Accountancy in the Control of Chain Stores

By Edgar R. Scherich

This paper is written in an effort to contribute constructively to the progress of chain-store merchandising and especially to a greater reliance on the accounting function in business to furnish the material through which the executive control is maintained and expanded. It is not submitted as a definite programme for any group of chain stores, but it has been evolved from a close investigation and study of one group of retail grocery stores which has been continuously successful for more than a quarter of a century, and it is, therefore, only a short step to specific application. This is, in fact, an adaptation of an accountant's report which was written to meet specific conditions, and those paragraphs relating exclusively to fundamental theory and accepted practice are retained as forming an excellent background for the presentation of the ideas concerning the individual chain grocery store.

In discussing this matter of progress, one cannot do so intelligently without, consciously or unconsciously, creating a vision of the future and holding it up before one's eyes as the goal of tomorrow or next year or even of the next decade. If one knows the results for which he is striving, he can make straight-line plans to obtain those results. On the other hand, if one has no clear cut vision of the future there can be little real planning and that without coördination.

Vision and creative imagination constitute the first element that will always be found in any large success, in the building of any great organization or in the creation and maintenance of an outstanding business. Attention is called to this one of six great factors in the success of any business enterprise because it is desirable to keep this factor in mind throughout the reading of this article, and because on the exercise of vision and creative imagination, more than on any other thing does the value of accountancy depend when applied specifically. Accountancy is to the planning executive what powerful binoculars are to eyes striving to pierce the veil of distance.

Business men too often little appreciate the real value of accountancy as rightly applied, maybe because accountants themselves do not see nor understand that value. Too often accountants lack that vision of the man who is looking forward to new and to better things and try to prescribe accounting according to some well known and time-honored custom. Is it not the accountant's province in the business world to walk side by side with the business organizer and manager, get and keep his point of view, aid his enterprise and refrain from casting in his path the stumbling blocks of custom? Surely the accountant should be as well trained in the elements of business success and as able to recognize the various factors of success and failure as the management. If he lacks vision, or is in any way doubtful concerning the rules for failure or success, then neither he nor his department can ever be worth much to management. At best he can only serve (a) to establish the financial position of the company and (b) in some poor measure to protect and safeguard its assets.

However, in the modern conception of the entrepreneur, these two primary objects of accountancy are greatly overshadowed by a third, (c) control of operations. Of course volumes have been written in the discussion of each of these objects. Each has been the subject of countless interpretations and it is not the purpose of this paper to enter into any discussion of these objects except to point out their relative importance to management.

Establishment of financial position and earnings record of an enterprise is important, and ever will be, because through it one determines the extent to which it is subject to that other element of business success, ample financing. However, if accounting were confined to this object alone, the effort expended in attaining it would be comparatively light.

It is the second of these objects, protection and safeguard of the company's interests, on which business men and accountants in the past have centered their efforts, often to the introduction of greatly complicated systems and burdensome routine. In a great majority of accounting cases, energies have been directed against theft and misappropriation of money. Very often they have overlooked the equally important safeguarding of other assets such as inventories, accounts receivable, working assets, et cetera. Today, management wants to know that all assets, whether cash, goods, choses in action or fixed property, are adequately protected against dishonest and disloyal employees. But still further, management is now interested in protection against carelessness and inefficiency, and in conserving the company's interests of whatever nature, tangible and intangible, against waste.

Intelligent control through records is the third and most important object of accounting and another of the six outstanding elements of business success. It is in the development of this object of accounting that progress has been sadly lacking; the business man and accountant alike seem little to realize the mighty tool which they have in their hands for constructive work.

Failure to take full advantage of accounting to exercise intelligent control of operations can almost always be traced to a lack of effective planning. With a little vision and constructive imagination, when once results to be obtained are clearly seen, it is a comparatively simple matter to work out the system that will give the utmost in effective control. The general plan of operations should include accounting as an integral part rather than as something separate or detached. And both routine and personnel should be subordinated to the general plan rather than the plan to either special routine or the conflicting whims of the various people charged with the execution of the plan.

