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Financial Manager's Report, September 1996

American Institute of Certified Public Accountants (AICPA)

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1996 Fall National Industry Conference and the Strategic Performance Measures and Finance Best Practices Conferences in San Francisco

Mark your calendars! The 1996 Fall National Industry Conference — *The New Finance — Building a Bridge to the Future* is being held **October 31–November 2** at the Hyatt Regency in **San Francisco, CA**.

The Fall National Industry Conference offers up to **21 hours of CPE**. You'll receive the highest quality technical training and get an insider's peek at industry trends. It's a dynamic program that industry professionals have come to depend on for gaining valuable insight from a myriad of experts.

The **1996 Strategic Performance Measures and Finance Best Practices Conferences** are being held as an optional session (**October 30**) to the Fall National Industry Conference. The programs have a repeat performance on **November 18 & 19** at the Northbrook Hilton, outside of Chicago. Representatives from leading companies share their success in designing and creating financial and nonfinancial strategic performance measures and best practices.

You'll learn about the cutting-edge topics and issues you need to gain the competitive edge in your business. For a copy of the conference brochure please call the AICPA Order department at (800) 862-4272.

More on the 1996 Fall National Industry Conference. . .

There are many highlights in this year's program. The conference offers the perfect mix — from software to human resources issues, FASB and corporate and individual tax updates to management challenges. The following are just a sampling of what the program has to offer:

- **Gregory Hackett**, of The Hackett Group, will give the Keynote, offering participants a private look into *18K — The Next Competitive Weapon*. Learn how to reduce, control and analyze general and administrative expenses to improve profitability.

- *Finding Financial Freedom Through Planning* advises you on what you need to do now, to ensure financial security by the new century. **Jonathan Pond**, Financial Planning Information, Inc. offers his ten best investment ideas and savvy advice on personal financial planning.
- **Dana "Rick" Richardson**, of Richardson Media & Technologies offers *Technology Trends and Forecasted Futures*. Mr. Richardson is a nationally recognized technology forecaster, and reviews the trends that will impact both the business community and our personal lives.
- **John Fisher**, of New Finance Associates, hosts an interactive forum where you'll hear about the trends that are affecting business today, and exchange ideas on how the AICPA can better serve your needs to maintain your competitive edge.
- Sessions like *Out of the Box Cost Leadership* and *Maintaining Internal Controls in a Downsized Environment* keep your management accounting side up to snuff.
- The luncheon address this year, *Our Economic and Financial Future*, is brought to you by **Douglas Cliggott**, Global Investment Strategy, Merrill Lynch & Co.

This program has always combined industry insight with a social element. This year's program is no exception. . .

Start the conference by attending the welcome reception. You'll have an advance opportunity to meet participants and peers. Our morning "Industry Breakfasts" continue to be an eye-opening way to start your day with members of your industry niche.

Our Thursday night receptions continue their reputation as great theme parties. This year you can expect something a little different — because you provide the theme! Do the mega monster mash at the **Fall National Industry Halloween Reception!** Join the festivities as you hobnob with fellow participants and have a ball. Have you ever wanted a tattoo? Your fortune told? Now is the perfect opportunity!

San Francisco hosts the conference and is one of America's best-loved and unique cities. Travel via cable cars, enjoy the lively atmosphere of Fisherman's Wharf, and take advantage of world-class shopping in Union Square. Try the unequaled experience of Chinatown or visit Sausalito by ferry. You may even choose to steal away for a relaxing day in Muir Woods. The Bay Area has a host of scenic and satisfying ways to spend your time — the hard part is deciding what to do first!

We have two exciting companion tours to choose from for both Thursday and Friday. *Muir Woods and Sausalito* (Thursday) and *Wine Country: Tours and Tasting* (Friday) will keep your companion busy. . . not to mention satisfied!

Inside The Financial Manager's Report

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Strategic Planning for Information Resource Management

A new guide published by The Society of Management Accountants of Canada, *Strategic Planning for Information Resource Management*, is designed to improve the creation, use, management, and delivery of relevant data, thus helping an enterprise capitalize on its base of information.

