER MANAGEMENT SERVICES’ reporting separately to top management (Executive director/Managing Director). Thus the extent of the professional skills, attitude and competence of the existing head of the finance department also influences the scope and functions of the Finance Department.

3. The Finance Department in any enterprise is a ‘Service unit’ or ‘staff function’ or an ‘advisory cell’. It provides relevant data, which usually originates in the finance department, to the operating managers in the functional areas of production, marketing personnel, purchase and also to corporate management.

4. The segments comprising the finance department are not necessarily clustered at one point. It could vary well be geographically dispersed over different segments of the enterprise. Thus, financial accounting may be centralised and cost and management accounting decentralised. An enterprise could have the concept of a ‘Product Accountant’, ‘Product Cost Accountant’, or ‘Product Management Accountant’ or ‘Group Management Accountant, or ‘Divisional Account’ depending on the needs and convenience of the enterprise. It is quite possible that Financial Accounting, Tax Accounting for Salaries of Non-Factory Personnel, Internal Audit, Systems Management and Management Services are centralised under the ‘Finance Department Head’ and Factory accounts payroll accounting, material costing, (stores costing), overheads accounting, cost book-
keeping management accounting (production/marketing) are decentralised and geographically dispersed to suit the needs of the company concerned.

5. The position and designation of the head of the Finance Department varies from enterprise to enterprise. Likewise, the positions and nomenclatures of the personnel attached to the finance department differ from company to company. Thus, in a company where product costing was important the post of ‘PRODUCT COST ENGINEERS’ emerged. The product cost engineers were responsible for “developing price targets and buying objectives for all purchased parts; and for analysing and studying suppliers claim for price increase and for estimation of cost changes due to various reasons and for analysing the effect of material variations of products”. In another company, the function of pricing assumed importance and the post of a ‘SR. PRICING ANALYST’ was created with specific responsibilities to “prepare cost estimates for pricing vehicles, engines and parts and for evaluating financial implications of various price options”.

Similarly it is possible that functions like ‘funds management’ may become important giving rise to the post of a ‘funds manager’ or ‘working capital executive’ or ‘overhead Costing’ may be important resulting in the post of an ‘Overhead Accountant.

6. The practise of combining secretarial/legal functions alongwith the accounting and finance function is increasingly evident. In one company the finance department was headed by a ‘Company Secretary cum Finance Manager’ who was responsible for “all financial, secretarial and taxation matters of the company.....” Yet, in another company, the finance manager was responsible for all financial functions, accounting, budgeting, planning and taxation. In addition, he was also in charge of personnel administration and secretarial/legal matters.

7. The distinction between financial accounting, management accounting and cost accounting is either not understood or ignored in designing the positions and corresponding job descriptions’. Thus, in one company a financial accountant, usually vested with a custodial, score-keeping, function, was responsible “for all aspect of statutory accounting and financial information systems”.

8. The term ‘Management Accounting’ is well known and the position of a Management Accountant is also accepted and is becoming fairly common. But the functions of the Management Accountant are heterogeneous in terms of company to company comparison. Thus in four companies we find the following versions:
COMPANY 1, the functions of a Management Accountant include financial planning, management and control, negotiations with institutions and banks, management accounting, taxation and reporting to Directors.

COMPANY 2, the functions of a Management Account include responsibility for all accounting matters for the manufacturing–cum–trading division of the company.

COMPANY 3, the functions of a Management Accountant include charge of the entire accounting and budgeting function of all operating divisions at the plant, AND responsibility for developing and operating the existing standard cost system, which aim to provide operating management with timely and meaningful control information.

COMPANY 4, the functions of a Management Accountant include total responsibility for accounting matters for a number of trading/manufacturing divisions, AND directly report to the Chief Accountant for taxation, company law and foreign exchange matters.

9. Liaison with financial institutions is assuming serious importance. This speaks of the dominant role of banks (development and commercial) in our corporate financial environment.

10. Although the position of the head of a Finance Department is oligopolised, if not monopolised, by professional chartered accountants in particular and professional accountants in general there is an increasing awareness of the inevitable need to accept the MBA/MMS/MFM* species in the mainstream of the Finance Department. The increasing intrusion of sophisticated management techniques and the impending invasion of finance by ‘Operations Research’ has already resulted in a handful of situations where heads of finance departments (at the Board Level) are Engineers with specialisation in Operations Research and some exposure to basic concepts in Finance. It is not untrue to say, that there are quite a few management accountants who are neither chartered nor cost accountants but are statisticians, or economists or engineers, with exposure to management accounting in management diploma/degree programmes. This approach to choosing management accountants from outside the professional accountants corps has proved to be a novel experiment and also a success. This trend will therefore continue with increasing slant in favour of persons with mathematical bent

* MBA — Master’s Degree in Business Administration
MMS — Master’s Degree in Management Studies
MFM — Master’s Degree in Financial Management
of mind, mathematical qualifications and professional exposure in the application of Quantitative Methods and Operations Research to corporate economic management.

