Anatomy of a Plan

BETTER PRACTICES FOR MANAGEMENT ACCOUNTANTS

BY JEFFREY C. THOMSON

Planning, budgeting, and forecasting. On various occasions, I have called these topics the "heart and soul" of management accounting and, on others, its "lifeblood." Therefore, I thought it appropriate to use the term "anatomy" to describe the key internal elements of the multiyear strategic planning process (which *includes* budgeting, long-run forecasting, and other types of decision analytics), current practitioner issues, lessons learned, and keys to success. The most important thing I'll discuss in this article is the roles that management accountants do or can play as critical influencers in the strategic planning process. I'll also cover some better practices for planning and budgeting. (Since few companies have reached a state of perfection in the planning and budgeting process, I prefer the term "better" rather than "best" practices.)

WHY IS PLANNING THE HEART, SOUL, AND LIFEBLOOD OF MANAGEMENT ACCOUNTING?

Planning is the ultimate forward-looking, influential activity that impacts key stakeholders over a long period of time. Management accountants and finance function professionals have been on a decade-plus quest to shift their roles from shareholder value *stewards* to shareholder value *creators*, from bad cop to respected and credible influencers at the decision table, from transaction processors to strategic business partners. This isn't a complete shift away from their "home base" of finance and accounting because management accountants must demonstrate technical accounting depth in order to have the "right" to influence a breadth of business operations. What better opportunity to influence operations, value creation, and business performance than involvement in an organization's multiyear strategic plan, budgets, and forecasts—those forward-looking activities that chart the path ahead for an enterprise's critical stakeholders, such as customers/members, investors, and employees, to name a few!

To do this, what knowledge and skills must management accountants and finance professionals have? They regularly list planning, budgeting, and forecasting as areas in which they are seeking to build additional competency, and Table 1 seems to agree. It lists strategic planning as number 1 and budget preparation as number 5 under "most important knowledge and skills," according to a job analysis conducted by the Institute of Certified Management Accountants (ICMA) in March 2006. The job analysis was conducted to test/validate whether the Certified Management Accountant (CMA®) exam content is consistent with the tasks and functions performed by management accountants in practice today and to suggest future content changes to ensure ongoing exam relevance as environmental conditions change.

Table 1: Knowledge and Skills Management Accountants Need to Possess

Strategic Planning	**87%**
Organization Management	83%
Decision Analysis	78%
Statement Analysis	75%
Budget Preparation	**75%**
Information Management	74%
Performance Measurement	71%
Cost Management	71%
Internal Controls	70%
Business Process	66%
Investment Decisions	64%
Business Economics	63%
External Reporting	63%
Strategic Marketing	58%
Global Business	57%
Quantitative Methods	56%
Corporate Finance	53%
Operational Paradigms	51%

Source: ICMA Job Analysis (March 2006–1,899 respondents)

Once management accountants gain these and other skills, a highly desirable set of jobs awaits them! An "FP&A" (financial planning and analysis) job is often a "required" stop on the career path for the aspiring management accountant, regardless of an organization's size or structure. The position could be inside the central group that manages the planning process (the central FP&A organization), which could be the chief strategy organization (CSO), the controller's department, or even you (in a small enterprise), among other organizational options. Roles could include developing a master planning calendar; developing guidelines, standards, and templates for business units to apply in their planning; developing forecasts based on external expectations; and "rolling up" business unit forecasts to determine gaps relative to market expectations for key performance metrics such as revenue growth.

Influential positions abound outside the central planning organization as well, namely in the business units, product groups, and/or departments that are the operational "piece parts" or components that make up the total organization. These roles are closer to the market action and could involve preparing departmental budgets, forecasting products or customer segment financials, and "negotiating" with the centralized planning group to create an optimal financial and operational planning view that achieves organizational objectives.

BUT WHY IS PLANNING STILL A MAJOR PAIN POINT FOR MOST ORGANIZATIONS?