In a majority of cases, accounting systems grow with the business and development is the result of fitting or refitting the system to meet some prescribed routine. One must understand management's aim in business, its point of view and then develop the results that are expected or desired and the methods to be used. With a clear-cut picture of the future in mind, with desirable results standing well outlined in the foreground, one can make a survey of the available methods and routines that may be followed to secure such results and determine the relative costs of methods and routines in comparison with results to be obtained. Under this procedure methods and materials are subordinated to the end in view, and management does not take the risk of having inadequate accounting.

What Management Should Expect of Its Accounting

In order that the reader may estimate the value of his own accounting system, or of any accounting plan which may be contemplated in his business, the following catalogue of reasonable requirements, all based on fundamental theory of management and proven in practical application, is submitted. By this catalogue he may ascertain if he is obtaining from his own accounting plan that which he has every right to expect.

1. Segregation or grouping of accounts to aid functional control;
2. Automatic revelation of the unusually good and the unusually bad features of operations;
3. Exact accounting for all money, goods and property; placing a definite responsibility and accountability on some individual for both tangibles and intangibles;
4. Instant comparison of receipts and expenditures by days, months, years, with standard performance and with representative performance;
5. Furnishing instantly statistics which reveal the efficiency or inefficiency of employees;
6. Furnishing sales statistics which reveal customer preferences and the buying habits of the communities;
7. Furnishing statistics on all relative matters, both internal and external, which may be used or wanted as a guide in the executive control of the business;
8. Providing management with statements of operations, within the shortest time after the close of the period, without creating an excessive or peak load in the accounting department near and at the close of the period, such statements to reveal excellent and poor or indifferent showing, without the necessity of going through a lot of detailed statements, and, at the same time, to reveal the causes;
9. Securing the desired results economically without friction or unnecessary burden on the part of producing departments;
10. Providing standard practice instructions to guide employees in all financial and record transactions and to place definitely the responsibility of employees for money, goods or property over which they exercise control.

This catalogue does not list everything that should be expected of a modern accounting plan. Other things, which have been omitted, are probably much better recognized than the ten enumerated here. These ten, however, have been chosen because they are the connecting links between accounting and control of business management. While these ten requirements are readily accepted and easily understood, it is in their interpretation and practical application that skill and special knowledge are required.

A further analysis of these ten requirements reveals that they can really be boiled down into five principles of scientific management. Or, putting it another way, the ten reasonable requirements listed are the exponents of five principles of management. These principles are: (a) functional control; (b) accountability; (c) attention to the unusual; (d) conservation of executive time and labor; (e) education.

Before discussing any of these principles as applied to chain-store retailing, it is well to make it plain that an accounting plan may function perfectly and fulfill every one of the requirements listed yet utterly fail of utility because the management fails to take action upon the information obtained through the operation of the accounting plan. Accounting is a wonderful tool in the hands of an experienced and skillful workman, but it does nobody good unless it is working constructively. Prompt and decisive action will insure maximum results. Only unfailing good judgment will guarantee that those results are the right kind.

Functional Control

The old military system of straight-line control, the system whereby all initiative originated at the top of the line of authority and passed by successive stages downward until it finally came to rest with the laborer who actually performed the operation, is fast disappearing from the field of large business operations. In its place has come a system which has been characterized as "functional control." This new system involves division of labor and emphasizes the advantage of training to do one job and do it well over the unrestrained effort to handle many jobs at one time. It requires that operations shall be controlled by functions rather than by departments, and that functions be coördinated by the chief executive or by an executive committee. This system permits the use of special knowledge in the control of every function which it was not possible to use effectively under the military type of control.

