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THE FINANCIAL MANAGER'S REPORT

A Quarterly Update for CPAs in Business & Industry ■ September 1992

Industry Members on AICPA Board of Directors Express Their Views

As mentioned in the May edition of *The Financial Manager's Report,* the AICPA Board of Directors for 1992–93 will include four members in industry. We recently spoke to these leaders about their professional activities and their goals as board members. In this issue, we will discuss the comments of Eric Schindler and Ken Hull.

Eric Schindler will join the board in October after serving as Chairman of the Members in Industry Executive Committee (MIEC) for the past two years. Eric is V.P. Finance and Administration for Columbia Paint Company in Spokane, Washington.

When asked what issues would be high on his agenda as a member of the Institute board, Eric cited efforts to reinforce the position of the CPA designation as the premier professional credential for financial managers in business and industry. "The AICPA must continue to communicate to employers about the benefits of employing CPAs on their financial management staffs. I want to be able to read a classified advertisement for a top financial management position ten years from now and see 'CPA required' or 'preferred.'"

Eric also mentioned tort reform as a key issue for the entire profession, including industry members. "Members in industry need to understand and support the AICPA's efforts in fighting for tort reform. Without reform in the professional liability area, escalating insurance costs will shrink the pool of qualified members of the profession willing to perform financial statement audits, thus driving up the costs to businesses of what are often 'required' audits." Eric also feels that the Institute's tort reform initiatives, including efforts to change the comparative negligence rules for securities-related lawsuits, could have a spill-over effect. "Comparative negligence tort reform should eventually lead to product liability reform and directly benefit many employers of industry CPAs."

According to Eric, industry CPAs who want to become more involved in the profession and make the Institute more responsive to their needs should consider volunteering for committee service at the state society or chapter level. "The MIEC is establishing a data base of key industry members, which will include state society committee members. This data base should be useful in alerting these members to current developments and opportunities at the AICPA and can be a valuable resource in obtaining a broad sampling of industry member feedback on professional issues." For those unable to serve on a committee, Eric suggested attending industy forums and conferences sponsored by the AICPA and state CPA societies. "At our annual National Industry Conference, we have established an Industry Committee Forum. We've used the feedback from these forums to shape the committee's positions on key issues, such as the Uniform Accountancy Act."

Industry members often say they feel disconnected from the AICPA. We asked **Ken Hull,** who will be serving his second year on the Institute's board, how he got connected. "After 10 years of paying dues, to both the AICPA and the Illinois CPA Society without realizing why, I decided to find out just what benefits these professional organizations were providing, so I signed on for a committee. Having been actively involved now for many years, I can honestly say that the value returned is far greater than the dues paid."

Ken, V. P. Finance for Follett Corporation in Chicago, added, "The better informed you are about the services provided members, the more you realize how they assist in skills development and professional improvement. And as you become actively involved, at least to the point of remaining informed about all the activities of your state society and the AICPA, that disconnected feeling disappears."

While acknowledging that any one board member can only have a limited short-term influence on AICPA activities, Ken does have an overall goal in mind with respect to his service on the Institute's Board of Directors. " During my term on the board, I would like to see the AICPA move programs forward that will continue to build on the general public's high level of confidence

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Lessons From An Internal Auditor

Chuck Brown, General Auditor of JCPenney Company, Inc., is one of the leading practitioners of internal auditing. He has carved out an important and dynamic role for his function at the retailing giant. At the recent AICPA National Industry Conference, Brown discussed the role of internal audit in an organization. The editors believe this information can be instructive for financial managers who perform a variety of functions for all types of businesses.

Chuck Brown describes auditing as a partnership with management. "The audit function must participate with management to ensure that strategies and expectations are being properly implemented and achieved. Our job is to challenge policies, procedures, programs and activities that are inappropriate, inconsistent, inefficient and ineffective."

An unfortunate perception in some organizations is that internal auditors exist to "dig up dirt," to "create trouble," or, at best, to identify potential problem areas. In a more enlightened approach, Brown says that JCPenney management's instruction to its internal audit staff is to resolve issues, opportunities and problems, not create them. In a cooperative effort with line management, Penney's IA staff acts as a catalyst for resolving issues. "The introduction of objective 'outsiders' (internal auditors) can be especially helpful in the resolution of issues that are cross-functional, sensitive or otherwise controversial."

