The Changing Role of Management Accountants in a Lean Enterprise – From ‘Bean Counter’ to Delivering Customer Value

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Executive Summary
Implementing Lean in organizations requires significant changes for all managers and staff including support staff, such as cost and management accountants. Lean enterprises utilize different forms of control and have disparate management information requirements than traditional organizations. Lean accounting involves a move away from traditional management accounting to better meet the needs of Lean organizations.

The change for management accountants can be challenging with substantial differences in the roles and requiring the learning of new skills and ‘unlearning’ of some existing ones. The good news is that, for those who can adapt, working in Lean organizations enables management accountants to move away from the ‘bean counter’ role to greater participation in the business, adding value to operational processes and strategic decisions.

Even for management accountants in non-Lean enterprises, Lean accounting provides insights and positive examples as to how some of the problematic ‘sacred cows’ of traditional management accounting can be slayed and replaced with more valuable information and processes.

Introduction
The different management information and control needs of Lean enterprises and the management and cultural focus on customer value, continuous improvement and elimination of waste creates demand for adapted management accounting, known as Lean accounting. This article first explores the traditional roles of management accountants. A brief overview of Lean concepts is provided including the nature of controls and information requirements in these organizations. Limitations in traditional management accounting in supporting Lean organizations are explored. The concepts of accounting in Lean enterprises are discussed and flowed through to changes in the roles and skills of management and cost accountants. Finally the example that successful Lean accounting can provide management accountants in non-Lean organizations is considered.

The Traditional Role of Management Accountants
While in some organizations the roles of management accountants and cost accountants are separate, in many companies cost related activities are encompassed in a broader role of management accountant. It is this broad definition of management accountant that is examined here. Management
accountants generally report through to the Financial Controller in the finance function, with the Financial Controller, who typically looks after management and financial accounting, effectively the head management accountant.

While the roles of management accountants can differ across organizations, the role typically includes the following activities:

• Collecting and coding product cost information from financial transactions, developing product cost standards and reporting the cost of products (on a unit and total basis) and valuing inventory in the financial accounts.

• Administering the annual planning and budget cycle, developing and populating budget templates and consolidating divisional budgets into an enterprise wide version.

• Producing monthly management reports including income and balance sheets for the month and comparison and analysis of monthly performance against budget and identification of variances against standard costs. Researching and reporting variances against budget and standards.

• Performing ad-hoc financial analysis to support operational manager and senior executive decision-making.

• Assisting with change projects, such as the implementation of new systems or development of new products.

![Figure 1. The change from ‘bean counter’ to business partner](image)

Historically management accountants have been tagged with the stereotype of ‘bean-counters’ due to the sheer volume of time spent recording and inputting data and producing reports with little time spent supporting operational decisions1. Over the last 20 years or so there has been an attempt in many organizations to migrate
the management accountant to a ‘business partner’ supporting operational managers by providing relevant management information and providing insightful ad-hoc analysis. This change is show in figure 1. In some organizations, the ability of management accountants to provide higher levels of support has increased due to automation of some of their cost collection and data input activities through the implementation of ERPs.

In many organizations, operational managers remain disappointed by the value provided by management accountants who remain bogged in time consuming budget processes, performing detailed variance analysis and removed from operations. The introduction of Lean accounting has the potential to change this.

A Brief Introduction to Lean

Lean is a continuous improvement system that developed out of the Toyota Production System. Originating in manufacturing, the Lean approach is now increasingly being used in service industries such as government, health care and financial services. While Lean has continuous improvement tools, such as 5S (order, cleanliness and visibility in work spaces), the 5 whys (root cause analysis) and value stream mapping, it is much more than these tools. Lean is an enterprise wide management philosophy involving changes in management systems, culture, organizational structures, processes, performance measures, employee skills and rewards.

Lean focuses on providing customer value to meet customer expectations on product/ service attributes, quality and timely delivery. A core principle of Lean is continuous improvement focusing on enhancing processes, eliminating waste and reducing inventory levels. A production system of flow is developed with one-piece flow the ideal and batch sizes minimized. Production is pulled through the system from customer demand rather than being produced to inventory for later sale.

Under Lean the organization is restructured from the traditional functional structure to value streams (all of the resources required to produce a family of products from order to delivery and including support staff, such as management accountants) and production organized into cells. This structure enables a greater focus on customer value and reduces the silos and conflicting performance measures of traditional organizations. Respect of employees is a key plank of Lean with employees empowered to improve processes and solve problems.