Knowledge-based business

Relatively few organizations recognize that the knowledge housed in the organization's databases can provide the means to rapidly move ahead of its competitors. The first organization in an industry to recognize and exploit the value of a piece of information, often something that is accessible to all industry members, gains a competitive advantage.

Information systems should be an essential, indispensable and strategic component of service delivery and should satisfy the organization's business and service goals. Fragmented automation efforts, unilateral commitments to mainframe-based applications, incompatible proprietary software platforms, disparate software and inaccessible data can prevent information systems from helping meet these goals.

The role and objectives of IRM

Information Resource Management (IRM) is an approach to planning that recognizes the relationship between business planning and technical infrastructure. It helps the organization move beyond data management to the strategically beneficial ability to leverage its information.

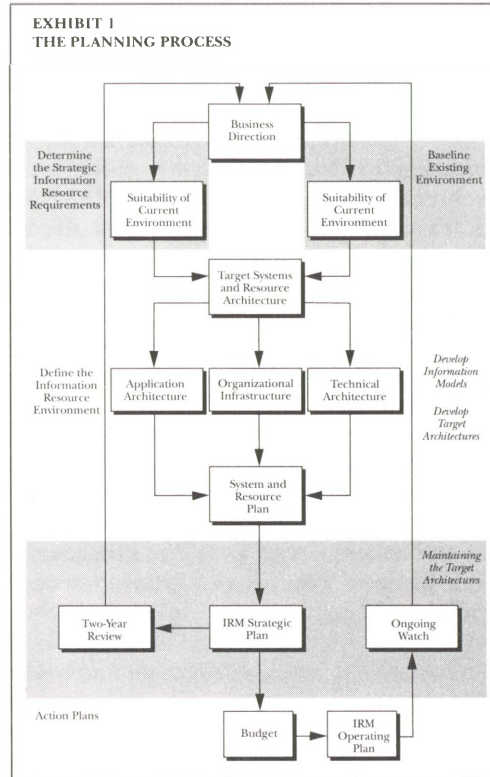
IRM focuses on designing, implementing and maintaining a balanced, enterprise-wide system of information, processes, and technology. In the IRM environment, technology is viewed as a means to assist the business to do things faster, better and cheaper — not as an end in itself. An effective IRM program provides for continuously scanning the environment for opportu-

nities that could drive the direction of an organization's business.

Developing the IRM Strategic Plan

Three key steps are involved in planning for the introduction of IRM:

- determining strategic information resource requirements.
- baselining the existing environment.
- designing the IRM.



The exhibit shows the relationship between these three steps. The process starts with a definition of the business direction. The process provides an opportunity to identify areas of vulnerability, which may need to be monitored closely and subjected to stringent controls.

The second step, baselining, provides a complete assessment of the current environment. The assessment focuses on system demographics, maintenance status, and system functionality.

The third step, designing the IRM, can be performed with the help of modelling techniques. Business, activity, data, process and enterprise models are developed in order to fully appreciate what information resources exist, what are needed, and where there are gaps. Powerful simulation and prototyping tools help systems architects and designers develop a living model of the business that can be maintained over time as a point of reference for defining the target business and information architectures.

The target architectures specify what the technological infrastructure will look like, but not how it will be constructed, which is spelled out in the strategic implementation plan.

Preparing and implementing the IRM Implementation Plan

The first stage in developing the IRM implementation plan is to define each project and assign priorities. Organizing priorities is based on three key factors: management need, benefit/cost, and risk. The development of project priorities and the definition of project interdependencies should result in the production of a project schedule that describes the sequence in which projects will be completed.

It is extremely important to consider the organizational impact of change when preparing the implementation plan. Managing the human and organizational factors is highly important to the overall success of the IRM initiative. To ensure a smooth roll-out of the program, a formal, structured change management program must form part of the implementation strategy.