Figure 1 portrays the current level of dissatisfaction with the planning, budgeting, and forecasting processes among leading CFOs. In 2006, KPMG and the Economist Intelligence Unit surveyed more than 200 CFOs about various dimensions of finance leadership, such as people, processes, and technology. Figure 1 indicates that planning heads the list of areas with which the CFO is most dissatisfied. Not surprisingly, other results from the survey reveal that

Figure 1: Where Is Finance Most Dissatisfied with Its Current Capabilities?

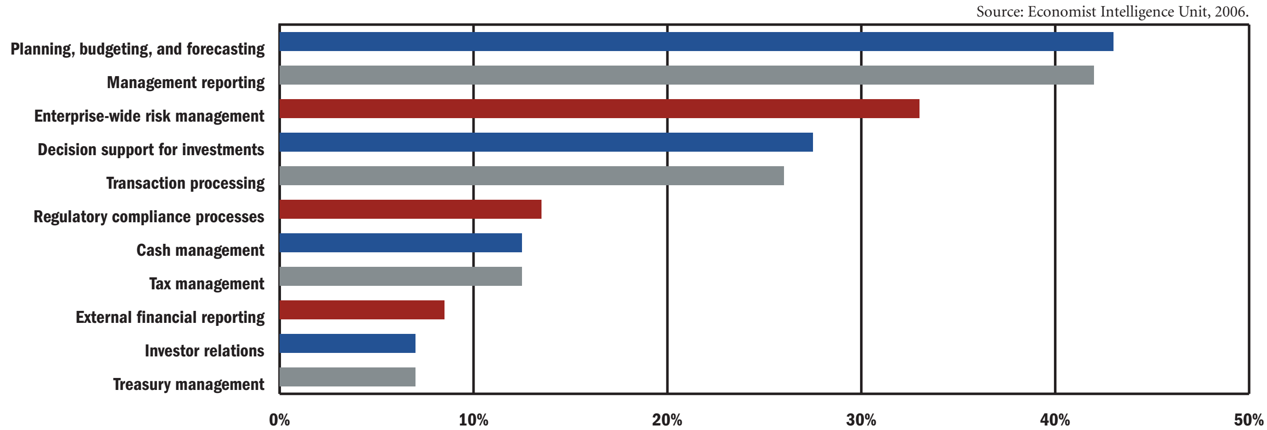
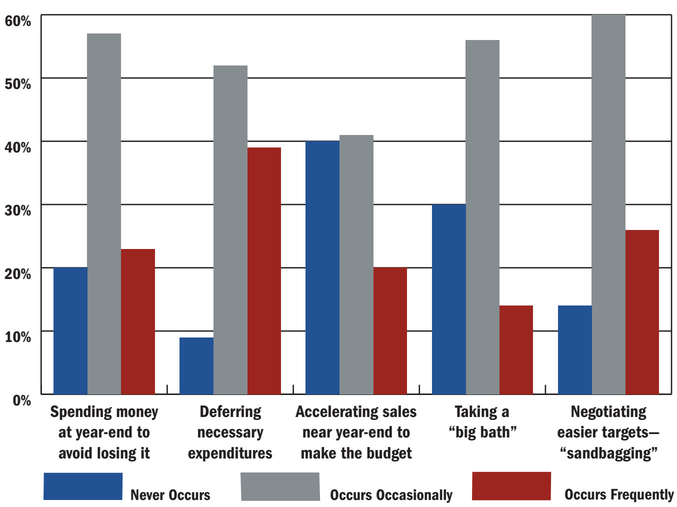


Figure 2: Budget Gaming



the planning process is the CFO's highest priority for performance improvement, ahead of management reporting, transaction processing, enterprise risk management, and regulatory compliance.