These attributes of Lean result in Lean organizations having different forms of control and management information requirements than traditional organizations. As control moves from hierarchical management control to the workers, information that is timely and relevant to the work performed and understandable by non-accountants, is required. Management information needs to address organizational objectives such as customer value, quality, continuous improvement and elimination of waste, reduction of inventories, increasing available capacity and support decisions on the utilization of freed up capacity.
Limitations of Traditional Management and Cost Accounting Information

Criticisms of traditional management accounting systems and information are not new or constrained to their application in a Lean Enterprises. Johnson and Kaplan published many of the issues raised by Lean Accounting advocates almost 30 years ago in Relevance Lost.

However, the inadequacy of traditional management accounting is greatly magnified in Lean enterprises due to specific management information requirements and the focus on continuous improvement and waste elimination across all processes, including accounting processes.

Traditional management accounting simply does not provide information required to support the Lean principles of customer value, continuous improvement and employee empowerment. For example, many manufacturing companies still use standard costing systems. Monthly reports are produced weeks into the next month, which is too late to identify and resolve problems that may have occurred six or seven weeks earlier. Complex variance reports are difficult to understand even by accountants so provide limited value to workers on the floor. The costing standards include arbitrary allocations (especially overhead), treat direct labor costs as variable even though they are often fixed in the short term and don’t differentiate between fixed and variable costs. These issues can result in flawed management decisions when standard costs are used. This is particularly an issue in Lean organizations that have freed up substantial capacity and are analyzing options to produce special orders, bring outsourced products back in house or introduce new products. Traditional management reports provide little insight into key objectives such as delivery reliability and capacity constraints and availability. In some organizations this has been augmented by non-financial performance measures using methodologies such as the Balanced Scorecard.

Traditional management accounting can contribute to decisions and reinforce behaviors that are the opposite of Lean concepts. Full absorption costing motivates overproduction and large batches to reduce reported per unit cost and increase perceived efficiency resulting in high levels of inventory causing space issues, obsolescence and lack of flexibility. Allocations of overhead based on direct labor hours can focus managers on reducing staff, which conflicts with the Lean philosophy of respect for people, rather than focusing on the overheads themselves.

Traditional static budgets are also problematic in a Lean environment. Budgets are often set in the months prior to the beginning of a year and seldom accurately forecast customer demand. This can result in managers overproducing to inventory to avoid unfavorable budget variances if customer demand is less than budgeted and can dampen the focus on continuous improvement if budgets are achieved. Traditional budgets and performance measures can result in each department seeking to optimize their performance to the detriment of the enterprise.
Financial statements can provide a misleading view of performance in the early years of implementing Lean even though customer performance improving significantly and cash flows increasing. The running down of inventories results in the financial accounts reflecting performance getting worse as overhead previously including in the value of inventory are expensed when incurred.

In Lean organizations all processes, including accounting processes, are subject to continuous improvement and elimination of waste. Traditional management accounting involves significant waste. With control moving to the factory floor and issues in using standard costs to support decisions, the value of recording hundreds of transactions and spending weeks on variance analysis is questioned. A major purpose of standard costing is to allocate costs between the cost of goods sold in the income statement and the inventory asset in the balance sheet. In Lean Enterprises inventory levels are reduced substantially to the point where more simple and less wasteful approaches to inventory valuation can be implemented without materially affecting the financial statements. Traditional budgeting and thousands of hours spent over months creating and reporting against out of date budgets is of little value in organizations where production is driven by customer demand.

Management Accounting in Lean Organizations
The focus here is on management accounting to provide information to manage Lean organizations rather than implementing Lean concepts to improve all accounting processes, such as financial reporting, payroll processing and accounts payable. Accounting in Lean organizations is a relatively new and evolving field, being the subject of a number of books over the last dozen or so years. Recent academic studies of 244 US companies have found that Lean accounting and other control practices work together and the implementation of Lean accounting improves the performance of Lean enterprises. When introduced into Lean organizations, Lean accounting is generally implemented gradually with aspects of traditional accounting simplified or dropped as Lean controls and reporting are introduced into the organization and management are comfortable that these controls are adequate.