Measuring success

The IRM plan should be reviewed at a strategic level at least once every two years, or more often if the corporate strategy is on a shorter review schedule.

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The *Financial Manager's Report* is a publication of the committees of the AICPA's Industry & Management Accounting Team. It is mailed five times per year to all AICPA members in industry as an insert to *The CPA Letter*. Opinions of the authors are their own and do not necessarily reflect policies of the Institute.

The Committees and Staff welcome your input on ways to make FMR more responsive to your needs. Please address comments in writing to AICPA, Industry & Management Accounting Team, 1211 Avenue of the Americas, New York, NY 10036-8775 or e-mail the editor at 103063,2154@compuserve.com.

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PRACTICAL STEPS FOR SUPPORTING THE HUMAN SIDE OF CHANGE

The ability to manage change has become a core competency in every area of business. Managing change involves analytic tasks such as developing new procedures and systems as well as the more personal work of developing beliefs and behaviors that enable us to approach our role from a new perspective. While new systems and procedures can be successfully developed by a sub-group of organization members, effective implementation requires all members of the organization to discover a new way to bring themselves to their work.

Most change efforts fail to achieve the desired results in the anticipated time frame. These failures are due in large part to an inadequate understanding of the human adaptation process and how it can be supported. When the human adaptation process isn't factored into a major transition, we find organization members trying to work with new procedures and structures while operating with old assumptions and behaviors. This mismatch leads to ineffective problem solving, quickness to blame, diminished creativity and a considerable increase in stress.

Fortunately, all of us know how to adapt, the ability is inborn. Our instinctive adaptation process follows a three phase pattern: Letting go, Experimenting and Building. (I described this model in the March 1996 issue of *The Financial Manager's Report* under the title "The Human Side of Change." This model is adapted from the work of William Bridges.) The overall pattern is predictable, but the timing of the development is not. Each of us progresses at our own internally determined pace. You can't control the adaptation process, but there is much you can do to encourage it. Below I describe practical steps you can take to support each phase.

PREPARATION

- Prepare organization members for a transition by presenting a well-constructed business case that makes change an imperative. Provide information on what is and isn't working.
- Describe how the organization could become more effective.

THE ADAPTATION PROCESS: LETTING GO

- Share the adaptation model to help organization members become aware

of their personal change process and what they can do to help themselves adapt.

- Normalize the feelings that are part of transformation. Let organization members know that it is okay to experience feelings associated with failure and loss when letting go of beliefs that have been important to us. By making these feelings acceptable you can diminish the need to resist by becoming angry, looking for someone to blame or denying the need for change. Help organization members understand that attempts to block these feelings will effectively block the Letting Go phase.
- Engage organization members in creating a two column chart showing the beliefs, expectations and behaviors that are no longer helpful and the beliefs, expectations and behaviors that will be effective. You may want to create different charts for different aspects of their roles.

THE ADAPTATION PROCESS: EXPERIMENTING

- As "Experimenters" explore new ways of operating, they will find themselves blocked by out-moded policies, expectations and procedures. Help them to identify the barriers they face and develop strategies for removing them.
- Work with your management and your peers to remove barriers and create temporary systems that will support experimentation.
- When possible create pilot teams made of organization members who are ready to find new ways to operate. Charter them to act as pioneers who explore the new territory and then return to show others what has been discovered.
- Help *Experimenters* tolerate the uncertainty and chaos that characterizes this phase so that they can stay with the process long enough to discover new behaviors and attitudes. Frequently debrief the *Experimenters* in small groups to help them reflect and learn from one another. Urge them to try many approaches to guard against any tendency to become attached to one approach before exploring a full range of possibilities. Encourage them to assume an attitude of curiosity about what they will discover next. Acknowledge all experimental efforts, even if they are unsuccessful.