In addition, many leading benchmarking organizations, such as The Hackett Group and APQC, have conducted research in the area of planning process cycle time and best practices. And an August 2007 *Strategic Finance* article by Theresa Libby and R. Murray Lindsay, "Beyond Budgeting or Better Budgeting?" based on a survey of more than 200 IMA members, also revealed a certain level of dissatisfaction with the annual budgeting process. Here are some additional "fun" (or maybe frightening) facts that reveal current practitioner pain points with the planning and budgeting processes:

1. Cycle times are too long and don't add value.

A. The average cycle time for completing the annual budget process is nearly four months (Hackett, APQC). While there isn't necessarily an official "best practice" benchmark, ideally this average cycle time would be closer to one month, depending on an organization's scale and scope.

B. It takes about 25,000 person days per $1 billion of revenue to complete the annual budgeting and planning cycle (Hackett).

C. A majority of IMA member respondents say the traditional budgeting process is too time-consuming, is slow to detect problems, and isn't reliable for measuring performance (Libby and Lindsay).

2. The traditional budgeting process doesn't incent "stretch behavior" in individuals or organizations but does incent gaming.

A. Bernie Ebbers, former WorldCom CEO now serving jail time, mandated expense performance at least 2% below budgeted amounts.

B. Jack Welch, the legendary CEO from GE, declared: "The budget is the bane of corporate America. It never should have existed. A budget is this: If you make it, you generally get a pat on the back and a few bucks. If you miss it, you get a stick in the eye—or worse."

C. Libby and Lindsay's research explicitly addressed the issue of budget gaming. A majority of IMA respondents indicated that three "gaming" phenomena occur at least occasionally: spending money at year end to avoid losing it (the age-old "use it or lose it" syndrome), deferring necessary expenditures, and negotiating easier targets (the "sandbagging" syndrome). See Figure 2 for further details.

3. Practitioners are generally using "low grade" technology or aren't pleased with their existing technology solutions to planning, budgeting, and forecasting.

A. More than 50% of respondents use Excel as their budgeting software, including *Fortune* 500 companies (Forrester Research Advisory Services, 2005). Although Excel is very functional and user-friendly when budgeting for a particular product or department, quality control issues arise when trying to achieve integration across multiple work units and rolling up totals to the organizational level.

B. More than 60% of users weren't satisfied that their BES (Business Enterprise Systems) software lived up to expectations (*Cost Management*, May/June 2006).Unless we understand the factors that drove this expectations gap, more recent BPM (Business Performance Management) software suites aren't likely to achieve the desired gains in integration and productivity.

KEY PLANNING ACTIVITIES AND THE ROLE OF THE MANAGEMENT ACCOUNTANT

Before discussing better practices for the multiyear strategic planning process, I'll define the key steps and activities that generally make up the strategic planning process, including the annual budget and forecasting processes. See Table 2 for current or potential roles for the management accountant and a list of the corresponding key planning activities.

The **Vision** and **Mission** are the cornerstones, the "rocks" of any organization that has been successful over a long period of time. The Vision is an emotion-inducing statement that tells where an organization is or aspires to be and that provides long-term direction. It should be inspirational, passionate, and evoke the organization's brand in one short, sweet statement. A Vision statement can evolve just as an organization evolves. For example, in its early days, Microsoft's Vision was "A PC on every desk and in every home." Today, its Vision is "Your Potential, Our Passion." The Mission is meant to describe, at a high level, the value the organization delivers to its various stakeholders and how to achieve the organization's strategic goals.

What role does the management accountant play regarding an organization's Vision and Mission? The management accountant may have an opportunity to be part of a team to create, validate, or change the Vision and Mission. There's no magic as to how often the Vision and Mission should be validated by all stakeholders. If an organization is humming along, the Vision and Mission will stand the test of time unless market changes or evolving technology suggest a change. If the organization is *puttering* along and not satisfying its stakeholders, the strategy—starting with the Vision and Mission—probably needs to be revamped.