Lean income statements (see figure 2 for an example) are reported by value stream and include actual costs rather than standard costs and variances. Movements in the value of inventory are reported separately to isolate the implications of reducing inventory levels. The value stream includes support staff assigned to that value stream with labor reported in total rather than broken down into direct and indirect components, simplifying administration. As most staff work in value streams, corporate overhead (often consisting of the plant manager and a few functional leaders) is quite low and is generally not allocated to value streams. While the objective is to limit apportionment of costs, sometimes large, costly equipment are used across multiple value streams. In Lean speak, these assets are known as Monuments. The costs of these monuments are apportioned to value streams based on usage with the objective to phase Monuments out and replace them with machines in the value streams.
Financial and non-financial performance measures form an important component of controls in Lean accounting. Measures are strategically aligned and linked and reported at the company, location (monthly), Value Stream (weekly) and cell/department (daily and hourly) level. Value Stream and cell measures are reported in a form that is very visible and understandable to workers posted on a notice board on the shop floor. Measures include operational measures (customer related: eg. on-time customer shipments; quality related: such as first time through; throughput measures: units per person and dock to dock; inventory measures such as inventory turnover), capacity measures (productive, nonproductive and available) and financial measures (such as revenues, material costs, conversion costs, return on sales).

Product costing is usually simplified under Lean accounting. In traditional manufacturing organizations, standard costing is used as a form of control, to value inventory for financial reporting and to support management decisions. Lean emphasizes alternative and more timely controls such as increased visibility, staff peer control and frequent performance measurement. A key focus of Lean is manufacturing to customer demand resulting in significantly lower inventory levels enabling less complex methods of inventory valuation. Consequently, standard costing is often ultimately eliminated or greatly simplified substantially reducing the time spent processing transactions and analyzing variances. Reported actual per unit product costs for a period are often simply value stream costs divided by the volume of product shipped. While this becomes less meaningful when there is significant diversity in products or service produced by a value stream or when the
value stream does not include all organizational processes, Lean accounting proponents argue that recorded costs are of limited value to support decisions. Product costs for decision-making are considered next.

In Lean accounting, product costs for decision-making has a number of aspects including:

- **The market, rather than company costs, sets the price of products.** The assumption is that the markets for most products is highly competitive and the ability to set pricing highly constrained, limiting the value of putting significant resources into recording product costs. In my experience, when the company and competitors are producing a diverse range of products for many different customer markets with potential for cross subsidization there are often opportunities for those that understand their product and customer costs. The level of understanding of product costs required will be dependent on the degree of product and customer diversity. However, under Lean, as in all organizations, the detail and frequency of cost analysis/reporting needs to consider the value of the information for decision-making versus the cost of producing it.

- **Target costing:** it is important to consider customer value up-front in designing or redesigning products and processes. This includes identifying target customer markets, product features required, competitor offerings and required pricing. This is then backed into a target product production cost to which the product is designed.

- **Incremental/marginal costing for analyzing special orders and bringing outsourced production/processes back in house.** As stated earlier, Lean frees up substantial capacity. In Lean accounting, instead of using a full absorption standard cost for these decisions, total value stream revenues and costs are modeled under different scenarios. This is important as many cost in the company are fixed in the short term (including direct labor) and pricing above the marginal cost will provide benefits to the company. Of course, capacity needs to be carefully monitored (as it is in Lean accounting) and the potential long-term impacts on pricing considered.

- **Throughput costing is important in product mix decisions.** In Lean production cells have relatively consistent team staffing. Decisions on which products to produce when capacity is constrained need to consider the volume throughput for each of the products along with the contribution of the products for a contribution per throughput hour comparison. This requires a good understanding of bottleneck constraints throughout the process.

*Intensive annual budgeting processes are replaced by rolling forecasts and monthly sales, operations and financial planning.* This reduces the significant effort of developing static and soon to be out of date budgets before the year begins. Instead of working to explain variances to these irrelevant budgets, time is spent each month updating rolling forecasts and developing/revising action plans.
Changes to the Role of Management Accountants in Lean Organizations

This article started with the traditional role of management accountants and the demands of operational managers and ambitions of management accountants to move the role from administrative, 'bean counters' to 'business partners'. Success in a Lean enterprise will require management accountants to go further – beyond the 'business partner' role to being a true member of the operations team delivering customer value.

*Management accountants move from being isolated in a support function to becoming part of operations* in a Value Stream structure and are expected to contribute as such. Many of the activities traditionally performed by management accountants are eliminated or greatly simplified in a Lean company. This includes simplified and more relevant monthly income statements, significantly less effort on standard costing and variance analysis and replacement of the cumbersome and time consuming planning and budgeting cycle with a more frequent rolling forecasts and action oriented sales, operations and financial planning.