The functions of retail grocery stores may be divided into primary and secondary. These functions are there whether they are exercised as such or not and whether the old line or new system is in practice. It is possible that some of the secondary functions are not yet always developed, but therein lies opportunity for progress.

The primary functions are (a) purchasing, (b) warehousing and (c) selling. The secondary functions are (1) transportation, (2) advertising, (3) display, (4) location of stores, (5) rents, (6) property, fixtures, arrangement, (7) personnel, (8) office management, (9) accounting. There is, of course, the function of management, which is not listed as either primary or secondary but is a function nevertheless. It is the coördinating influence which presides over all other functions. There is also the function of finance which might be considered as both primary and secondary.

It is impossible to separate these functions, because there is often no visible line of demarcation between functions. Consequently functional control demands team play and the coöperation of all workers. For instance, the personnel function invades all departments and every other function; office management includes the control of all office workers and office routines whether attached to purchasing, selling, accounting or other function; and accounting controls the gathering of figures regardless of what other function is concerned with them. Functional control does two things—first, it uses special knowledge or skill to govern every transaction and, second, it requires team play and consultation among all executives.

Control Through the Use of the Unusual

George Horace Lorimer in his "*More Letters from a Self-Made Merchant to his Son*," writes:

> "In the first place, you don't need to bother very much about the things that are going all right, except to try to make them go a little better; but you want to spend your time smelling out the things that are going all wrong and laboring with them till you've persuaded them to lead a better life. For this reason, one of the most important duties of your job is to keep track of everything that's out of the usual. If anything unusually good happens, there's an unusually good man behind it, and he ought to be earmarked for promotion; and if anything unusually bad happens, there's apt to be an unusually bad man behind that, and he's a candidate for a job with another house."

The principle here laid down is so self-evident that further discussion would be a waste of time. The practical application of this principle is the task of the accounting function. It is the work of the accounting function to determine the unusual in all departments of the business and to present the facts in concise statements to the management.

Before anyone can determine the unusual, it is first necessary to determine the usual. In cost accounting, this is spoken of as setting a standard or applying standard costs. In commercial accounting, it is spoken of as budgeting. The idea is to find out what normal conditions are and what revenues and expenses should be under normal or probable conditions. This entails a great deal of careful planning on the part of accounting officers and still greater study and analysis on the part of operating officers, but the results of careful planning, study and analysis are well worth all the effort given to them.

When a standard scale of operation is set up for every function, going into sufficient detail to separate conflicting factors, it is then a comparatively simple matter to establish actual accomplishment and compare it with the standard. It is in this process of comparison that the unusual appears, and when the accounting plan is properly drawn the process of picking it up for executive attention is automatic.

Standard performance is supposed to be the best possible showing that can be made. It is not, however, the only basis of comparison that is possible or desirable. In fact the usual basis for comparison is past performance. Comparison with past performance ignores altogether the quality of the performance, and the tendency is to rejoice over any improvement when the probabilities are that the improved performance compares unfavorably with what the performance should have been.

There is another basis of comparison, especially effective in the control of chain stores. This is the comparison of actual performance with representative performance. In fact this comparison has much more psychological value than comparison with standard performance. Representative performance is flexible, which is both a merit and a fault. The tendency to error in its use is eliminated only by the use of good judgment in its application. On the other hand, good judgment may suggest variations which are helpful to meet existing psychological conditions.

Accountability

Too frequently one sees executives who demand an exact accounting in all money matters, sometimes displaying harshness and evidence of suspicion, but on the other hand never think of requiring an accounting for merchandise. Consistency is always a desirable quality in management. In the case of accountability it is not only desirable but necessary. What good is there in locking the cash register and leaving the store filled with merchandise open to all kinds of carelessness, theft and manipulation?

It is not enough, therefore, for accounting to trace merchandise into a retail store in the terms of money, drop there its surveillance, and jump to the cash register, leaving the merchandise in the store to take care of itself. That gap in accounting control must be filled and it is by no means an easy thing to do. Especially is this true where sales records must be kept by the selling force, as is the case in the retail grocery store.

