



BY B. DOUGLAS CLINTON, CPA

The accountancy profession is facing a crisis. Evidence suggests that widespread systematic institutional bias permeates the accounting education system and fosters misperceptions that are applied to practice. Higher education has essentially omitted management accounting from the required portion of the accountancy curriculum. Junior-level *cost* accounting texts provide precious little guidance on how to run a business: Essentially, they replicate traditional cost accounting tools (e.g., cost-volume-profit analysis or variance analysis—not complete management accounting approaches) covered in principles-level courses while often just adding greater detail. (I use the term *cost* accounting throughout this article in the narrowest sense to refer to the support

of external reporting.) Public accounting in general, the National Association of State Boards of Accountancy (NASBA) and individual state boards, the Financial Accounting Standards Board (FASB), the American Institute of Certified Public Accountants (AICPA), and other groups have displayed an approach to the profession that has elevated financial accounting to an undeserved position. Academic *research* also overemphasizes financial accounting (as I'll explain later).

In the area of practice, the 2003 Institute of Management Accountants (IMA®)/Ernst & Young (E&Y) joint survey (whose results were published in "Roles and Practices in Management Accounting Today," in the July 2003 issue of *Strategic Finance*) offered startling statistics that provide a siren song for the profession. The data in the

When will the accountancy profession finally recognize the value of management accountants?



survey revealed that 98% of decision-making users of accounting information believe it is significantly distorted and complain of impaired cost visibility, yet 80% of these respondents said change wasn't a priority. Professional accountants in business (PAIB)—I'm borrowing the term from the International Federation of Accountants (IFAC)—and academics have been arguing among themselves over which management accounting tool is better—essentially fighting an internecine battle that prevents us from helping management make decisions. At the same time, opportunistic consultants are continually rushing in, all too willing to provide services that reflect great inconsistency and produce an equally wide range of ineffective results. Moreover, managers don't know how to compare accounting optimization methods such as activity-based

costing (ABC), resource consumption accounting (RCA), or Lean Accounting, so they seem to have lost hope that any change would be beneficial or cost effective given that contemporary management accounting innovations have left them dissatisfied.

These and other influences have resulted in excessive regulation and inadequately trained professional accountants in business. The dominant accounting approach in business practice—traditional standard costing—doesn't have the ability or proper focus to provide useful data for decision support—accounting's most important and fundamental purpose. To end the crisis, the global accountancy profession and its thought leaders must acknowledge the problem and be willing to address it on behalf of decision makers in organizations vs. the

parochial interests of financial accounting or those out for a fast buck.

RECENT HISTORY

During the late 1990s, the premier organization representing PAIB in the United States—the Institute of Management Accountants (IMA®)—was suffering from an identity crisis that led to a dilution of focus. Responding to declines in university accounting program enrollment and professional membership, IMA decided to become more inclusive. It began the Certified Financial Manager (CFM®) certification program, changed the name of its flagship publication from *Management Accounting* to *Strategic Finance*, and made additional efforts to appeal to those in finance and information systems (rather than just accounting). IMA also didn't seem to provide a significant degree of intellectual leadership or strong advocacy for the profession and its constituents. These moves caused poor results from which the association is still trying to recover: PAIB felt somewhat abandoned, many accounting advertisers withdrew their support from the magazine, and finance and information systems professionals largely failed to get on board.

Meanwhile, the entire profession seemed to be suffering from a decline in the level of disciplined practices, or a lack of accountability for the rigor of management accounting approaches as implemented. The most popular new allocation method of the 1990s, activity-based costing, lost favor with many companies, and opportunistic consultants parading as the discipline's leaders struggled to offer effective alternatives. As practitioners and academics continued to bicker about which method or new tool was better than the other, many of the primary beneficiaries of those tools (i.e., management) walked away from the table, unable to see the value proposition of adopting proposed new tools that reflected the "flavor of the day." In addition, leading PAIB and accountancy professors were (and still are) inappropriately reflecting an external financial accounting focus rather than internal decision support as the primary purpose of the accountancy profession. An example of this is a quote from a May 2005 *Journal of Accountancy* interview with Steven F. Vieweg, CEO of the CMAs of Canada: "Every management accountant must have his or her roots in financial accounting, specifically GAAP."

