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Chief financial officers and controllers need to understand the importance of becoming effective change agents. To be effective, they must have good technical and human relations skills. While the accounting literature has primarily focused on the technical aspect, management literature has recognized that good human relations skills are necessary for the implementation of change.

Although the accounting profession has recognized the importance of change, implementation appears to be lagging, and management accountants have been criticized for this [Kaplan, 1984]. An example is the implementation of variable costing for internal purposes. Accounting textbooks and leaders in the field of management accounting have indicated for several years that variable costing is the most appropriate method for internal purposes. The limited accounting research that has been conducted, however, indicates that variable costing is not a widely used technique.

Data from a field study of 48 manufacturing firms, which examined the use of variable costing for internal purposes, illustrates the change issues that accountants need to consider when implementing changes within an organization. The design and results of the study are discussed as well as the behavioral implications.

Approaches to Change

Technical

One justification for the existence of any staff manager is the manger's ability to create change. Since staff managers, including the chief financial officer and the controller, do not contribute directly to the transformation of raw materials into finished goods, they must contribute indirectly by improving the way in which that process functions.

The current primary approach for change used by those who educate accountants is very simple. The accountant learns about some new technique through a class at an educational institution, a seminar, or by reading a scholarly journal. The individual teaching the course/seminar or writing the article provides a description of the technique that is being prescribed and a justification for its use. If current or future accountants accept the justification, they are supposed to go to their work place and implement the technique.

Those who are prescribing the technique view implementation as a technical problem. They provide the staff manager with all of the knowledge about how the method works and the technical information about implementation. This usually includes information about programs and software that can be used. The individual may even be provided with examples and material for communicating the technique to others. Almost all of the assistance is technical in nature.

The technical approach to change is best evidenced by the journal articles that have been written in the last five years by leaders in the field of management accounting such as Howell, Johnson, Kaplan, and Stacy. These articles have cited deficiencies in traditional management accounting systems and identified changes that would improve these systems. The primary focus of these articles has been on the technical aspects of change. Other aspects of change, such as human relations, have been overlooked or inadequately addressed.

Human Relations

While the accounting profession has focused primarily on the technical approach to change, a very different view of implementing change is found in the management literature. This approach is based upon the premise that all change takes place to people and through people. This people-oriented view recognizes that successful change is more than a technical issue. Successful change is implemented by individuals and, consequently, those individuals are also changed.

The people-oriented approach recognizes that people may resist even the most logical attempts to implement change. The individual, when making decisions, does not always attempt to find the best alternative for the organization; instead, most seek what is called a satisfactory solution [March & Simon, 1958]. Those who are satisficers, rather than maximizers, may not be willing to change simply because they are not unhappy with the current situation. If the status quo is viewed as adequate, then the operative phrase is "if it ain't broke, don't fix it."

This approach to change also recognizes that most change attempts fail, not because the change agent is technically unqualified, but because the agent lacks the skills required to work with people. The most important skill is communication. The change agent must be able to make clear not only what the change is but also convince others of the need for that change. The people-oriented view of change puts a great deal of emphasis on motivation and group dynamics skills. The change agent needs to understand that much of the resistance to change is not technical but involves emotion and feelings. The change agent must also have a good understanding of the nature of power and the need to gain support for change from powerful persons. Recent accounting literature [Johnson & Kaplan, 1987; Lammert & Ehrsam, 1987; Smith, 1989; Briner, Truitt & Wilson, 1989] indicates that the profession is recognizing the importance of gaining support for change from powerful persons (management).

The technical and human relations approaches to change provide two different ways of implementing change within an organization. Accounting research, however, indicates that neither method has been effectively used by accountants to implement variable costing.

Variable Costing Research

For many years accounting students have been taught that firms should use variable product costing for internal purposes even though absorption product costing is required for external reporting. This prescription is based upon the premise that the former permits more control of internal operations while the latter is considered a better method of valuing inventory and measuring income in external reports.

The limited accounting research that has been conducted indicates that absorption costing, rather than variable costing, is being used for internal purposes [Lere, 1976; Imhoff, 1978, Akers & Porter, 1988; Cooper & Kaplan, 1988] and that variable costing is not considered an important management accounting tool [Hawkins, 1983; Elmore, 1986]. Since such research is limited and primarily uses a survey approach, a field study [Akers, 1988] was conducted to determine if the prescription was being followed.

