Management accounting

Finance

Question One: The economies of Europe and that of America experienced a financial crisis because of too much liberalization of their economies. The European Union and the United States government advocated for a free market economy. The definition of a free market economy is rather an ambiguous concept. This is because it is used to refer to a variety of issues in an economy. For example, a free market economy is used to refer to a market whereby there isn’t any government regulation (Atrill and Mclaney, 2012). In other circumstances, a free market economy refers to a market where by the prices of goods and services are controlled by the laws of supply and demand. A free market economy can also be used to refer to a market which does not have a monopoly. Proponents of a free market economy have made a mistake in advocating for an economy which is free of regulation as the best method of economic governance. This is because the free market economy failed to prevent the occurrence of the financial crises in Europe and the United States. It is important to denote that markets is a social institution, and therefore markets cannot act, but it is the behavior of the people within the market that will affect the market under consideration (Atrill and Mclaney, 2012). It is therefore important to regulate the behavior of people so that they do not destroy the economy of a state. For instance, the economic crisis in America was precipitated by the failure of the mortgage system in America (Bhimani, 2012). People took too much money for mortgages, leading to a rise in value of properties. However, they were unable to pay back the mortgages because of their high interests. Had there been laws to regulate the lending behavior of banks, and individuals, this crisis would not have happened. Question Two: Positive accounting theory refers to an academic research in the field of accountancy which tries to

explain and predict actual accounting practices. Positive accounting theories try to give an explanation on why certain accounting procedures and practices are popular, as opposed to other accounting policies and procedures (Bhimani, 2012). This concept of positive accounting theory was developed to give a better explanation on how best to use certain accounting concepts and practices. Positive accounting theory has three main criticisms, and they are (Atrill and Mclaney, 2012); Positive accounting theories do not have a provision for any prescription, nor does it state what is supposed to happen. They only predict and explain what would happen. This is the main aim of positive accounting and it is therefore not sufficient to explain various concepts of accounting. Positive accounting theory is not value free, and this is because it only predicts and explains what individuals might do, without giving an explanation on what individual should do for purposes of solving a financial/ accounting problem. Positive accounting theory makes an assumption that every agent (managers) and principal (owners) have an interest in benefiting themselves, as opposed to the organization. The main interest of the agent and principal is to maximize wealth, without putting a consideration on the adverse effects of their actions. These criticisms of positive accounting theory are right. This is because positive accounting theories can lead to the alienation of accountants. This is because they do not provide a prescription to a certain accounting problem. The assumption that an agent and a principal are concerned with their own selfish interests, without considering the consequences of their actions is false. This is because many institutions consider their environment of operation before enacting policies. Question Three: In the capital market, allocation of assets is amongst the most

important decisions that are related to investments. Investing in these markets is very risky, because of a variety of factors and therefore there is a need of an appropriate analysis of the capital market. A number of firms have emerged which are responsible for providing information and solutions to investors in regard to capital market investments (Atrill and Mclaney, 2012). On this basis, the main assumption in regard to capital market research is that it is very risky to invest in a capital market, and therefore investors need information that can help them in making informed decisions. Capital market research deals mostly with gains made in numeric terms. Behavioral accounting on the hand involves the integration of key stake holders of an organization into the decision making process. This method of accounting research helps analysts to identify and analyze how the behavior of an individual will affect the organizations value. On this basis, the key assumption that behavioral accounting method makes is that the human factors play a role in the valuation of a company (Bhimani, 2012). Behavioral accounting research and capital market research differ considerable in the manner in which they explain human behavior in relation to business or investments. Take a hypothetical example of two companies, A and B. If company A has a more experienced staff, and good managerial capability, as compared to B, and then in accordance to behavioral accounting, company A is more profitable than company B. In regard to capital market research, if company A makes profits as compared to company B, regardless of its managerial practices, and work force, then company A is more valuable than company B. Capital market research denote that investors are more concerned with figures, as opposed to human behaviors. Bibliography: Atrill, P., & McLaney, E. J. (2012). Management accounting for decision makers (7th

ed.). London: Pearson. Bhimani, A. (2012). Introduction to management accounting. Harlow: Financial Times Prentice Hall.