

NEW IFAC PUBLICATION STRESSES THE NEED FOR BETTER COSTING TO SUPPORT DECISION-MAKING

To be an effective strategic business partner, the professional accountant in business needs to have a deep and critical understanding of the organization's costs, which involves harnessing the power of cost measurement and modeling with incisive information to support effective management decisions. By helping their organizations to understand resource consumption and costs, professional accountants can better show how value is being created or destroyed.

IFAC's International Good Practice Guidance, *Evaluating and Improving Costing in Organizations*, establishes six fundamental principles of improved costing to provide useful managerial information for internal use while still efficiently supplying external financial reports with the transparency needed by lenders or other stakeholders, such as the investment community and regulatory agencies.

Developing a decision support model

With the right mindset and approach, professional accountants in business can not only develop a decision support model to help management better understand the causes of events (why things happen) and develop a clear and direct connection to operations (to evaluate change options), but also support planning for desired future outcomes.

The effective use of costing to support decision-making requires information based on well understood cause-and-effect relationships between an output and the economic inputs required to produce it. This publication warns that highly aggregated cost information, compiled predominantly for external reporting purposes, may not reflect such relationships closely enough to adequately support decisions about future internal strategies or operations.

Professional accountants in business play a significant role in ensuring that the costing models and systems they use provide relevant information and analysis to support performance evaluation as well as planning and management decisions.

Costing information is the basis of the decision support model that is essential input to both interpretative, diagnostic activities to analyze past performance, and to predictively guide decisions about every aspect of an organization's future operations.

Supporting value creation

The publication highlights the sustainable value for stakeholders that can be created by improving the efficiency and effectiveness of an organization's value-creating operations. Therefore, professional accountants should recognize the constraints of looking at organizational performance solely in terms of a financial accounting model. High quality and relevant managerial decision support means that employees, supervisors, and managers throughout the organization receive the information and analysis that helps them to make value-creating decisions.

Appropriate understanding and analysis of resource consumption and costs is essential to operational management. This includes achieving increased efficiency and productivity, understanding the impact of investment decisions, evaluating pricing decisions, and the determination of the profitability of products, services, and customers. Although costing has historically heightened awareness of the organization's cost of operations (what, when, and where) in order to better manage them, its greater value lies in its forward-looking perspective (how and why) for planning and informing decision-making at strategic and operational levels.

Professional accountants in business can make a difference in their various roles

Professional accountants in business draw on a broad base of capabilities in undertaking a variety of roles, as both suppliers and users of costing information. In the front-line business management role, they can be decision-makers; in the decision-support role, they assist the consumers of costing and operational information. Regardless of their perspective, professional accountants have important roles to play in (a) ensuring that cost data is ‘fit for purpose’, (b) clarifying decision requirements, and (c) deciding how best to present information and analysis (including method of delivery, e.g., hardcopy, web-based portal, etc). This includes considering the relevance of revenue and cost information to the range of factors and issues pertinent to a particular decision.

They can also help their organizations to invest in developing an appropriate decision support model that is not impaired with the deficiencies of a system focused on identifying full costs for financial reporting standards. Most significant decisions facing management are marginal or incremental, and require robust information on the way costs behave throughout the organization.

The publication clarifies the range of useful cost concepts that form the basis of managerial insight, such as throughput costs, incremental costs, short-term variable/proportional costs, attributable costs that support divestment decisions such as outsourcing, and full costs to support strategic decisions, such as entering a new market.

A companion Costing Levels Maturity Model

As a companion to *Evaluating and Improving Costing in Organizations*, IFAC has published separately a new *Costing Levels Maturity Model*. It is aimed at helping professional accountants to assess their organizations’ existing capability for supporting internal managerial analysis and decisions, along with the opportunities to improve it. The model, which is in a beta

version, can also help organizations determine the level of costing sophistication necessary, given their organizational requirements and the decision needs of managers and employees.

How to access the International Good Practice Guidance

The International Good Practice Guidance can be accessed from the Professional Accountants in Business (PAIB) section of the IFAC bookstore (www.ifac.org/store/). IFAC seeks comments from professional accountants and IFAC member bodies on *Evaluating the Costing Journey: A Costing Levels Maturity Model* to help its continued development. IFAC also welcomes feedback on this International Good Practice Guidance and all its other guidance available at www.ifac.org/paib . Comments can be sent to Stathis Gould, Senior Technical Manager, PAIB Committee (stathisgould@ifac.org).

About IFAC and the PAIB Committee

IFAC (www.ifac.org) is the global organization for the accountancy profession dedicated to serving the public interest by strengthening the profession and contributing to the development of strong international economies. IFAC is comprised of 157 members and associates in 123 countries and jurisdictions, representing more than 2.5 million accountants in public practice, education, government service, industry, and commerce.

IFAC's PAIB Committee develops good practice guidance, provides resources and facilitates the exchange of knowledge and best practices among the more than one million professional accountants worldwide employed in commerce, industry, the public sector, education, and the not-for-profit sector.