An important aspect of the internal audit function is working with the audit committee. According to Brown, the committee has some specific expectations from internal audit. These include an annual report on its activities; early notification of significant or sensitive issues; an opinion report on the control system; a statement on the adequacy of the audit staff; the establishment and maintenance of a reporting process to ensure that corrective action is taken; and an assurance of independence.

In return for the commitment to deliver on the organization's needs, Brown believes that the internal auditor is entitled to have certain expectations from management. JCPenney has fashioned an **Internal Auditor's Bill of Rights** (see box). This Bill of Rights consists of a set of principles that can be applied to internal auditors at organizations of all sizes and could certainly apply to all financial managers.

Management's Attitude
Internal Auditor's Bill of Rights

1. The right to a precise and detailed definition of their responsibilities.
2. The right to a full understanding of the corporate policies they are expected to enforce.
3. The right to know what kind of moral behavior management expects of its people.
4. The right to be problem solvers as well as problem identifiers.
5. The right to be brought into the mainstream of the company.
6. The right to a complete understanding of the company's goals and aspirations.
7. The right to a career path in the company.
8. The right to the total support of their company's top management.
9. The right to expect senior management to set the right tone for the environment in which they work.
10. The right to feel important — indispensable, in fact — to corporate management.

Industry Members on AICPA Board *(continued from page 1)*

in the services provided by CPAs. Promoting the image that all CPAs are valued advisers to business in areas where they have special skills is critical. In turn, I would like to see all industry CPAs recognize the value of this image by becoming active members of the AICPA. This will build a much stronger professional organization that can be a force for the betterment of all CPAs."

Ken believes that industry members can play an important role in shaping the Institute's future. "I believe all members should continually challenge the Institute leadership to meet their needs. The AICPA is the members' organization and it should provide products and services that the members see as having value."

As always, we welcome readers' comments in reaction to the ideas expressed by Ken and Eric. Please join the AICPA in wishing them success in their terms on the Institute's Board of Directors.

In our next issue, we will talk to Brenda Acken and Tom Jordan, two other industry members who will serve on the Board in 1992–93.

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Selected Readings for Financial Executives (No. 731450CL) is available for only **$79,** and you can earn **8 hours of CPE credit.** To order, fill out the form on the back of this notice or call the AICPA Order Department at 800/862–4272. When ordering by phone, please ask for operator CL9. *(If you are a resident of Florida, Missouri or New York, please order by calling your state CPA society: Florida 904/224–2727, Missouri 314/997–7966, New York 212/973–8300.)*

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A New Model for Financial Management

David Allen is chairman of the Financial and Management Accounting Committee (FMAC) of the International Federation of Accountants (IFAC), the coordinating body for the world's accountancy associations. In the following excerpt from an article available through IFAC, he describes in concise and clear language the global trend in the profession away from a historical, passive scorekeeping role to a forward-looking, management-oriented active role. Industry accountants are at the forefront of this trend as their employers look to cut back on any activities not considered value-added. Does your job description fit in with the new model outlined below?

Accounting vs. Financial Management

There are some key differences between the accounting model designed to serve the needs of a passive independent reporter on stewardship and the financial management model designed to serve the needs of the financial manager, proactively involved in the control of an enterprise:

- Accounting is concerned with verifiable facts about the past. This leads to a focus on how much of the wealth created by an enterprise has been realized in the form of tangible assets. Financial management, on the other hand, is concerned with judgments about an uncertain future. Its focus is on the creation of wealth, and hence, on profits as yet unrealized and assets as yet intangible.
- Accounting is governed by objectivity — the characteristic of an outsider looking in. It is therefore rooted in costs and oriented towards capital maintenance: Profit is what you could afford to distribute and still be as well off as you were. Financial management, on the other hand, must embrace subjectivity — the characteristic of an insider looking out. It is therefore rooted in values and oriented towards earning an adequate return: What you need to be capable of distributing in order to warrant the employment of capital.
- Accounting is essentially static, seeking to report on a relatively short, discrete time frame, and is based on such concepts as the distinction between capital and revenue. Financial management, meanwhile, is essentially dynamic, paying due attention to the long-term continuum and based on cash flows and the time value of money (otherwise known as the cost of capital).

None of this is to denigrate the traditional accounting model, which is vital to stewardship reporting. Neither is it to support calls heard in many quarters to modify it so as to include some judgment (e.g., replacement costs or intangibles) which, by definition, would destroy objective verifiability. Rather, it is to highlight the fact that members of the profession who are employed within enterprises are concerned not only with accounting but also with financial management.

