



by Simon Dekker

President and CEO – Dekker, Ltd.

The following represents a summary of my personal views on management accounting for the future and some opportunities for Cost/Schedule Control Systems Criteria (C/SCSC) to flourish in the commercial business sector.

World Competition and History of Management Accounting

From 1920 to about 1970 there was no competition that could match the economic might of the U.S. Traditional accounting practices focused on maintaining information associated with outside reporting to owners, creditors, investors, and the IRS. The basis for reporting was mostly weighted on labor, with cost collection points that centered about general accounting practices that did little to accumulate day-to-day operational data to help managers make decisions. Bottom-line profit and loss statements were the focus throughout this period, and academia dedicated itself to providing an army of professionals who were taught rigid financial practices directed solely at the outward appearances of a business unit, not the internal operation. The executive perspective was to enable a company to grow, and to compile and report information pertinent to that goal. Short-term profit statements to induce capitalization was key. To an overwhelming degree, that philosophy still remains the same. It has become ingrained into the culture.

From the industrial revolutions to the 1920s, the purpose of the financial system was to derive profitable product pricing information. The process of taking raw materials through its product conversion process was articulately monitored to derive a product's cost, a profitable consumer price, and profitability margins to calculate Return On Investments and performance. Process conversion data to produce a product was much easier then because a typical business unit maintained a narrow discipline and it was, no doubt, easier to compile and report the detailed cost information. An example of companies using price cost collection methods of the period were DuPont Powder, Winchester Rifle, and AT & T. Management cost accounting associated to the internal operation permeated to various other industries that included textile mills, steel mills, railroads, ship building and construction.

Around 1915 to 1930 companies began to emerge that were multidimensional with regard to their business disciplines. They would incorporate each conversion process to produce a product, take care of the distribution channels, warehousing, and retailing. Combining these operations into one conglomerate required fund. The mission of the financial system was to promote an organization for the purpose of raising money and methods were derived that became standardized and picked up by academia as the Generally Accepted Accounting Principles (GAAP). When Income Tax was initiated by the government, it used GAAP as a model and those principles became even further entrenched into the finance culture.

In the late '60s and early '70s competition for the American market place grew. There appeared to be some form of magical management techniques that enable companies to literally take over market niches that were traditionally dominated by the U.S. The take over transpired in small manufacturing at first, then permeated to the automotive, electronics and service industries. Today, even commercial aviation is threatened from abroad. Their foreign enterprises placed more consideration on their ability to plan. Focus of their management information systems returned to product pricing and the internal product conversion process. Most of the cost disciplines used by American firms at the turn of the century were exported to foreign business

enterprises, refined and used to cover every aspect of an operation associated to the deployment of a product. Instead of focusing on labor as a primary cost driver, each sub-process within the manufacturing and marketing of a product was closely tracked and rolled up so that suitable reporting could be performed along all levels.

This form of strategic cost collection associated to the process flow of product deployment continues today and is just starting to surface within American business units. All ramifications concerning a product are considered, from customer service back to engineering and design. Marketing, administrative, sales, distribution, production, and deployment “events” are considered to be the cost drivers in the modern financial system. These events cover the entire life cycle of a product and provide cost and resource information relative to the operation. Each individual product has a simple life cycle chain of events that can be tailored to incorporate events that represent strategic cost drivers to a particular product’s life cycle. The life cycle of events become budget collection points for labor, material, other direct charges, and any attribute that might effect the product cost of sales. These budgets are then tracked to provide product conversion cost models for future reference, and historical cost performance data describing product profitability in the field. Each product offering is measured separately for accurate cost history and profitability assessments. The American accounting industry refers to this form of management costing as, “Activity Based Costing.” It is no way intended to replace GAAP, as general accounting in its current form is very important. ABC is intended to fill a missing link in finance to help business units compete in a world market oriented economy. Strategic planning tied to the official book of record is now becoming very “fashionable,” especially to high tech firms where large capital expenditures are necessary to deploy products to the marketplace. In high tech, it would be pointless to seek financial profit and loss statements on a monthly basis for a product that might not exist for years; yet, a means to determine accomplishment against business-oriented objectives is necessary within the Management Information System portfolio. Keeping in synch with the required plan, in terms of cost and deployment schedules, is key to obtaining the best Return On Investment profile. Consider a Biotech or Pharmaceutical company that invests millions of dollars in research before the first influx of monetary reward is realized. In high tech, it is important that the corporate goals and objectives are understood by all performing entities regardless of their discipline.