The foregoing analysis bring to the fore the all pervasive character of the finance manager in an enterprise of current times. In fact, it is not untrue to say, that this is an universal tendency. This is because in the post–World–War II epoch the entire approach to finance has changed all over the world. As an article in the Fortune, entitled "The New Power of Financial Executives points out /'Top financial officers now have a hand in everything from mergers and budgets to personnel and marketing. They also woo bankers and stock analysts. Because they usually know more about the company than anyone else they often move, finally, right into the driver's seat" The Finance Manager of today is a "planner", 'organiser', co–ordinator and 'controller'. As a planner the finance manager give a finance orientation to the corporate planning process. plans velates to the routine, day to day activities of ensuring plan, (budget) period. Plans relate to the growth aspects of an enterprise like expansion programmes and diversification schemes.

Both the factors, routine operations and growth, are analysed from the finance manager's view point, and placed before the corporate management for further action which includes interpretation and decision making. The organisation function includes:

(a) communication between the finance and the other departments, &
(b) between the functional areas of management inter-se. The Finance Manager assumes the role of a co–ordinator or a 'liaison executive' who promotes the relationship between all departments, so that the personnel at various levels of responsibility act in unison to achieve the intended corporate objective. The Finance Manager makes use of budgeting, accounting and reporting techniques to establish a rapport between the finance departments and other departments; AND between the functional departments themselves.

The finance manager, as a co–ordinator is a link between the activities of different segments of business. It is this link which makes finance an essential ingredient of the line managers activities in the functional areas like production, marketing, personnel and purchase. Further it is in this context that the scope of finance function has extended its limits and transcended beyond its traditional bounds into other areas of business.

As Ezra Solomon says: "financial management is properly viewed as an integral part of over-all management rather than as a staff specially concerned with fund raising operations. Thus, in addition to raising funds, financial management is directly concerned with production, marketing and other functions within an enterprise whenever decisions are made."*

Keeping in view the importance of Finance and the key role played by the Finance Manager in today's enterprise, Exhibit ONE presents the conceptual process involved in the 'modus operandi' of the finance function in an enterprise and Exhibit TWO presents the different functions of the Finance Department and the kind of personnel usually employed to handle the different roles. (Note to Exhibit Two) Finally, Exhibit THREE shows the conceptual comparison and contrast between the different functions of the Finance Department in terms of the information required to effectively discharge the said functions.

THE EMERGING FINANCE FUNCTION

We have just finished discussing the functions of the Finance Manager in the past (Traditional Functions) and the present (Managerial Finance Functions). We have also presented an overview of the conceptual process involved in the Financial Management Function and the organisational role of the Finance Manager. We may also briefly comment on the emerging profile of the Finance Manager. The changing functions of the Finance Manager, in the past, have been influenced by the pressures of the external environment like pace of technological advancement, squeeze on profit margins, greater opportunities for entrepreneurial activities and the growing size of the modern corporation. Therefore, there has been a shift of emphasis in the Finance Function which in turn has contributed to a change in the role of the Finance Manager. The emerging profile of the Finance Manager will also be conditioned by the environmental pressures and characteristics and of course the local exigencies encountered by an enterprise from time to time. Our environment is now, and, in the future, will be, characterised by the following:

First we live and are likely to live in a World of complex and rapid change. Business decisions have to be taken fast. Decisions relate to a number of issues. Decisions transcend beyond the present into the future short and long run. Decisions are inter-related and also inter-disciplinary.

in character. In short, decision making is complex, dynamic, inter-twined
and inter-disciplinary. Decisions have to be taken within decreasing
reaction of time.

Fourth, in our environment, unless there is a major change in the
political and economic philosophy, the commanding heights of the
economy will continue to be in the hands of the State.

Keeping the above tendencies in view, the emerging profile of the
Finance Manager will include a wider range of services like:

(a) electronic data processing;

(b) effective liason with the Government on major and may be even
minor financial problems concerning enterprise;

(c) making use of quantitative methods in management decision
making and in the financial management of enterprise and pro-
moting computer based operations;

(d) accepting and promoting the idea of increasing decentralisation
of the Finance Function to facilitate speedy decision
making.