Of the methods already developed for control of merchandise operations within the retail store an elaboration of the gross-profit method seems to be the only one giving the desired results with the economy desirable in this kind of store.

In mass selling, theoretical gross profit is never realized. Marking up 33⅓% over cost represents 25% on sales. At the end of a period the seller takes stock, finds only 20%, or perhaps 22%, is realized and becomes conscious of the fact that somewhere there has been a loss of from 3% to 5%, which may be as much as the net profits. If this invisible loss could be saved in many cases the net profits could be doubled. But unless one can put his finger on the factors which cause this often invisible shrinkage, efforts to reduce it will probably be of little avail.

It is, therefore, necessary to determine and classify the factors involved and to keep accounts with as many of them as possible. The following classification will serve for the present discussion as it may be used to explain any loss in gross profit which may occur from the time the goods leave the warehouse, or direct delivery by manufacturer or producer, until the money representing the sale price of the goods is deposited in the company's depository.

1. Errors in pricing and extending:
   - (a) Warehouse requisitions,
   - (b) Invoices for direct store deliveries.

2. Errors in charging:
    (a) Warehouse requisitions,
    (b) Invoices for direct store deliveries.
3. Losses in making change.
4. Destruction of merchandise:
    (a) Breakage, spillage and tare,
    (b) Shrinkage, spoilage and evaporation,
    (c) Obsolescence and deterioration.
5. Price changes—authorized:
    (a) Declines—showing a loss,
    (b) Advances—showing a gain.
6. Special sales—authorized.
7. Special sales—unauthorized:
    (a) Where credit is extended to make a sale,
    (b) Where price is cut to make a sale,
    (c) Where sales are made to "friends" at unauthorized prices.
8. Theft of merchandise:
    (a) By driver of truck,
    (b) By store employees,
    (c) By store manager,
    (d) By customers,
    (e) By strangers when store is closed.
9. Theft of money:
    (a) By store employees,
    (b) By store manager,
    (c) By strangers.

The contribution of the factors under groups 1, 2 and 3 to the invisible loss in merchandising can be nothing but negligible, unless there is a deliberate attempt to hurt certain store managers or on the other hand to make a favorable showing for certain managers at the expense of other managers. Either is a possibility, but the probability is remote. Errors which are not deliberate will not be confined to any one store or group of stores and it will be found that the "overs" will almost surely compensate the shorts. So, unless there is something definite pointing in this direction, these factors may be eliminated from consideration.

It is not meant, however, that precautions should not be taken to prevent unintentional errors of the nature indicated nor to be sure that such errors are not being made intentionally. This should be on the audit programme of the organization's internal checkers as well as on the programme of the outside accountants.

It is possible to account definitely for the factors grouped under classes 4, 5 and 6. In fact, if one is to accomplish anything in the control of invisible loss such accounting is imperative. Economy and expediency require that the store managers themselves supply information on forms regularly supplied for the purpose. The fact that store managers themselves are interested parties does not condemn the procedure, for it is still possible to obtain reasonable accuracy in these reports and to detect those that have been deliberately manipulated. Here, more than anywhere else in the accounting, is the need for comparison with standard and representative performance demonstrated. Without such comparison one is unable to learn what he should expect. With it one will be able to identify managers who have been careless about destruction of merchandise or are deliberately falsifying their reports.

Let us suppose that in a group of 100 stores fifteen show something out of the ordinary in their reports on factors grouped under 4, 5 and 6. The accounting department, either through its own workers or through the stores-supervision department, should immediately institute a check on these fifteen stores, and no matter what may be the conditions in an individual store there are methods available whereby the factors in probably 90% of the cases may be definitely determined. As previously pointed out, it is only those with unusually bad showing that have to be considered.