In summary, general bookkeeping of a company has evolved little since 1920 in the U.S. The “no competition” environment enabled cost collection practices to proceed without much formal regard to the internal planning and monitoring of performance. Middle and lower managerial structures within business units were left to their own devices to monitor progress against business objectives. In most instances, the wealth of information compiled within an organization’s financial system was, and still is, seldom accessible by strategic planners. Few financial professionals truly understand the needs of technical performing entities and no formal mechanism has been established to compile, process and report financial information in a manner that is useful to planners.

Where Cost/Schedule Control Systems Criteria (C/SCSC or C/S) Fits

C/SCSC is celebrating its 25th anniversary. It was developed by the Air Force to help monitor contract cost and performance for large scale system acquisitions. While commercial accounting professionals are striving to define a standardized approach to facilitate cost planning and performance , a well defined methodology via C/SCSC evolved. The accounting industry is currently trying to define various aspects of ABC that the criteria already establishes.

C/S is a sound approach to a standardized method of establishing and tracking against a project’s plan. In C/S, it would be relatively simple to initiate a Work Breakdown Structure incorporating all phases of a product life cycle. The Organizational Breakdown Structure would simply be department and sub-contractors associated to a product, as it would be for a government contract. Cost information would be compiled with the desired association to the operational aspects of product conversion and deployment. If a contract can be monitored via C/S by the government, then it should be able to handle commercial capital projects as well.

Though it was conceived for government contracts, there is no reason it could not be used in conjunction with GAAP for commercial use, once a few deficiencies are resolved:

- C/SCSC has a bad image commercially. It is considered to be a government reporting REQUIREMENT. It is seldom implemented as a strategic goal of a company. When a company wins a contract, the discipline is acknowledged by management. As time progresses, and with certain enhancements oriented toward a commercial business unit, a simplified version of C/SCSC is implemented accommodating commercial needs.
- C/SCSC must become adopted by academia. Currently, C/SCSC is closely held and there is a great misconception that it is difficult to do and is costly to implement. This misconception is based upon the fact that only an expert can implement it. This philosophy benefits C/SCSC culturalists, but not the general acceptance of C/SCSC as a strategic part of any MIS. If the discipline is to flourish, it must be taught in all accounting, business administration, and technical curriculum as the standard to plan and track capital projects.
- C/SCSC must become a part of GAAP. Trade associations in program control and project management must affiliate themselves with trade organizations for accountants to establish a continual dialogue.
- Scheduling techniques, especially the Summary Stacked Linked Activity Method of scheduling, must become incorporated as part of C/SCSC. In addition, traditional Critical Path Method of scheduling needs to be considered as well.
- A method to disclose profit and loss must be incorporated into the criteria to show owner information associated to a product's life cycle. Trade associations should focus on this issue if C/SCSC reports are to be adopted by a company's executive management committee in support of enterprise and work group oriented disciplines.
- Technical Performance Measurement to track information associated directly to product parameters in support of commercial market influences and built-in obsolescence goals is urgently needed. This information would be used to predict future product enhancements and release points from a marketing point of view and to keep technical entities abreast of market driven influences on a product from sales in the field.

If these issues can be overcome, C/S will become the standard for Activity Based Costing. There is a pinnacle of opportunity for all C/S professionals to ensure that the discipline is widely understood and promoted not just in government contracting, but also with commercial ventures. C/S needs to be made simpler, not harder. Implemented correctly, C/S can help companies focus on products that perform well in the market place, and to discontinue products that do not.