THE ADAPTATION PROCESS: BUILDING

- Work with your management and peers to help secure the specific authorization and resources needed to create the new structure.
- Make sure that organization members have opportunities to help develop the new processes that they will perform.
- When necessary remind organization members who are ready to build and implement the new way of operating that some of their colleagues may need more time to adapt. Teach them what you have learned about helping others move through the adaptation process. Help them apply it.
- The Building Phase is characterized by excitement and anxiety generated by concerns about successful implementation of new ideas. Help the group understand their concerns and direct their energy into the work effort.

The change agent role provides many opportunities for using your coaching, influencing and creative problem-solving skills. At times the work can be frustrating; however, it is usually quite rewarding.

Jane M. Maloney is president of Inter-Action, Inc. a New York-based consulting firm specializing in organizational effectiveness. For more tips on how you can support change contact her at jmmaloney@aol.com or directly at (212) 864-4287.

Outstanding CPA in Business and Industry Award

You are invited to participate in the nomination of candidates for the 1997 AICPA Outstanding CPA in Business and Industry Award. This award was created to recognize the achievements of individual CPAs employed in business and industry and to promote the CPA designation as the premier professional credential for financial managers. The award will be presented at the AICPA's 1997 Spring National Industry Conference, May 14-16, 1997 in New Orleans, Louisiana. For complete information, call Jodi Ryan at (212) 596-6105. The deadline for nominations to be considered for the 1997 award is October 18, 1996.

Customer Account Profitability

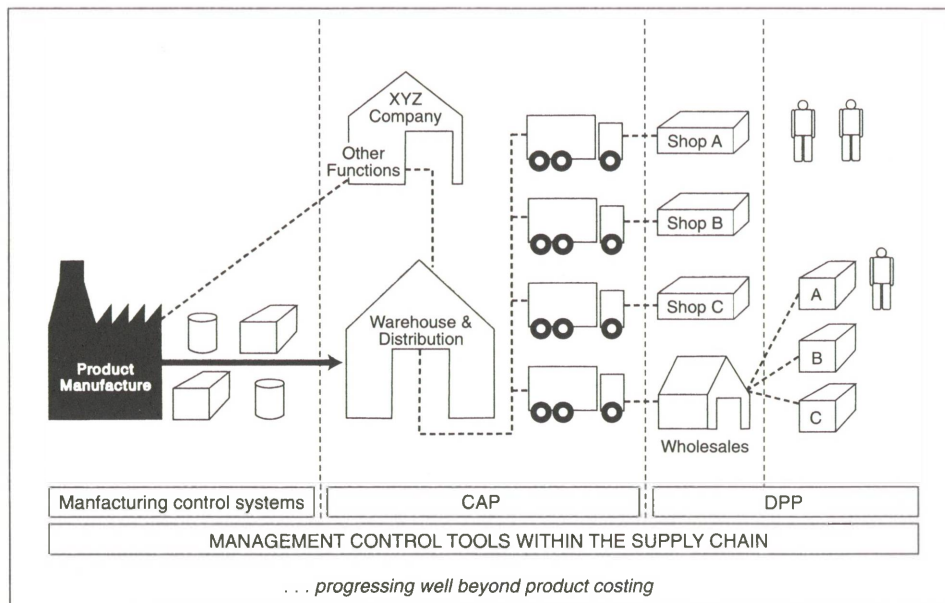
As interest continues to grow in measuring, managing and improving the cash flow and profitability of customer service, activity-based costing (ABC) techniques are recognized by many businesses as a means of producing meaningful and actionable information. ABC is at the core of the customer account profitability (CAP) analysis finding favor in an ever-widening range of organizations. This article, by Gary Ashworth of Ernst & Young and Tim Connolly of Partners for Change, is an abridged version of the 1995 IFAC/FMAC Article of Outstanding Merit, originally published as "Managing Customers for Profit" in Management Accounting (U.K.) in April 1994.