Considering our situation, it's quite ironic that Vieweg's comment was made in an article titled "The future has never looked brighter." Does *financial* accounting have the biggest or most important presence in defin-

ing the accountancy profession? The fact that public and financial accounting dominate the landscape is a classic example of perception defying reality. What *is* real, suggests 2005 data from the Bureau of Labor Statistics, is that of the five million PAIB in the U.S., as many as 93% work inside organizations in value-adding, decision-support roles (vs. the other 7% who work in assessment or compliance roles).

Is an increased auditing presence from public accounting what the profession needs? IMA has publicly recognized the burden of Sarbanes-Oxley legislation, citing estimates that increased regulation has eroded shareholder value to the tune of \$35 billion, with many of the associated costs being shifted to the auditing firms, who have taken a conservative, *document everything* approach to compliance in order to avoid litigation resulting from negative audit outcomes. In examining the root causes of this huge economic hit on publicly traded corporations and the U.S. economy, a recent IMA study, *Management's Assessment of Internal Control over Financial Reporting*, corroborates what the Securities & Exchange Commission (SEC) only recently acknowledged is a major driver of the cost: While the external auditors have had guidance in the form of Public Company Accounting Oversight Board (PCAOB) Auditing Standard Number 2, inside management has had no such guidance that allows them to conduct practical, cost-effective assessments of their systems of internal control.

Now our profession has reached a crossroads. Key trends such as the increasing complexity of accountancy support of business decisions (stemming from increasing business complexity in general), increasing global competition, and the availability of Internet commerce will force PAIB to step to the forefront or become irrelevant. To be successful, they must recapture the respect of their primary customer—management. To help them do this, the profession will need to make some significant changes.

CAUSE AND EFFECT

Table 1 contains a short list of reasons for the current crisis in accountancy. If I had to pick two of the largest problems from the list, they would be: (1) Textbooks tend to focus on external reporting rather than on internal decision making and support, and (2) the degree of regulation in the U.S. capital markets is too great.

Academia and practice converge in fostering the current crisis, so understanding their roles is the first step toward a solution. The accountancy knowledge supply chain in the U.S. depicts the capture and dissemination of

Table 1: Indicators of a Crisis in Accountancy

- ◆ Financial accounting dominates practice (strong capital markets seem to drive external regulation and discipline in practice).
- ◆ Cost accounting textbooks tend to focus on external reporting rather than internal support to help management make the best decisions.
- ◆ Public accounting (not PAIB) is the primary funding source of higher-level accounting education, swaying the influence of professors toward compliance accounting.
- ◆ Corporations aren't able to compete with public accounting in funding higher education given corporations' need to fund all business functions (i.e., not just accounting).
- ◆ Professors often foster the image of PAIB being a second-class citizen (likely a product of the funding issues or the lack of influence surrounding PAIB).
- ◆ There is a strong history of common knowledge about external reporting participants (e.g., CPAs) but not about those "management accounting" professionals helping their company management make strategic decisions (e.g., Certified Management Accountants (CMA®s)).
- ◆ Strong capital markets in the U.S. and a high degree of regulation are swaying efforts toward external financial reporting.
- ◆ Historically, organizations representing PAIB haven't displayed a clear focus of advocacy for the profession of management accounting (but this is improving).
- ◆ There is a lack of best-practices discipline or a clear path to implementation or self-regulation.
- ◆ Inability to require best practices given authority but no teeth to enforce compliance (i.e., authoritative documents are present and are continually being produced by IMA, but companies are not legally required to follow them).
- ◆ CFOs and other professionals don't trust internal system information.
- ◆ Funding of improvement in decision support isn't a priority in organizations surveyed (IMA/E&Y 2003 survey).
- ◆ Other countries applaud our sophisticated capital markets yet beat us in the marketplace. (Because there is less regulation in other countries, companies have a greater ability to focus on decision support.)
- ◆ Other countries place PAIB on a more equal footing with financial accountants.
- ◆ There is an emphasis on using overly simplistic methods to address complex operations.
- ◆ Confusing operational cost concepts (fixed and variable) with decision cost concepts (avoidable and unavoidable). For example, the term "fixed" doesn't mean that the cost is unavoidable with a particular decision—it merely means it doesn't change with output.