Second, in the past finance was considered as a part of the broader
discipline of ECONOMICS, and studies on the art of business finance have
always sought recourse to the science of economics. Eventually, corpo-
ration finance has emerged as a distinct discipline with a standing of its
own in the Academic and Business World. And today, quantitative
methods are slowly being accepted as a necessary evil part of corporate
finance. In the Western Countries, particularly the USA, Quantitative
Methods form an integral and rather important part of corporate finance.
The day is not far off when our environment may compel or demand the
use of quantitative methods in answering the problems in managing
the finances of an enterprise. Quantitative Methods will ultimately
dominate the field of corporate finance. It is a question of time but no
denial to the Operations Researcher. This means another shift in the
emphasis of the Finance Function in the future. Corporation Finance will
meet the same fate as economics. Once upon a time statistics was a part
of economics. Eventually, economics became a part of statistics in view
of the increasing resort to statistical methods in providing answers to Economic Problems.

Third, the computer is a fact of life. In the future, it will be a more conspicuous fact playing an active role in the day to day chores of a manager. A constant interaction with the computer is therefore inevitable.
EXHIBIT-1 A

Exhibit One B shows the conceptual process involved in the modus operandi of the finance function. Thus:

Step A: Enumerates the Corporate Objective.

Step B: Converts Corporate Objective into a Corporate Financial Objective.

Step C: Says that Corporate Financial Objective is achieved by Wise Management of the Uses of Funds.

Step D: Shows Wise Management of the Uses of Fund in ongoing Investments.

Steps E/F/G: Show Wise Management of the Uses of Funds in Proposed Investments—Step F relates to Long Term Uses and Step G relates to Short Term Uses.

Steps H/I/J: Show Wise Management of the Source of Funds Step I relates to Short Term Sources and Step J relates to Long Term Sources.

The Financial decision making process presented in Exhibit 1B is subject to the various constraints encountered in our environment viz. capacity constraints (either licensing policy or production constraints), raw material constraints, price constraints (drugs price control order 1970 and similar controls on other industries) money constraints (developments banks and commercial banks), Foreign exchange constraints, infrastructure constraints like power supply and distribution, port capacity shipping space and services, wagon supply and movements, industrial relations and various legislations like Income Tax Act, Companies Act, Foreign Exchange Regulations Act and Monopolies Restrictive Trade Practices Act. The Finance Manager has to strike a delicate balance between the internal and external environment of the firm.
<table>
<thead>
<tr>
<th><strong>EXHIBIT TWO</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>FINANCE DIRECTOR</strong></td>
</tr>
</tbody>
</table>

| **(A)** FINANCIAL ACCOUNTING |
| **(B)** COST ACCOUNTING |
| **(C)** TAX ACCOUNTING |
| **(D)** PROJECTS MANAGEMENT OR CAPITAL BUDGETING (including liaison with term lending institutions like ICICI, IDBI, IFCI, LIC, UTI and SFC's and Agencies concerned with pricing and procurement of funds like Controller of Capital Issues, Stock Exchange Authorities and Commercial Banks) |
| **(E)** BANKING AND FUNDS MANAGEMENT (Liason with Agencies concerned with Procurement and Pricing of Funds viz. Controller of Capital Issues, Stock Exchange Authorities and Management) |
| **(F)** MANAGEMENT ACCOUNTING |
| **(G)** AUDIT AND SYSTEMS MANAGEMENT |
| **(H)** ELECTRONIC DATA PROCESSING |

- Receivables
- Payables
- General Ledger
- fixed Assets
- Building
- Payroll
- Shareholder Reporting (Companies Act 1956)
  - Cost Records (VOLUNTARY) AND/OR
  - Cost Records for Cost AUDIT (S209) (iv) of Companies Act
  - Tax Planning
  - Tax Liability Assessment
  - Tax Returns Filing
  - Personnel Personal Tax Planning
  - Sales Tax Identifying Tax Impact of various Alternatives
- Product Costing (ATTENTION DIRECTION)
- Internal Audit
- Systems Audit
- Management
- Services
- Decision Making [PROBLEM SOLVING]
NOTE TO EXHIBIT TWO

1. Function (A) i.e. Financial Accounting is usually vested in a Chartered Accountant, although experienced accountants having just high school education are not unknown.