Richard Allaway, of the global drinks group IDV, underlines the power of CAP applied to the Gilbey Wines and Spirits group: "the evidence of the channel [profitability] analysis was incontrovertible. . . I can't believe that we shall turn out to be the last company to discover that a whole division is, in reality, delivering a negative profit from serving its particular market sector. If this case shows anything at all, it is that profitability analysis can lead to much bigger changes than you might anticipate."

Direct product profitability (DPP) is an established tool used by retailers to optimize product contributions as they flow through to the point of customer purchase. Various manufacturing cost control systems focus on product costs in manufacturing operations. CAP, however, brings something new to the table. It enables a full understanding of profitability within the organization, identifying costs and added value at any number of levels in a profitability hierarchy. Typically, this might involve reporting at the product, order, customer and market/trade sector levels.

The significance of CAP can be illustrated by considering the issues that surround the decision to allocate scarce resources to customer supporting activity. Take advertising and promotions, which typically vary between 15 and 30% of gross sales value: where should management invest these funds? Brand profitability will provide information supporting the choice between brands, but historically this has only been augmented with gross profit information about customers. By capturing these costs, and those related to other services provided to customers, a *net customer account profit contribution statement* can be produced.

Focus of CAP within a typical business framework



However, a reliable and meaningful CAP system is not introduced lightly. It requires a cross-functional view of business activity, and attribution of costs and activities using techniques that go well beyond traditional cost apportionment. These factors have deterred many businesses from developing the ongoing, dynamic systems they need to manage performance in their market environment. Business relationships change almost daily and the account management actions to be taken as a result of these changes need to reflect the overall profitability of the trading relationship. We have seen one company that uses customer profitability information relating to individual customers to prioritize order production scheduling at times of maximum plant capacity. Another company, Crookes Healthcare, uses a sophisticated CAP system to produce monthly key performance indicators that form the basis for managing long-term customer relationships. Other organizations have found that they can benefit from a one-off exercise with periodic subsequent updating. Whatever the nature of the system, several critical success factors apply. They include:

- a driving need to produce and use the analysis. For example, in the UK brewing industry it was the break up of the tied trade system of working.
- a clear vision of the expected benefits, which can normally be quantified — although this may take some time.
- a willingness to support the system

with management action. CAP will not achieve anything in itself.

- the development of the system has to be seen as an investment. Distractions are easy during the set-up phase and if they are allowed to prevail, momentum will be lost and the system may never be completed.

Why is CAP an issue?

The changing business environment may put pressure on the value of trade with key customers in various ways, for example increased trade concentration (as in the UK retail chemist sector), the consumer-driven structural changes that have taken place in the printing industry or the growth in purchasing power of the major UK grocery retailers. A similar drive for change is driven by the creation of innovative customer relationships such as those developed by the Dell Computer Corporation, with direct-from-manufacturer sales and service with unlimited telephone problem-solving support. Customer profitability management is an integral part of the proactive response to the impact of these changes in the customer relationship.

What is CAP?

A meaningful customer profit contribution is simply the difference between the revenue earned from a customer and all the costs that can be justifiably associated with that customer. Customer revenues and related trading margins

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Strategic Planning for Information Resource Management *(Continued from page 2)*

At a strategic level, one of the key benefits of an IRM environment is that, as it matures, the organization will be able to capitalize of the increased level of knowledge and improved technology and collections of corporate data in previously unthought of ways. It is important to organize a method of capturing this learning so that it can be used on a continuing basis to improve the overall IRM environment.

The role of the management accountant

A management accountant can provide valuable insights about information and decision-making throughout the organization and thus, through IRM, help improve decision-making and realize the organization's strategic business plan.

Strategic Planning for Information Resource Management is published by The

Society of Management Accountants of Canada as *Management Accounting Guideline # 9 (revised)*. It is available individually from the AICPA (product # 028963) or as part of *The New Finance: A Handbook of Business Management* (product # 028900). Other recent publications, *Measuring the Cost of Capacity* (product # 028961), *Measuring the Impact of Managing Diversity Issues* (product # 028963), and *Benchmarking Information Referral Service — revised* (product # 028950) are now available. This AICPA binder features publications on current management topics such as benchmarking, activity-based costing, and performance measurement. Please call the AICPA Order Department at (800) 862-4272 for a gratis brochure (# G00107) detailing each publication or to order the series.