The great majority of people are honest and one may reasonably assume that store managers are as honest as other folk. Therefore, if honesty were the only reason for a good showing with regard to any of the factors listed under groups 4, 5 and 6, the representative performance of the two-thirds of managers who have the best showing may well be considered as the measure of honesty one has a right to exact of all managers and proceed to bring the other one-third up to that average. But there are other reasons which have substantial effect. Two of these reasons are sure to be much more prevalent than lack of honesty among managers. They are carelessness and inefficiency. Managers who are absolutely honest may be very careless and inefficient. Therefore, all the factors listed under group 4 should be controlled by comparison with standard performance rather than with representative performance, because representative performance does not set up a true gauge of efficiency.

Factors listed in group 7 are not in themselves dishonest. They are, nevertheless, contrary to good policy, and the manager who consistently violates the avowed policies of the company for which he works is disloyal. No company can violate its published policies, however intermittently it may do so, and not lose some of its prestige. Therefore, losses from the factors in group 7 must be considered, from the standpoint of control, as resulting from disloyalty and dishonesty and they are to be treated as such. No other course is open unless the company acknowledge privately a policy inconsistent with its published policies and permit managers to report on these losses as they report on losses from groups 4, 5 and 6.

There are now left groups 8 and 9, which are losses attributable directly to dishonesty, whether of employees, customers or professional thieves and robbers. It has been determined that factors in groups 1, 2 and 3 exert no appreciable influence on the results of operations. Results of factors in groups 4, 5 and 6 are subject to a definite accounting. Therefore the dishonor factors, which must include group 7 as well as groups 8 and 9, can be pretty definitely weighed by first determining the extent of the gross-profit loss and then deducting therefrom the weight of accountable factors in groups 4, 5 and 6. With the weight of the dishonor factors definitely established there remains only the responsibility of the store manager to be worked out. The burden of this rests with the accounting function but by means of the process of elimination this is a relatively simple matter.

It is the duty of the accounting function to determine the factors resulting in loss, or bad showing, or the unusually bad, and the extent to which each factor has contributed. It is then the duty of management to determine the factors which will correct these unusual tendencies. Certainly as between accounting and management there is no longer any reason to be in doubt concerning the causes and extent of contributing factors of the heretofore invisible loss of gross profit; and the possible gains from the elimination of all or even a part of this loss are so large that there is no longer any excuse for not setting up the necessary machinery to effect its control.

Conservation of Executive Time and Labor

It seems that accountants, particularly public accountants, delight in throwing together a mass of figures in a more or less elaborate report and then wonder why the executive to whom it is addressed does not become enthusiastic about it. The answer is simple. The ordinary executive is not an accountant and in all probability is not trained in reading accounting statements. He can not readily visualize the figures that he finds on the pages before him. Unless the figures are translated to language that he understands he fails utterly to grasp the meaning of important features that are perfectly plain to an accountant. On the other hand, the executive may have had accounting experience and be perfectly capable of reading the most complicated accounting report or statistical compilation, yet it takes a lot of time and study to go through a large report and find the things that ought to come to his attention, and he finds that he must either curtail his attention to accounting reports or forego other duties that also seem important.

The gist of the matter is that the usual accounting report fails to satisfy, regardless of the fact that it may be a good report. One often wonders why the accountant so persistently holds himself aloof from the solution of this problem, when the answer for him is so easy.

There is probably no other business that lends itself so readily to executive control through the use of figures and properly prepared accounting statements as does the retail grocery chain. Certainly in no other business is it so easy to prepare statements which will conserve the time and energy of executives in getting at the essential facts.

So well known are the advantages of having all figures at the earliest possible time that it is unnecessary to comment on the proposition that the chain-store executive should have monthly reports covering the entire field of his company's operations. There will be reports which he will want and should get from day to day. But the monthly report will be the great instrument of executive control.