The **Environmental Scan** ensures that you are vigilant about looking "outside your own walls" and not becoming too isolated in setting strategic goals. Michael Porter from Harvard University developed a "Five Forces" framework that models an industry as being influenced by Supplier Power, Buyer Power, Barriers to Entry, Threat of Substitutes, and Degree of Rivalry. Strategic business partners seeking to gain a competitive edge for their organization can use this framework to better understand the industry context. If your organization is planning to introduce a new product, service, or technology, understanding these influencers before proceeding with internal prioritization, resource allocation, and business cases is critical to building market acceptance and financial viability.

As part of the Environmental Scan, management accountants could assess all environmental factors that impact business success within their company, business unit, product line, or department (e.g., a detailed competitive analysis of your new product line vs. a competitor's). Or their role could be more quantitative in nature, such as forecasting their competitors' or industry peer groups' key performance metrics over the multiyear strategic plan (e.g., revenues, expense-to-revenue ratios) to ensure that stretch organizational targets are set relative to their key competitors vs. internal run rates and "what we did last year + x% better." Or they could compare the demographics of their customer or member base against the broader industry to determine gaps and product marketing implications for key market segments (e.g., U.S. vs. international, gender, organization size, etc.). Management accountants should perform the Environmental Scan every three to six months to ensure that external dynamics are reflected in their latest forecasts.

Product/Market Priorities actually involve several steps. First, baseline your current products and services relative to your key targeted market segments. Are you delivering products, services, and solutions that satisfy the

Table 2: Key Planning Activities and Management Accountants

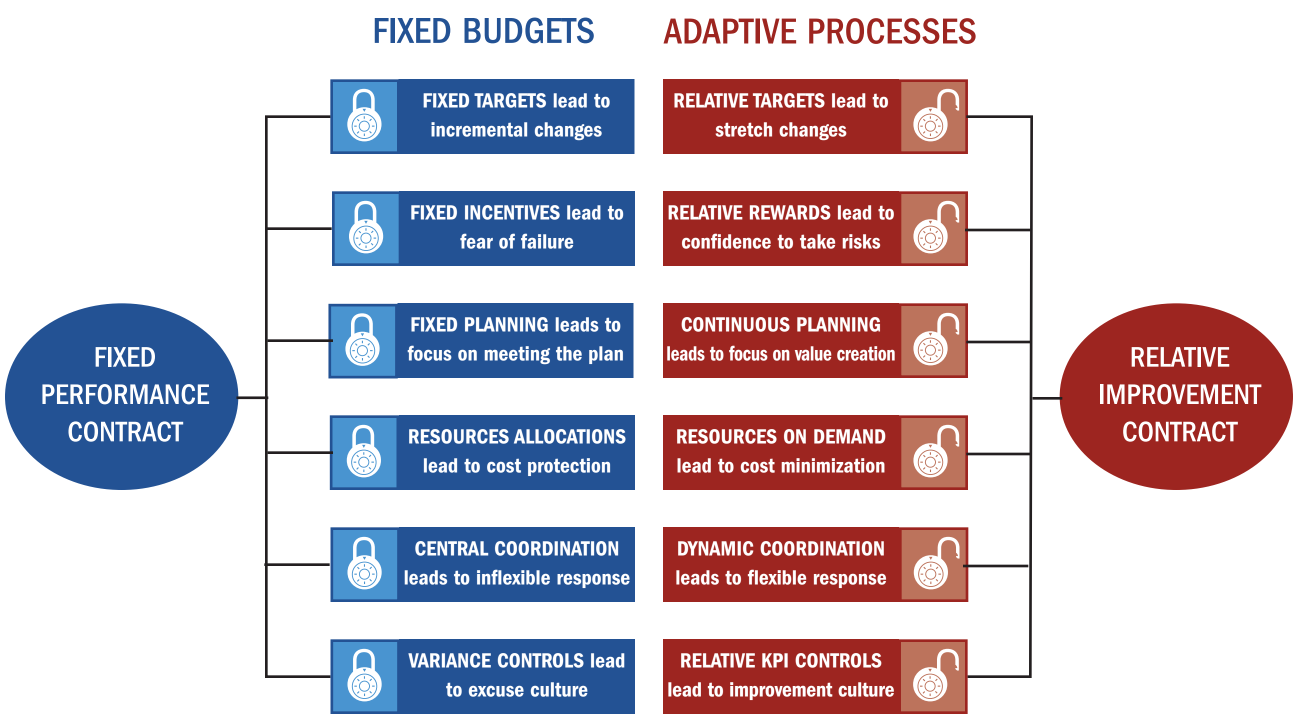
KEY PLANNING ACTIVITY	ROLE OF THE MANAGEMENT ACCOUNTANT	SUGGESTED FREQUENCY
Setting/Validating the Vision	Contributing to feedback sessions to set or validate the Vision.	Every three years
Setting/Validating the Mission	Contributing to feedback sessions to set or validate the Mission.	Every three years
Environmental Scan/ Business Landscape	Research and synthesize intelligence on key environmental factors, including regulatory environment and competitors.	Every three to six months
Product and Market Priorities	Identify key market segments, inventory current product and service set, and determine the priority products and markets for resource allocation, market launches, etc.	Every six to12 months
Strategic Change Portfolio	Work with cross-functional teams to create and update "strategic initiatives" that overlay the multiyear baseline view to achieve strategic goals.	Every six to12 months
Determine Measures of Success ◆ Strategic goal setting ◆ Forecasting at micro and macro levels (Baseline + Initiatives) ◆ Budget detail ◆ Financial and nonfinancial measures	Key role for the management accountant in terms of determining goals, key financial and nonfinancial measures (e.g., use of balanced scorecard and strategy maps), long-run forecasting of key measures, budget expense detail for first year of plan, etc.	12 months (budget/plan cycle) supplemented by periodic in-year outlook updates (e.g., quarterly)
Develop, Deploy, and Sustain a Continuous Improvement Process ("the plan for the plan")	Work closely with cross-functional teams to support or lead continuous process improvement efforts for one of the organization's most critical business processes: strategic planning, budgeting, and forecasting.	Ongoing