Companies Sought to Host Educators Onsite

This past spring, the AICPA Academic and Career Development team launched a new and exciting program for accounting educators. Merrill Lynch and Co., Inc. and Media General, Inc. hosted a group of educators and discussed cutting edge issues and practices being conducted in their respective industries, namely financial services and communications. The visits were well received by all, including the company hosts. First, it gave companies a direct opportunity to communicate their needs to educators as far as desired student competencies. A secondary benefit was that it provided a forum for different departments within the company to learn about activities of other areas. Third, the program and companies got good publicity in the *Journal of Accountancy*.

As a result, the Institute wishes to continue the program and seeks volunteer companies to host educators. This past year, visits were offered in conjunction with regional meetings of the American Accounting Association (AAA) which draws large groups of educators. As a first preference, the Institute is seeking company sponsors which are available at the times of those meetings and in close proximity to where those meetings are being held. A list of upcoming meetings is provided below. However, all companies are welcome to volunteer as hosts. Interested companies should contact Liz Koch, Manager of Education Programs at (212) 596-6219 for more information or to volunteer.

Attention Internal Auditors

Beginning in November 1996, this newsletter will include short articles on hot topics and key issues that internal auditors face. In order to provide you with guidance that will be valuable to you, we would appreciate your sharing ideas and suggestions to us. Also, if you are willing to write a short article (1000 words) or review one written by another, please let us hear from you. Please call Hadassah Baum, technical manager, Industry & Management Accounting Team at (212) 596-6019.

1997 AAA REGIONAL GROUP MEETINGS

Southwest	March 11-15, 1997 New Orleans, LA
Mid-Atlantic	April 10-13, 1997 Baltimore, MD
Midwest	April 17-19, 1997 Oak Brook, IL
Southeast	April 24-26, 1997 Nashville, TN
Northeast	April 24-27, 1997 Binghamton, NY
Western	May 1-3, 1997 Rohnert Park, CA
Ohio	May 2-3, 1997 Dayton, Ohio

1996 Fall National Industry Conference and the Strategic Performance Measures and Finance Best Practices Conferences *(Continued from page 1)*

1996 Strategic Performance Measures and Finance Best Practices Conferences

You have requested an alternative to the "sit and listen" style of programming. These conferences do just that, offering roundtable discussions with peers and experts in SPMs and best practices.

More on . . . Strategic Performance Measures Conference

There will be group breakouts to support you in acquiring the most knowl-

edge: *Introduction to SPM Implementation (Basic)* and *Continuous Improvement of the SPM System*.

Sessions include *The Why and How of SPMs*, *You as a Change Agent: Overcoming the Challenges to Successfully Implementing an SPM Program*. (Intermediate & Advanced)

More on . . . Finance Best Practices Conference

Sessions include *Best Practices Vision Development Through Benchmarking*, *What*

is a Best Practice and How Do You Know One When You See One, and many others. Learn how to build a tactical action plan, and gain insight from companies already on the leading edge of their industry.

For a copy of the conference brochure or to register, please call the AICPA Order Department (800) 862-4272. If you have any questions regarding the conference, please call Cathy Brosnan at (201) 938-3568.

Self Study Course Launches CPAs into Cyberspace

CPAs Guide to Navigating Online demonstrates the basics CPAs need to access online resources such as the Internet, the AICPA's Accountants Forum on CompuServe, and various bulletin boards of special interest to the profession. It includes keystroke-by-keystroke instructions along with free software and enough free online time to complete the course and do some "surfing." While completing the course, users can take advantage of the "mentored

self study" approach which provides on-line access to a technology expert from course developer Kent Information Services, Inc.

Recommended CPE Credit: 16 hours.

Format: Text and online contacts (739055CLA9) \$195.00

SEC Update!