The following outline of a monthly statement is submitted as a starting point for a company operating one, two or more groups of stores:

1. Comptroller's interpretations and comments.
2. Detailed balance-sheet.

3. Condensed balance-sheet.
4. Summary of losses and gains.
5. Statement of losses and gains—stores group No. 1.
6. Statement of losses and gains—stores group No. 2.
7. Analysis of direct store expense—stores group No. 1.
8. Analysis of direct store expense—stores group No. 2.
9. Stores statistical report—group No. 1.
10. Stores statistical report—group No. 2.
11. Special stores gross profit report—group No. 1.
12. Special stores gross profit report—group No. 2.
13. Special stores expense report—group No. 1.
14. Special stores expense report—group No. 2.
15. Analysis of warehouse expense.
16. Analysis of truckage.
17. Analysis of supervision.
18. Analysis of administrative expense.
19. Special report of unusual expenses.
20. Turnover statement.

One of the important features in this outline is the page or two of interpretations and comments by the comptroller. If these interpretations and comments are concisely made, written as statements of fact only, but with references to authorities and arguments found elsewhere, and if they deal with the vital points in the reports which anyone not an accountant might miss, they serve as an invaluable aid to the executive, as well as a time saver. Some executives object to comments by an accountant on the theory that it is a reflection on the executive's own ability and an invasion of his prerogatives. It is held by some that the accountant, for purposes of harmony in the organization, must refrain from commenting on the figures, because it might offend the executives. However, if the comments and interpretations stay strictly within the realm of fact, even though reasonable conclusions are drawn from the facts presented, only the self-conscious executive would feel offended.

A feature of the condensed balance-sheet should be the addition of extra columns to show for each class of assets and liabilities the average per store. This is most useful in consideration of the financial structure and in keeping the investment per store at a minimum. It is also an effective guide in planning new stores.

Statements numbered 4, 5, 6, 7, 8, 15, 16, 17 and 18 should be presented in comparative form for periods, the current month being compared with the corresponding month of the preceding year and with the preceding month of the current year. The cumulated results to date should be compared with the results of the corresponding period of the preceding year.

Because of their intimate connection with the discussions of this paper suggested forms of "statement of losses and gains," and "stores statistical reports" are presented herewith. It is in the former that the inside facts concerning the gross-profit loss are revealed and in the latter that the loss is traced to individual stores.

It should be noted that the "statement of losses and gains" is divided into two parts, the first being headed "gross-profit analysis," and also that this part of the statement does not deal with retail sales but rather with the merchandise for sale that went into the retail stores during the month. The purpose of this part of the statement is to show the potential gross profit, as well as to set out the accountable features of the gross-profit loss and this method is pursued because it was found unsatisfactory to start with retail sales as their exact cost was not available. On the other hand, the monthly purchases are easily kept at both cost and retail, and as there is little fluctuation in store stocks the potential gross profit can be determined by this method. Of course considerable fluctuation in store stocks at beginning and ending of the period will influence the gross profit, and this is a matter which must have attention.

The second part of this statement, which is the profit-and-loss statement, is the standard form for a trading company with the interpolation of three lines to show the "gross-profit-dollar loss." This is accomplished by the use of ratios. In the upper part of the statement the balance of potential gross profit is reduced to a ratio. In the lower part of the statement the realized gross profit is also reduced to a ratio. The first ratio is then subtracted from the second ratio and the result (due allowance being made for fluctuation of store inventories) is the ratio loss of gross profit. The gross-profit-dollar loss is then found by multiplying the sales by the ratio loss.

Further examination of this statement reveals the fact that all the accountable factors, that is, the factors in groups 4, 5 and 6, discussed in previous paragraphs, are taken care of in the upper part of the statement. Therefore the gross-profit-dollar loss as shown in the lower part of the statement represents the loss that is due to the factors in the inconsequential groups 1, 2 and 3 and in the dishonor groups 7, 8 and 9. Of so little weight are the factors in groups 1, 2 and 3 that any red figure appearing in the lower half of the statement as gross-profit loss casts immediate suspicion upon the store managers to whom it is traced.