needs and wants of these segments? Is there a gap that could result in a reassessment of your **Strategic Change Portfolio**—the portfolio of strategic initiatives that will require incremental funding over and above the baseline, multiyear financial view? The final step involves rating and ranking the products and services relative to your key market segments to help in allocating resources. As an influential member of cross-functional teams in larger organizations, the management accountant can play a key role in the project prioritization and resource allocation processes. Market research—the voice of the customer—is also critical for effective prioritization.

The Strategic Change Portfolio will drive sustainable growth value for stakeholders. This portfolio generally falls into two categories: (1) "Market Facing," such as new products and services, and (2) "Infrastructure," such as human resources, IS/IT systems, etc. The management accountant can play many important roles here. One is working with his/her team to conceive, develop (via a business case), and deploy (via a project plan) strategic initiatives. Another is providing financial support for the change initiative, including estimating business case revenue and expenses that are incremental or add to the baseline financial trajectory had the action (the change initiative) not taken place. While being strategic and forward looking, first and foremost the management accountant is the financial steward of the Strategic Change Portfolio, the market basket of change initiatives, over and above an organization's baseline or "momentum" trajectory, that will allow the enterprise to achieve its long- and short-run strategic goals. Finally, rigorous project planning that includes milestone tracking and release of funds relative to the achievement of milestones ("the banker") is another key role for the management accountant. The Strategic Change Portfolio should be assessed annually when the plan cycle begins and then ideally every six months.

Determining Measures of Success is where the quantitatively minded management accountant (aren't we all?) can make a real difference in the strategic planning process. This includes setting the broad multiyear strategic goals for the organization. These goals should contain a balanced set of measures, including financial viability, as measured by revenue, expenses, and margin; customer growth, as measured by new customers and customer retention statistics; customer satisfaction, as measured by surveys and market share; and employee development, as measured by staff retention and career development. A traditional role for the management accountant in the annual planning process involves developing a budget

Figure 3: Principles of the New Performance Contract



that covers the first year of the multiyear strategic plan—but at a lower level of detail (e.g., expense line items by department).