knowledge and practices that reflect the present state of imbalance—an overemphasis on financial accounting. It starts with the writing and production of cost accounting textbooks and flows through certification testing that primarily reflects the educational exposure to accounting that students receive in transitioning to become professional accountants in business. From experience gained in professional practice, corporate accountants, controllers, internal auditors, and a variety of analysts (and individuals with other titles) develop their own beliefs and practices that remain largely rooted in the education they received. Thus, we must first look at academia.

ACADEMIA

When I examine our cost accounting textbooks, it's remarkable to me how heavily steeped they are in financial accounting. Chapter titles, organization, and content tell the story clearly. Cost behavior chapters slice costs into the operational concepts of variable and fixed yet don't introduce decision cost concepts of avoidable and unavoidable until much later—and then only in a special context. Early cost chapters appear more concerned with the income statement format and cost-of-goods-sold/manufactured format than the costs themselves. Job costing, process costing, activity-based costing, and standard costing are all described as methods for assigning costs to final cost objects. All four allocate costs to separate items in the general ledger (GL) into inventory costs and cost of goods sold for external reporting purposes. Support department cost chapters teach us how to force all of their costs into one or more overhead pools so that they can be fully absorbed into the giant mass of overhead that's allocated to end products en masse.

When we finally get to the performance evaluation chapter, we find the age-old methods and metrics that are used to calculate results by which the external reporting world lives and dies. These always include return on investment (ROI), residual income, and (due to popularity) another form of residual income—economic value added (EVA®). Essentially, what we have with the typical cost accounting text is a financial accounting book with a bit of pop accounting and a few decision-support techniques thrown in for good measure. Perhaps this is why it's so easy for many professors to switch back and forth in teaching either cost accounting or financial accounting—because they are often taught to serve similar interests.

Also, how many professors *teach* “cost” accounting yet still advise their students that public accounting is the best career path? How many believe that the curriculum

is skewed toward financial accounting? Just look at the number of required upper-level courses. Most programs have only one required upper-level course for PAIB, and it's a *cost* accounting course that primarily replicates the principles-level cost texts but with incrementally more detail. We should at least consider including an accounting information systems course in that list since PAIB operate the technology involved with their jobs.

How about the research agenda in academia—has it remained balanced? Hardly. During a panel discussion at the American Accounting Association (AAA) annual meeting last August, one panelist pointed out that financial accounting specialties make up only 17% to 19% of the total AAA membership, yet more than 50% of the articles published in the AAA's flagship journal, *The Accounting Review*, are about financial accounting. At the same conference, keynote speaker Anthony Hopwood, editor of *Accounting, Organizations, and Society*, expressed similar disappointment with how the profession has increasingly narrowed its focus to financial accounting at a time when we should be broadening our focus outside business and cross functionally within business. With accounting higher education evidencing this narrow focus, is it any wonder that financial accounting dominates?

PRACTICE

I've already mentioned the results of the 2003 IMA/E&Y survey, yet three issues stand out:

- ◆ Costs aren't immediately visible, tool adoption isn't a priority, and traditional tools are still used.
- ◆ The predominant belief is that costs are distorted, allocated costs are increasing, and allocation is where most distortion occurs, yet these problems aren't being addressed.
- ◆ Complexity is increasing, yet traditional allocation techniques are used that don't account for or consider this complexity (e.g., 70% are direct labor based).