Variable Costing Field Study

The field study sought to determine the extent to which firms use absorption costing for external purposes and variable costing for internal purposes. The primary purposes of the field study were to determine: (1) the product costing method being used for external reporting purposes; (2) the product costing method used for internal financial reporting and budgeting; and (3) reasons for the methods used internally.

Forty-eight manufacturing firms located in the mid-south were visited.

External financial statements and internal financial reports were examined to determine the product costing method being used. Either the chief financial officer or the controller was interviewed to determine the reasons why a particular product costing method was being used.Firms that allocated at least 80% of their fixed manufacturing overhead for any particular use were considered absorption costers. All other firms were considered variable costers.

Table 1 presents the number of firms that were using absorption and variable costing for external reporting and internal financial reporting.

The frequencies show that the majority of the firms in this study were using absorption costing for external reporting and internal financial reporting.

Table 2 presents the number of firms that were using absorption and variable costing for external reporting and internal budgeting.

Table 1
Cell Frequencies

		External Reporting		
		Variable Costing	Absorption Costing	
Internal Financial Reporting	Variable Costing	4	7	11
	Absorption Costing	0	36	36
	Totals	4	43	47*

*One firm was excluded from statistical analysis after the interview revealed the firm did not meet the established criteria.

Table 2
Cell Frequencies

		External Reporting		
		Variable Costing	Absorption Costing	
Internal Budgeting	Variable Costing	2	7	9
	Absorption Costing	0	27	27
	Totals	2	34	36

The interesting aspect of the budgeting results is that 11 firms did not use budgets. Of those firms that did, the majority used absorption costing for both external reporting and internal budgeting.

The results indicate that most of the firms in this study were not following the prescription that absorption costing is used for external purposes while variable costing should be used for internal purposes. Although most of the firms were using absorption costing for external purposes, they were not using variable costing for internal purposes. This result is consistent with the results of prior research that were previously discussed.

Results of Field Study - Reasons for Methods Used

The chief financial officers and controllers provided several reasons why they were not following the prescription. A few of the respondents were using absorption costing for both external and internal purposes because they felt the external reporting requirements dictated internal usage. The viewpoint is consistent with Kaplan's argument that "contemporary U.S. practice ... is characterized by the internal use of accounting conventions that have been developed and mandated by external reporting authorities" [Kaplan, 1984]. Some felt the arguments supporting the use of variable costing were not sufficiently persuasive. It is interesting to note that the debate concerning which product costing method is superior has continued for almost 30 years.

Some of those not following the prescription were doing so because they had not been able to successfully distinguish between fixed and variable costs. Identifying fixed and variable costs in practice is often not as easy as the accounting literature implies. Several were not using different methods because they believed the benefits did not justify the costs or they simply did not feel they had the resources necessary to implement the prescription. Others stated the time-worn reason that "this is the way we have always done it around here." Finally, many did not use two different methods because they believed the conversion to variable costing internally would require wholesale reeducation of the nonaccountancy managers. Rather than invest the time and resources to train a large number of individuals, it was easier to continue with the use of absorption costing for both internal and external reports.

With the exception of the respondents who felt absorption costing was the best method for internal purposes and those who had difficulty identifying fixed and variable costs, the reasons for not changing were basically non-technical. While several of the respondents indicated variable costing was the most appropriate method for internal purposes, they thought absorption costing was sufficient. The implication is that most of the firms in the study were seeking a satisficing rather than a maximizing solution. Consequently, most of the firms were reluctant to implement change. This is not surprising from the standpoint of human relation problems in making change. This reaction, however, is unexpected if change is seen from the technical point of view because the technical approach to change views knowledge as the primary obstacle. Since knowledge can be obtained through education, change is seen as a relatively straightforward process.

Behavioral Implications

Research [Lynn & Lynn, 1984] into the behavioral approach to change suggests that successful change includes several elements: (1) timing, (2) preparation and planning; (3) good communications, (4) support from management, (5) consideration of resistance, and (6) participation of operating personnel. Although most of the firms in the study were not following the prescription, there were some firms using absorption costing externally and variable costing internally. The ways in which they were able to implement the prescription illustrate several of the key elements of the behavioral approach to change.