Two Aspects of Financial Management

In this respect, financial management comprises two distinct but interrelated aspects. The external aspect, usually referred to as the treasury function, is concerned with the relationship between the enterprise and the capital market, notably:

- The identification of sources of funds, ranging from borrowings through various hybrids to equity capital;
- The assessment of the likely reward expectations of the providers of funds, which will take the form of interest and dividends and, usually, also tax; and
- The employment of the various sources to the extent, and in the proportions, deemed appropriate.

Meanwhile, the internal aspect, usually referred to as the financial control function, is concerned with the relationship between the enterprise and its constituent businesses (in most cases defined in terms of products and/or markets), notably:

- The identification of opportunities to expand in particular business areas;
- The assessment of the likely returns on each; and
- The deployment of funds in support of those opportunities considered to be worthwhile.

The key link between the two aspects is the time value of money — what the treasurer sees as the rate of return necessary to warrant the employment of funds, the controller sees as the criterion for their deployment. In this way, the discipline of the capital market is harnessed as a basis for the allocation of resources within the enterprise, thereby maximizing its chances of survival and growth.

Specifically, this leads to the expression of the financial objective of an enterprise as being the maximization of the value of the enterprise which, for all practical purposes, means the maximization of the net present value of projected cash flows to its investors.

Industry accountants should embrace the role as a key member of the management team working toward meeting that objective.

The full text of the original article can be obtained by calling Milou Kelley of IFAC at 212/486–2446.

Benchmarking and Competitive Superiority

By Gary D. Zeune, CPA, CPC, and Jerald D. Vaughan

As we move well into the '90s, the quality movement has gained considerable momentum in the U.S. At several larger manufacturing firms, such as Ford Motor and Xerox Corporation, an early component of their quality-improvement efforts was benchmarking. However, you don't have to be a large company to use benchmarking. Smaller companies are now discovering the power of this process-improvement technique.

What is benchmarking? It is simply selecting an internal process or practice that can be improved and identifying, through research, the firm that is the "benchmark" for that particular process. In discovering what's behind the "best of the best," benchmarking allows you to not only find out *what* "world-class" firms are doing, but also *how* they are doing it. Basically, you are determining the extent of the gaps between your performance and the benchmark's and developing improvement action plans to close those gaps.

Benchmarking can be a powerful tool to achieve competitive superiority. But how do you know what to benchmark? It is important to establish priorities, or the organization may become overwhelmed with so many studies and projects that successful implementation is jeopardized. A key question: What are my company's critical success factors? Your strategic planning process will be a good place to start; however, don't forget to ask, "What's important to the customer?" Benchmarking is an excellent tool for clarifying customer requirements and building effective internal processes for delivering them.

You don't have to be a Xerox to gain the benefits of benchmarking. Many small to mid-sized companies, both manufacturing and service, are now using the process. For example, Atlanta-based Risk Sciences Group, Inc., a $2.6 million insurance firm, used benchmarking to gain better cost control and to assure their clients that they are getting the best service at the most competitive prices. As a result, Risk Sciences has achieved much higher client retention and 1991 revenue growth of 57% over 1990.

Benchmarking is not a quick fix. It requires commitment by top management and extensive training for successful implementation. There will be a unique learning curve associated with your specific business, but benchmarking can provide "windows" to the external environment and to customers. Benchmarking is a way for firms to become learning organizations focusing on the continuous improvement that will allow them to attain competitive superiority.

World-class companies have used benchmarking to achieve and maintain that status. Such companies will share their success with you as long as you return the favor (other than trade secrets). Do your research. Find the best, make a telephone call and get started.

Gary D. Zeune of Columbus, Ohio, specializes in strategy formulation and implementation for small to mid-sized companies and publishes *The Competitive Superiority Report: How "Ordinary" Companies Thrive on Competition.* For a free copy, call 614/221–6228.

Jerald D. Vaughan of Discovery Organizational Consulting in Columbus, Ohio, specializes in quality strategy development and implementation. For information on process improvement and training, call 614/236–9636.

Industry Executives Highlight World Congress of Accountants Program

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Even if your company doesn't yet participate directly in the world market, you need to broaden your understanding of the emerging global economy and learn about changes in international finance and accounting. The World Congress convenes only once every five years and won't return to the U.S. until sometime in the 21st century! Boost your career and enhance your global knowledge by participating in the XIV World Congress of Accountants! Call the AICPA Meetings & Travel Services Division at 201/938–3232 for details and registration information.