2. Function (B) i.e. Cost Accounting is preferably vested in the cost accountant, although B. Com. or M. Com. with costing knowledge are also given a chance.

3. Function (C) i.e. Tax Accounting is vested in a Chartered Accountant or B. Com/M. Com. preferably with a thorough knowledge of ‘LAW’ and special professional skills in Tax Management.

4. Function (D) i.e. Projects Management OR Capital Budgeting is given to a person having professional skill and necessary expertise in Capital Budgeting. In practise a people with different discipline are given this function in different enterprise. Thus, economists, graduates in business schools and professional accountants, engineers are found handling this portfolio.

5. Function (E) i.e. Banking and Funds Management is usually vested with professional accountants or graduates from business schools.

6. Function (F) i.e. Management Accounting is performed well by persons having professional training in the specific function of management accounting. It is given to Chartered Accounts/Cost Accountants and in many cases to professionals trained in business schools.

7. Function (G) Audit and Systems Management is taken care of by Chartered Accountant or a B. Com/M. Com. Systems Audit is taken care of, again, by Chartered Accountants. Graduates from Business school and those with professional training in systems management are also being increasingly vested with this function.

8. Function (H) i.e. Electronic Data Processing is vested with professional skills in computer science. Professional accountants with professional training in computer management, or business school graduates specialising in computers/quantitative methods operations research, or statisticians/mathematicians with professional skills and training in computers handle this portfolio.
9. Management Services are vested in the hands of persons with professional knowhow of MANAGEMENT.

10. The Finance Director is usually a Chartered Accountant or a professional with a proven track record and experience in the field of FINANCE. There are at least a few cases where engineers or statisticians with professional knowhow of Finance head the Finance Function.
### EXHIBIT THREE
#### A PROFILE OF DIFFERENT FUNCTIONS

<table>
<thead>
<tr>
<th>Function</th>
<th>Whether Mandatory or Voluntary</th>
<th>Nature and Timing of information needed</th>
</tr>
</thead>
<tbody>
<tr>
<td>A Function</td>
<td><strong>Mandatory</strong> per Company Law.</td>
<td><strong>Historic Costs/Revenues</strong> i.e. <strong>Actual Costs and Actual Revenues.</strong></td>
</tr>
<tr>
<td>Accounting</td>
<td>Formats prescribed per S.211, Schedule VI, of Companies Act.</td>
<td></td>
</tr>
<tr>
<td>B Cost Accounting</td>
<td>a) Mandatory for Companies producing select list of products. [S.209(1) (d)] of companies Act.</td>
<td><strong>Historic Costs/predetermined Costs with emphasis on progressive evolution of STANDARD COSTS.</strong></td>
</tr>
<tr>
<td></td>
<td>b) Not Mandatory for products not within the purview of S.209 (1) (d) of Companies Act.</td>
<td><strong>Standard Costs/Actual Costs.</strong></td>
</tr>
<tr>
<td>C Tax Accounting</td>
<td><strong>Mandatory</strong> par S.211 of Income Tax Act 1961.</td>
<td><strong>Projected or Estimated Revenue, Costs and Profits to compute Tax Liability.</strong></td>
</tr>
<tr>
<td>D Project Management or Capital Budgeting</td>
<td>Obligatory if negotiating loans with Financial Institutions (ICICI, IDBI, IFCI, UTI, LIC, SFC's)</td>
<td><strong>Historic Economic performance and projected Economic Performance with emphasis on profitability and Liquidity.</strong></td>
</tr>
<tr>
<td>E Banking and Funds Management</td>
<td></td>
<td><strong>—do—</strong></td>
</tr>
<tr>
<td>F Management Accounting</td>
<td><strong>Voluntary</strong></td>
<td><strong>Projected Costs and other data/Actual Cost aid management and other data in the smooth conduct of business.</strong></td>
</tr>
<tr>
<td>G i) Audit</td>
<td>Internal Audit (Mandatory per 1975 MAOCARO)</td>
<td><strong>Historic Data and details of Records Specified.</strong></td>
</tr>
<tr>
<td>ii) Systems</td>
<td><strong>Voluntary</strong></td>
<td><strong>Overall information about information systems.</strong></td>
</tr>
<tr>
<td>Management</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
NOTE:

* Historic Costs are actual costs based on ex post events and are accurate.
* Standard Costs are scientifically Predetermined Costs.
* Estimated Costs are Predetermined Costs.
* Predetermined Costs are costs computed in advance and may or may not be Scientific.