Revised! *SEC Reporting* outlines the latest Securities and Exchange Commission pronouncements bearing on

financial reporting of publicly held corporations. It explains and illustrates the relationship of the initial registration statement, forms 10-K and 10-Q, and the proxy statement, providing a thorough practical understanding of SEC reporting requirements.

Bonus: CCH's *SEC Handbook* is included with the course.

Recommended CPE Credit: 14 hours

Format: Text (736334CLA9) \$149.00

Earn 24 Hours of CPE Credit for Only \$129!

CPE Direct, the AICPA subscription series that enables members to earn up to 24 hours of CPE credit for reading certain *Journal of Accountancy* articles and completing a study guide, is still only \$129 if you subscribe now!

The price includes four study guides, issued quarterly, which are based on designated articles in the three preceding monthly issues of the *Journal*. The articles will cover information on a broad range of subjects, including financial accounting, auditing, taxation, international business, consulting services and human resources. CPE Direct study guides will also contain

other readings, checklists or practice aids to enhance members' insight. The study guides will be released in March, June, September and December.

To receive CPE credit, members need to read the designated articles, complete the study guide, answer the questions and return the answer sheet for grading. A passing grade affords the member an AICPA Certificate of Completion stating that the member has earned 6 recommended CPE credits in a specified field of study.

Six credits in specified fields of study will be given each time a quarterly answer sheet is sent in, for a total of 24

credits. Since CPE requirements vary from state to state, please contact your State Board of Accountancy for information concerning your State requirements as to the number of CPE credit hours which you must earn and the acceptable fields of study. Please note: The North Carolina State Board of Accountancy does not accept CPE Direct credits toward its requirements.

Order now to receive the September 1996 Study Guide CPE Direct (No. GO1059-CLA9)

Price: \$129.00

Recommended CPE Credit: 24 hours

To order: Call (800) 862-4272 (option #1), fax to (800) 362-5066, or write the AICPA Order Department, P.O. Box 2209, Jersey City, NJ 07303-2209. These courses are also available through your state society.

Customer Account Profitability *(Continued from page 4)*

are generally clearly understood, but developing a meaningful customer specific cost is sometimes more difficult.

The figure on page 4 shows the focus of the customer account profitability measurement within a typical business framework or supply chain structure, i.e. beyond product costs which generate trading margins by customer, to now include the costs of all the relevant major customer interface/service aspects which erode the trading margins achieved. These include the need for a better understanding of how the company's resources are used in:

- marketing, selling and negotiating with customers,
- making deliveries,
- administering the arrangements of the sale and delivery, and
- all the other activities which are necessary to satisfy customer needs.

In other words, CAP gives a company an improved understanding of, or new

insights into, its sources of profitable business. The real value must then be in acting on that new information as a powerful catalyst to profit improvement.

While many companies have obtained interesting insights from activity-based product costing exercises, the scope to make changes as a result is often limited, because relatively few non-product related costs will change as a result of changing product volume or mix. The experience with customer account profitability, however, is different. Customer-driven resources such as salesmen, marketing expenses, delivery costs, telesales, and sales order processing often have a higher discretionary element than product-level costs. Customer-driven resources are also often easier to switch between customers and market segments.

Key principles of CAP

Three key principles about customer costing should be emphasized:

- *customer costs must be related to the revenues they generate.* This normally points to a life cycle, rather than an annual view of the profitability of the relationship.
- *not all costs should be attributed to customers.* Full attribution clouds visibility of how costs behave and, therefore, impedes the ability to make informed decisions. Costs should be attributed at whatever level is appropriate within an overall business model.
- *make it absolutely clear who can influence or control different types of cost.* Many organizations lack the clear customer focus to make this possible without realigning responsibility and accountability.

The principles of effective customer profitability management using CAP are therefore clear. Management now faces the challenge of establishing whether it can adopt these principles, overcoming the organizational, cultural and technological barriers that lie between them and success.