All these issues have the common theme of increasing complexity but addressing the increasing complexity with steadfast simplicity.

Managers (and the rest of us) have a tendency to use the *easiest* method available to get a job done, usually to address the immediacy of a *pain point* whether it's from SOX compliance or rapidly expanding business complexity requiring decision-support data on which someone can act. But *easiest* doesn't translate to *optimal over the long run*. For example, I would like to assume that fixed costs are always unavoidable, but this isn't true for all decisions.

Organization theorists agreed years ago that complex systems are necessary to deal with organizational complexity. Remarkably, PAIB have been tempted to go in the other direction. This is certainly encouraged by Just-in-Time with its use of backflush costing, but not all companies can or should use JIT. The good news is that today we have the benefit of integrated, enterprise-wide systems (such as enterprise resource planning (ERP) systems) that make dealing with complexity much easier than in the past. These systems are capable of maintaining the integrity of information as it flows and changes from multiple touch points across an organization's value chain. Once managers are shown how accounting can take advantage of these systems, complexity can be handled without an army of accountants. (Value chain integration is "the ability to track quantitative elements (quantities) in various operational applications and to overlay them with dollar values without the need for data duplication" and is discussed in more detail in an article I wrote with Anton van der Merwe, "Management accounting—approaches, techniques, and management processes," in the May/June 2006 issue of *Cost Management*.)

This brings us to market forces. The strength of the financial capital markets in the U.S. is sophisticated beyond all other countries. (This is merely an artifact of having the largest free-market economy in the world.) The Certified Public Accountant (CPA) designation is something that all people seem familiar with, even if they don't understand what it means (but the Certified Management Accountant (CMA®) designation is not). The degree of regulation of our companies in terms of external reporting requirements is unrivaled as well. In recent years, just when we thought it couldn't get worse, the U.S. Congress supplied a knee-jerk reaction when told to "do something" about the numerous ethical violations of monstrous proportions at Enron, WorldCom, and Tyco, and the SOX legislation made its way to the marketplace. Audit fees soared as a result. IMA has publicly stated that the problem isn't the SOX *legislation* but the implementation that the SEC acknowledges is skewed to support the auditing firms vs. the practitioners in the trenches struggling to see the value in their compliance programs.

Congress failed to see that auditors can't inspect ethical behavior into business reporting—companies must build the behavior into their corporate infrastructure. Moreover, no one recognized the importance of PAIB to the process. The first response of corporate CFOs was to call their external auditors, but the primary intention of the regulation was to force managers to become accountable

Changes Needed in Management Accounting

Academics must...

- ◆ Consider as unacceptable the domination of the profession by financial accounting.
- ◆ Submit themselves as learners rather than teachers, and be open to new ideas.
- ◆ Be willing to lead as unbiased guardians of essential truth.
- ◆ Support the PAIB's customer—management.
- ◆ Go beyond replicating what they've been taught.

Practitioners must...

- ◆ Widely recognize that accountancy is on a burning platform (i.e., in major crisis).
- ◆ Learn what management needs and wants.
- ◆ Include management in developing or embracing a solution.
- ◆ Focus on ensuring the success of the enterprise rather than the accounting profession.
- ◆ Institute disciplined practices based on sound decision-support principles.

Publishers must...

- ◆ Be willing to take risks as opposed to perpetuating popular myths.
- ◆ Seek progressive writers who are willing to embrace accountancy's primary customer.
- ◆ Avoid the merely popular methods and focus on covering *effective* methods.
- ◆ Accept nothing less than content based on sound principles that will help PAIB/management accountants guide management to make the best decisions.

for their financial statements, which, of course, they were already required to do. IMA has made the point to the highest powers of the SEC that the way to assure a positive audit outcome *and* drive sustainable business performance is to have properly educated professional accountants in business doing their job from the inside in the areas of decision support, planning, and control.

