

A New Era for

By Kelcey Thompson

Implementing
management
accounting to
inform business
decisions

Two of the main reasons why 46% of all businesses fail are emotional pricing and lack of knowledge about pricing. Do you know how to insulate your business from making those mistakes or how to make your accounting software program help you make informed decisions?

Accounting practices are evolving. In the past, companies focused primarily on financial accounting, which is exactly what it sounds like: performing accounting to supply financial institutions and CPAs with your information to make lending decisions or for taxes. Financial accounting is not an effective management tool; it is a financial tool. It does not give you the ability to control your data; it simply means entering data, and it provides you with only the basic information on your financial state. Thankfully, the evolution of accounting has led to management accounting.

Improved Decision-Making

In order to succeed in today's market, you have to know the gross profit for every department within your company. That is where management accounting comes in. It is the utilization of your data and accounting software program to produce information that leads to informed managerial decisions. It is the process of entering data to create managerial reports versus entering the data and creating basic financial reports. General managers and owners then can use these managerial reports to control their own destinies, knowing how, when and where to grow their businesses.

We have been told time and again by our clients that they know they should be printing their financial reports. They know they should be reviewing the reports on a regular basis, but these reports are not giving them the information they require. That typically means they are still using financial accounting, which simply shows how much is coming in and how much is going out. By implementing management accounting, their financials become the backbone of their businesses; no managerial decisions are

made without them.

When looking at management accounting and all it has to offer, here are some terms that may assist you:

- Chart of accounts: a list of the accounts to which your money is allocated (income, parts, equipment, office supplies, etc.);
- Cost of goods sold: charges incurred that are directly related to the sale/production of your goods or services (parts, equipment, commissions, etc.);
- Expenses: overhead charges incurred that are directly related to running your business (rent, salaries, office supplies, etc.);
- Departmentalization: a list of departments (profit centers) within your company (service, sales/installation, rental, etc.); and
- Gross profit: income minus the cost of goods sold.

Proper departmentalization depends on a comprehensive chart of accounts. Once developed, assigning all income and cost of goods sold to each department provides the gross profit for each.

Are you making a 40% or 5% profit? Are you sure you are making a profit at all? When our clients have implemented departmentalization, we have seen everything from personnel changes to a department being recognized as a true profit center versus being just a necessary evil.

The Next Steps

Burdened labor costing, flat rating, pricing and benchmarking are some of the programs that become available once you have begun performing management accounting.

Burdened labor costing is a calculation that provides you with the true cost of having direct labor (i.e., service technicians on the road). Say that after departmentalizing your income statement, you know that your service department is only making a 5% profit. Now you need to determine your burdened labor costing so that you can know the exact costs of direct labor. Right now, do you know how much that service technician

is costing you? Do you know if you are truly covering all of the costs involved? After completing burdened labor costing, many of our clients have experienced a shift from a negative profit to a 40% profit. We are able to tell you how many hours each service technician has to bill each day—not work, but bill—in order to cover his own costs. Without burdened labor costing, you may be throwing good money after bad trying to make a department profitable.

Flat rating is providing a service for a set price. It allows your customers to know how much they are expected to pay prior to the service being performed. This takes away their feeling of being nickel-and-dimed, while allowing you to know you have covered all of your costs and are receiving a set profit margin.

Pricing is a critical aspect of profitability and staying in business. Burdened labor costing provides the direct labor cost, vendor invoices reveal how much your parts cost, and time studies can tell you how long it takes to complete service calls. Create your flat rate pricing based on information from your business. We have constantly seen gross profits grow from consistency for all service calls—no more gray areas, no more guessing games in front of customers and no more 5% gross profits.

Benchmarking is a standard or point of reference in measuring the current value or profitability of your company in order to track performance and determine future business plans. It means deciding at what level you want your company and people to perform.

Departmentalization gives you gross profit per department—now you can set a benchmark for that department. Burdened labor costing tells you how many hours have to be billed each day—now you can set a benchmark for each employee. Flat rating provides you with average performance times—now you can set a benchmark for those service technicians in the field.

Once you have set your benchmarks, you have the ability to monitor your business. You have true numbers

Financials

at all times on which to base bonuses, employee retention and separation, business growth and more. You have control over the destiny of your business.

Failure due to emotional pricing or lack of knowledge of pricing does not have to happen to you. You have the ability to use management accounting and the programs above to create the proper pricing structure for your business based on your data.

Let financial accounting be a thing

of the past. Let profitability and growth be the future. *wqp*

Kelcey Thompson is vice president of Applied Management Group Inc. Thompson can be reached at kthompson@appliedmg.com or 262.697.4470.

For more information on this subject write in 1003 on this issue's reader service card.

Top-of-the-line

Filtration Products

Delivered on time and within your budget

- Full line of filtration media
- Ion exchange resins
- Includes solvent free and WQA certified
- Stainless steel and fiberglass exchange tanks
- Activated carbon
- US Resin brand and other top brands
- Pro chemicals

Our Products Are WQA Certified

Many of our products are certified by the Water Quality Association and our sales representatives are highly trained and advanced Certified Water Specialists (CWS). Your sales rep will be able to help you identify and select the best product for your specific need or application. And since US Resin has warehouses in California and Ohio, we also offer industry competitive pricing with low freight rates.

 **U.S. Resin Company**
888-565-1102 • Fax: 888-462-1101
info@usresin.com • www.usresin.com



A leader in the water conditioning industry since 1976.



Write in 759

UFI
UNITED FILTERS
INTERNATIONAL

Visit us at
Booth #160

FILTERS & VESSELS

**U.S. Manufacturer
for 40 years**

Member of Water Quality Association
Eastern Water Quality Association
Pacific Water Quality Association

901 S. Grant, Amarillo, TX Phone: 806-373-8386 Fax: 806-371-7783
www.unitedfilters.com info@unitedfilters.com

Write in 760

PureRite® Water Filtration Solutions.
The Smart Choice.

- Solutions for a wide range of water problems
- Integrated systems and logistics to speed delivery
- Advanced manufacturing techniques
- A full line with impressive breadth and depth

Manufactured by Kemflo, our PureRite® brand of high quality drinking water and whole house filtration systems and components delivers value for your customers and higher margins for you. With 30-plus years in water filtration, the company is a highly reliable resource for OEMs around the world. **To learn more, go to www.purerite.com.**

PURERITE®
SOLUTIONS. DELIVERED.

6635 Caballero Blvd.
Buena Park, CA 90620 USA
(888) 424-9185
www.purerite.com

See us at WQA Aquatech, Orlando, Booth 460

Drinking water and whole house sediment filtration systems and components

© 2014 Kemflo International PUR-1-3

Write in 758