The behavioral approach suggests that successful change requires good timing. This is particularly true if there exists a general feeling that the change is not justified because the current situation is acceptable. One of the firms, Martin Industries, Inc. [Briner et. al] reported that the change to variable costing for internal purposes was made possible by changes in personnel. Another firm reported that the change to variable costing for internal purposes was made possible because of declining profitability; the accountant was able to justify the change because the benefits (economic survival of the firm) exceeded the costs necessary for implementation. The behavioral model recognizes the need for unfreezing old behavior. Often,. the manager needs to be willing to wait until the right moment to suggest the change.

Successful change also requires extensive preparation, planning, and good communication. Martin Industries Inc. developed an extensive plan for implementing and communicating the need for change. Implementation and communication were accomplished through the distribution of internally developed educational materials and seminars conducted by an outside consulting firm. The educational material, which was distributed to management and appropriate production personnel, described the new approach and provided evidence justifying the use of variable costing for internal purposes. The plan of implementation was communicated to the individuals during the seminars that were led by the outside consultant.

While communication of the plan is important, the behavioral approach recognizes that continued communication is necessary if change is to be successful. This was accomplished at Martin Industries, Inc. by the establishment of a continuing education program for individuals associated with the firm.

The behavioral view of change also recognizes that successful change can not occur without the support of top management. Several of the chief financial officers and controllers indicated that the main problem in introducing variable costing was getting the support of their nonaccountancy superiors. Without this support, they were unable to convince the other nonaccountancy managers that the change they were proposing was worth the effort.

Recognition of the fact that there can be some resistance to change is another key element. Change may be seen by the individuals who must make the change as a threat to their power [Zaltman and Duncan, 1977]. Some of the firms in the field study had not implemented variable costing because manufacturing feared a reduction in its power relative to the sales department. As long as absorption costing was used, the sales department could not accurately determine the fixed and variable costs of the products. This prevented sales personnel from arguing for a sales price which was equal to the variable costs. The lack of detailed product cost information provided power to manufacturing. Installing an accounting system that made that information available to the sales department was met with resistance from manufacturing because it feared the loss of power.

To overcome resistance to change, the chief financial officer/controller (change agent) must find ways to deal with those kinds of fears. Management research [Stanislao and Stanislao, 1983]. indicates that good change agents create change in a way that reduces unnecessary negative impacts on individuals. Effective change agents also establish systems that allow those affected by the change to share in the positive results of the change. For example, the profitability of a firm should be enhanced if sales personnel are provided and use, in an appropriate manner, detailed product cost information. The rewards from increased profitability would be shared by both manufacturing and sales.

The importance of including operating personnel in the planning stages is the last element of successful change that is examined.This prescription is derived from the fact that effective change is not possible without the support of those who must implement the change. One way to gain that commitment is to actively involve, in the planning stages, those individuals who must make the change work. This participation, if it is to have the desired impact, must not be token involvement [Jenkins and Lawler, 1981]. Those implementing the plan must have an impact on the nature of the final plan that is adopted. In the case of implementing a variable cost system, the ideal way to elicit this involvement is to seek the assistance of the operating units in identifying fixed and variable costs. Leaders in the field of management accounting, such as Johnson and Kaplan, have stated that management accountants need to increase their communication with operating personnel [Johnson and Kaplan, 1987]. In addition, they argue that the operating personnel may have a better understanding of the cost structure than the management accountants. This participation would also increase commitment to the overall process.

Conclusion

The results indicate that most of the chief financial officers and controllers of the firms in this study have not implemented the prescription that organizations should use variable costing for internal purposes. Although the accounting literature has focused more on the technical approach to change, the reasons cited for not implementing variable costing were primarily nontechnical. The accountants of those firms that were successful in implementing variable costing were able to do so because they recognized that successful change requires both human relations skills and technical expertise.

The accounting profession needs to recognize the importance of the behavioral approach to change. Accounting curricula and seminars conducted by various accounting associations (AICPA, IIA, NAA, etc.) need to include material on the behavioral approach. Until this approach to change is properly recognized by the profession, accountants will not be properly trained as change agents and, therefore, cannot be expected to implement change.

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