Now let's consider the knowledge supply chain effects that shape our profession. Accountants often want to identify more with the profession than with the entire accountancy knowledge supply chain. This may seem like a subtle point, but the view is important in how it shapes practice. Despite the recent scandals, accounting in gener-

al tends to be a proud and well-respected profession. The problem is that we can be so hung up on the proud profession that we can find ourselves in our own little compliance world. With all its sophisticated and complicated rules, financial accounting in the U.S. forces PAIB to place their concern *first* on the rules/law of compliance, then on decision support (if there's time for it). It's time to remember that management is our real customer.

FINDING THE ROAD TO A SOLUTION

The crisis in accountancy won't be easy for academics or practitioners to rectify, but describing the problem and suggesting a proposal to remedy accountancy's flaws is a start on the road to ending it. Achieving a meaningful solution must include the changes shown in the sidebar (p. 29) for academics, practitioners, and publishers.

It's time for academics to reject the unacceptable dominance by the financial accounting requirements of our programs, our advice to students, and our behavior. We must reorient our thinking to new ideas rather than continue replicating the external focus that currently dominates our field. We should examine whether what we teach concentrates on management decision support *first*—and then make sure it does.

Management must be a part of the process involving practitioners. They will have to be convinced that professional accountants in business have something to offer them. We must determine what management needs and wants and find a way to give it to them instead of just talking to each other. We must shift our focus to ensuring the success of management and the enterprise rather than the success of the accountancy profession. If we do this, PAIB will succeed as well.

Publishers will need to take new risks in seeking the solution for management accounting. That means making large changes in the way most *cost* accounting textbooks are written. The difficult part will be avoiding traditional content just because they believe it's what the customer wants. Thus, the onus falls on professors to demand better texts. Quality control will require a basis of conformance to sound management accounting principles as opposed to what was in the last edition. Publishers can't be responsible for the change, but they can be a part of it, and their role will be meaningful.

HOPE FOR THE FUTURE

Cost accuracy and transparency can be improved greatly with cost assignment that follows operational quantities (i.e., physical, nonfinancial resource consumption) in inte-

grated ERP systems without reinventing transactions separately in the accounting system. The consumption of quantities of resources is already being tracked by a separate module in ERP systems. Cost accounting only needs to value the consumption of those quantities. As suggested by Anton van der Merwe at IMA's Annual Conference in June 2006 and in a letter to the editor in the November/December 2006 issue of *Cost Management*, the GL is an artifact of the external reporting system that isn't required for sound management decision support. The GL should become a *recipient* (rather than a source) of cost information where cost management is achieved by merely tracking quantities and the values that are associated with them. If nonfinancial quantities are being accounted for by an operational system already, duplication, inaccuracy, and increased cost will result from the traditional approach of tracking nonfinancial quantities separately in the management accounting system.

Although professional accountants in business still aren't recognized as clearly adding value to the bottom line, the outlook remains hopeful. IMA has taken important steps to convince the accounting profession of this. The association has recognized the seriousness of the problem, has demanded that the profession place a proper emphasis on strategic decision making, and has encouraged the increased use of properly educated professionals who are capable of adding value to an organization's bottom line. Now IMA is trying to return to an appropriate emphasis on "management accounting" by issuing new/updated Statements on Management Accounting (SMAs), an independently validated certification program, new research initiatives, and a research funnel of professional development products reflecting the body of knowledge and the needs of adult learners. Its leaders are speaking out—as evidenced by the many public statements on SOX problems (via meetings with the SEC, comment letters, press releases, research studies, articles, etc.).

We have taken the necessary first step toward a solution: recognizing there's a problem. Yet professional accountants in business and professors must also acknowledge the problem as a community of professionals and embrace a willingness to achieve meaningful change. The needs of decision makers are at stake. ■

B. Douglas Clinton, CPA, Ph.D., is the Alta Via Consulting Professor of Management Accountancy at Northern Illinois University. You can reach Doug at (815) 753-6804 or clinton@niu.edu.