*Enlightened management accountants can make an even bigger contribution to the success of the organization* despite the removal and reduction in these traditional management accounting activities. Eliminating and reducing these wasteful, time-consuming activities will provide more time to enable management accountants to use their skills to enhance customer value. Continuous improvement requires constant analysis of operations and reporting of relevant, timely performance information. The inevitable freeing up of a capacity through implementing Lean will open many opportunities for the company to utilize that capacity to create more customer value. This will include delivering special orders, developing new products and taking on new customers and a greater portion of existing customers’ business when the improved customer value of Lean is recognized. It will enable currently outsourced processes and production to be brought back in-house. The financial analysis skills of management accountants can potentially add substantial value to Value Streams in assisting with continuous improvement and supporting Value Stream leaders with these product and production decisions. While Lean accounting greatly simplifies management accounting, management accountants can help shape the appropriate level of understanding of product costs dependent on the diversity of products produced by value streams.

*While a great opportunity exists, it will require the acquisition of new skills and knowledge and difficult unlearning* for many management accountants. Management accountants will need to embrace the Lean philosophy and tools, both in the operations side of the business but also Lean accounting. This involves learning about Lean through reading and attending internal and / or external training. It means participating in Lean activities, such as facilitating Kaizen events (continuous improvement sessions) and attending GEMBA (work place) walks. It requires learning about Lean accounting, both producing timely, relevant information to support the business and removing waste from accounting processes.
For some it will require unlearning much of what they had learnt and applied previously in standard costing and reporting. They will need to gain a real understanding of operations including processes through cells, capacity and bottlenecks. They will need an understanding of the real behavior of costs (fixed and variable) and be able to model the financial implications of different scenarios cognizant of capacity constraints. This includes learning and applying throughput and target costing techniques.

Relevance of Lean Accounting to Management Accountants in Non Lean Enterprises

The limitations of traditional accounting are not limited to organizations that implement Lean as indicated in Relevance Lost. The information requirements of Lean, the focus on continuous improvement and the elimination of waste and the restructuring to Value Streams magnifies the issues associated with traditional accounting and builds the impetus for change.

![Figure 3. A Lean call to action for management and cost accountants](image)

Moving to Lean provides a cultural and management framework to break away from traditional management accounting methods to a greater value added role for management and cost accountants. The experience of Lean accounting can inform accountants in non Lean companies. So what should cost and management accountants do?

It is not appropriate for non-Lean organizations to move to full Lean accounting without a Value Streams structure or without replacing traditional controls with those embedded in Lean and still reporting high inventory levels. However, there are still lessons to be learned by management accountants in other organizations. As Lean accounting advocates have indicated, many of the aspects of Lean accounting are not new and have been applied in non Lean organizations. For example, Beyond Budgeting has been a movement away from traditional budgeting to rolling forecasts and the Balanced Scorecard made popular the use of various categories of financial and non-financial performance measures to augment
Likewise, the need to consider relevant costs and capacity in new product and make versus buy decisions has long been advocated for all organizations\textsuperscript{12}. The Lean accounting movement provides insights and successful examples of the slaying of some traditional management accounting cows to motivate and guide the way for improvements in other organizations.

While the implementation of Lean must come from the top, management accountants can perform a significant role in building the momentum and a business case for a move to Lean. Using some of the performance measures common in Lean organizations enables non-Lean organizations to be benchmarked against those on the Lean journey highlighting the potential benefits of going Lean.

Conclusions
Adapting to the requirements of a Lean enterprise will be difficult for many management accountants. Not all will be able to adapt to the new role. Those that can develop the new skills required will gain an in-depth understanding of operational processes and participate in improving the production of products and services to better add value to customers. The understanding gained of the behavior of costs in the organization, cell and value stream capacity, throughput, and bottlenecks along with strong analytical skills will enable them to assist company executives and value stream leaders with important decisions to utilize freed up capacity, such as pricing special orders, bringing outsourced services back in house and introducing new products. For management accountants in non-Lean organizations, learning and experimenting with aspects of Lean accounting and commonly used performance measures will provide insights as to how management accounting can be improved and potential help influence a case for implementing Lean.

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NOTES


3 This article gives a very high level description of Lean. There are many books that give a more detail treatment including Lean Thinking: Banish Waste and Create Wealth in Your Corporation (2003) by James Womack and Daniel T. Jones published by Free Press New York.


8 Relevance Lost: The Rise and Fall of Management Accounting.
9  *Practical Lean Accounting: A Proven System for Measuring and Managing the Lean Enterprise.*