This loss is easily traced to individual store managers by having the books so kept that the same type of statement is readily prepared for each store. For those that are seriously out of line, this idea of accounting for gross-profit loss in monthly reports is carried further by having these out-of-line stores appear on the "special stores-gross-profit report" where the results are arranged in the same order as in the profit-and-loss statement except that the detailed classes of expenses are omitted and in their place is listed such information as (a) gross-profit ratio of best 20 stores, (b) number of times on special gross-profit report, (c) number of times on special expense report, (d) amounts recovered, etc. Only the stores with bad showings are on these special reports.

In this statement it has been found that gross-profit results are best visualized in terms of ratio while expenses are compared with a predetermined budget. Stores, where the expenses are out of line, go on the special stores-expense report on which the detail of the expenses is shown. Wherever possible the particular expense that is out of line is indicated by brackets, asterisks or circles in red ink.

With this outline, if the accountant has done his work conscientiously and well, it will not take the executive who reads his report long to find the things that need his attention. However, it is not an outline with which a routine accountant can do much. On the other hand the man who puts it into execution should have considerable vision and be a real technician by whom the language of figures is easily translatable into terms of management.

Use of Accounting in Control

Every dollar spent in the furtherance of an accounting plan designed for the control of operations is wasted unless the danger signals are heeded and decisive action is taken whenever the figures reveal out-of-line performance. In other words, it is useless to spend money on any other than the simplest safeguard accounting unless one makes use of the information obtained by control accounting.

Sometimes when the accountant has revealed startling and often serious details in business operations, the executive says, "What would you do?" If the executive is a good man he does not do this just to avoid solution of the problem, but he does it because he has not grasped the accounting technique involved. In other words he is merely asking the accountant to put the matter into language that he understands.

Let us take a case in point. Here was a group of one hundred stores. Statements were made quarterly rather than monthly, and at the end of one quarter it was found that twenty stores showed net losses ranging from $100 to $1500 for the quarter. The general manager, seeing nothing but the fact that these twenty stores lost money, treated them all alike and when he called in each of the managers to discuss the matter he could tell them nothing more than that they had lost a certain sum of money. Those of the store managers who knew why the money was lost were silent and those who did not know the reason were less able to cope with the problem than the general manager, so little progress was made.

While the same conditions were going on into another quarter an investigation was made in which five of these twenty stores were shown to have lost money because of excessive direct store expense, some of which was avoidable, and the other fifteen lost because of a failure to make a satisfactory gross profit. Of the fifteen, one showed excessive price declines, three excessive special sales, one excessive merchandise shrinkage, and four showed excessive price declines, special sales and shrinkage. The other six stores showed normal declines, special sales and shrinkage, but their inventories were continually short. When this information was divulged, and a method of procedure was being sought, it was immediately apparent that two facts precluded a satisfactory approach to a solution. The first of these was that the statement upon which action had to be predicated was a quarterly statement which was already two months old. The other fact was that no internal machinery had been set up to distinguish the careless and inefficient from the dishonest.

In 20% of the total stores in the group losses were accruing at the rate of 10% on the total investment in all stores. In the five stores showing excessive expenses enough could have been saved to instal and maintain budgetary expense control over all stores. In the other fifteen stores a reasonable profit was sacrificed because the accounting plan had not been adequately fashioned for the purposes of control.

The management might have done well to ponder over this proposition, especially in view of the fact that some of the fifteen managers might have been merely careless or indifferent. Was not the company itself careless in permitting the matter to assume such proportions without finding out as definitely as possible whether the losses were resulting from carelessness or dishonesty? All these men could not be discharged, and the company could not afford to retain them all. Some were inherently dishonest, others incorrigibly careless or indifferent, and they should have been discharged, but many of the others were excellent salesmen, with probably a large following. Any company in such circumstances will find that it costs much less to help managers to master their shortcomings than it does to train new managers.

