TYPES OF ACCOUNTING SYSTEMS

The cost accounts described in the previous sections provide only one of the various components in a financial accounting system. Before further discussing the use of cost accounts in project control, the relationship of project and financial accounting deserves mention. Accounting information is generally used for three distinct purposes:

• Internal reporting to project managers for day-to-day planning, monitoring and control.

• Internal reporting to managers for aiding strategic planning.

• External reporting to owners, government, regulators and other outside parties.

External reports are constrained to particular forms and procedures by contractual reporting requirements or by generally accepted accounting practices. Preparation of such external reports is referred to as financial accounting. In contrast, cost or managerial accounting is intended to aid internal managers in their responsibilities of planning, monitoring and control.

Project costs are always included in the system of financial accounts associated with an organization. At the heart of this system, all expense transactions are recorded in a general ledger. The general ledger of accounts forms the basis for management reports on particular projects as well as the financial accounts for an entire organization. Other components of a financial accounting system include:

• The accounts payable journal is intended to provide records of bills received from vendors, material suppliers, subcontractors and other outside parties. Invoices of charges are recorded in this system as are checks issued in payment.

Charges to individual cost accounts are relayed or posted to the General Ledger.
• Accounts receivable journals provide the opposite function to that of accounts payable. In this journal, billings to clients are recorded as well as receipts. Revenues received are relayed to the general ledger.
• Job cost ledgers summarize the charges associated with particular projects, arranged in the various cost accounts used for the project budget.
• Inventory records are maintained to identify the amount of materials available at any time.

In traditional bookkeeping systems, day to day transactions are first recorded in journals. With double-entry bookkeeping, each transaction is recorded as both a debit and a credit to particular accounts in the ledger. For example, payment of a supplier's bill represents a debit or increase to a project cost account and a credit or reduction to the company's cash account. Periodically, the transaction information is summarized and transferred to ledger accounts. This process is called posting, and may be done instantaneously or daily in computerized systems.

In reviewing accounting information, the concepts of flows and stocks should be kept in mind. Daily transactions typically reflect flows of dollar amounts entering or leaving the organization. Similarly, use or receipt of particular materials represent flows from or to inventory. An account balance represents the stock or cumulative amount of funds resulting from these daily flows. Information on both flows and stocks are needed to give an accurate view of an organization's state. In addition, forecasts of future changes are needed for effective management.