Another approach to an understanding of the necessity for searching the figures for the answer to that question of invisible gross-profit loss, was made by several comparisons of individual stores with representative performance and of one group with another group. The following is indicative of these comparisons:

	Sales	Gross profit	Ratio
Store No. 21	$54,962.78	$9,633.26	.1752
Store No. 84	54,055.82	11,733.74	.2170
75 stores with best performance	50,789.04	10,591.60	.2085
25 stores with poorest performance	42,287.60	7,683.72	.1817
20 stores with best performance	43,771.02	9,788.54	.2236
80 stores with poorest performance	48,792.08	9,589.06	.1965

It is readily seen that volume of sales has nothing to do with the ratio of gross profit realized. The twenty best gross-profit stores have only a slightly higher sales average than the twenty-five worst. Store No. 84 is better than the seventy-five best, but not so good as the twenty best, which would indicate that there is nothing unusual in its performance. On the other hand, store No. 21, on practically the same volume of sales, shows about $7.00 a day less in profits than store No. 84 and $8.20 a day less than the representative showing of the twenty best stores. Here is an illustration that not only shows to what proportions these gross-profit losses attain but may encourage managers to think and ask questions and thus to make money for the company.

STATEMENT OF LOSSES AND GAINS—STORES
Group No. 1—June 30, 1929

Gross-profit analyses	This month last year	Last month	This month	To date this year	To date last year
Purchases at retail					
Purchases at cost					
Potential gross profit					
Potential gross-profit ratio					
Price declines					
Special sales					
Shrinkage—merchandise					
Shrinkage—produce					
Inventory shortage					
Total losses					
Price advances					
Inventory averages					
Total gains					
Net loss—above sources					
Balance potential gross-profit ratio					
Profit-and-loss statement					
Sales					
Inventory beginning of period					
Purchases at cost					
Inventory end of period					
Cost of goods sold					
Gross profit realized					
Gross-profit ratio					
Net potential G-P ratio					
Gross-profit-ratio loss					
Gross-profit-dollar loss					
Direct store expense					
Supervision					
Truckage					
Warehouse					
Administration					
Total expense					
Total-expense ratio					
Expense budget					
Gain or loss over budget					
Net gain					
Net-gain ratio					

STORES STATISTICAL REPORT
June 1929

Store No.	Sales	Gross-profit ratios			Expenses			Net gain	
		Potential	Actual	*Loss*	Budget	Actual	G/n *L/s*	This month	To date
1......	$2,801.49	.2254	.1880	*.0374*	$457.88	$587.92	*$130.04*	*$110.25*	*$1,210.40*
2......	4,917.55	.2260	.2131	*.0129*	815.93	745.83	70.10	270.20	1,576.94
3......	3,728.87	.2263	.2063	*.0200*	638.62	668.52	*29.90*	98.01	649.04
4......	6,305.04	.2221	.2063	*.0158*	1,121.32	1,091.21	30.11	284.04	1,373.25
5......	3,549.28	.2304	.1871	*.0433*	780.20	740.45	39.75	*65.15*	*381.29*
6......	4,222.47	.2240	.1762	*.0478*	798.45	701.22	97.23	*91.42*	*521.17*

If the management should start out with the avowed policy of bringing the performance of the twenty-five poorest stores up to the average of the seventy-five best, what would this mean in dollars and cents, if it were actually accomplished? The difference in ratio is .0268 and the annual sales of these twenty-five stores with the poorest showing are $1,057,190. If the annual sales of these stores were multiplied by the increased gross-profit ratio there would be in sight a potential improvement of $28,332.69.

If the programme were extended to bring the performance of the eighty poorest up to that of the twenty best, it would mean a gain in profits of $105,781.23 a year. If the programme were still further extended to bring all stores up to standard performance and if success should attend the efforts, would the results be worth while?