Management accountants also need to help forecast at macro and micro levels via financial modeling. Financial modeling is a critical element of determining key measures of success over the multiyear planning horizon. A *macro* financial model is often the first step. Here the modeler collects all available internal data (e.g., department spend history) and external benchmarks (e.g., competitor growth rates) and creates a macro financial projection over the planning period. This view may be limited to the key financial and performance indicators consistent with the strategic goals, such as revenue, operating expense, margin, and customers. It also is used to test the reasonableness of individual product or departmental views relative to expectations of the market and organizational stakeholders (the infamous "rollup"). A *micro* financial view also may be developed in conjunction with the macro view. This micro financial view would decompose revenue into a price and a quantity/volume component (P x Q = R), for example. The advantage of having a complementary micro model is that, once the piece parts are calibrated to the reported or planned total at the macro level, the model can be used for "what if" and scenario planning purposes during the periodic outlook update process (e.g., quarterly). For example, what's the financial impact if we raise prices? What's the financial impact if we improve our customer retention rates based on a new strategic initiative?

Finally, **Developing, Deploying, and Sustaining a Continuous Improvement Process**, or planning for the plan, is truly the "lifeblood" of a strategic plan because it ensures focus on execution, continuity, and intervention if necessary. Developing the multiyear strategic plan and putting it on the bookshelf to collect dust while focusing on the in-year budget only (the one that affects our pay in the short-term mentality that guides American business) could spell doomsday for the long-run viability of your plan. There are improvement opportunities galore in the central planning group or in the individual work units: Setting the master planning calendar of accountabilities and deliverables, developing external competitive benchmarks, developing and communicating robust business cases, and forecasting key performance indicators are just a few examples. The continuous improvement process is indeed continuous, much like the blood flow in the human body that sustains us all.

BETTER PRACTICES

Now let's concentrate on some "better" practices.

1. Treat Planning as a Key Business Process. Nothing is more important to an organization's long-run viability, sustainability, and value creation for stakeholders than its strategic plan. But a plan without an enabling process is like human blood flow without the arteries and ventricles—the connective tissue, if you will. First, establish the end-to-end process including accountabilities, time frames, and measures of success. Engage everyone at some level in the plan, not just the central planners or the designated planner or planning coordinator in your group. Good governance principles apply to strategic planning just as they do to any other key business process, and establishing the master planning calendar with deliverables and milestones is vital to downstream success of the process—and ultimately the plan. A critical core competency for the management accountant involved in a leadership role in an organization's planning process is project management skills, which are vital if planning is to be implemented effectively as an end-to-end process or system with key milestones, deliverables, and resources to be managed.

2. Execution with Enablers Means Excellence ("E cubed"). While excellence as defined by achieving strategic goals is never guaranteed, a passion for execution and a set of enabling tools and processes are critical success factors. Several enablers come to mind: (a) a regular process, perhaps as part of operations reviews or results meetings, to review the status of strategic initiatives and goals and to discuss "interventions" as necessary (e.g., reallocate resources, consider new pricing plans, etc.); (b) a milestone-tracking process (integrated with most project management software packages) to manage the progress of strategic initiatives, to release business case funds when key milestones are achieved, and to send out "alerts" if milestones are missed or are in danger of being missed (alerts are usually standard fare in business intelligence or business process management software); and (c) integration of a true risk-based approach into the strategic planning process.

A risk-based approach ensures that the key risks to achieving strategic goals/plan objectives are identified and that interventions are implemented to manage the risk to a level acceptable to all stakeholders. For example, when the Institute of Management Accountants (IMA®) initiated its annual planning cycle, staff responsible for planning participated in a one-day workshop on risk management. My main point is that risk management is a global body of knowledge that contains resources to guide practitioners. (For example, IMA offers two Statements on Management Accounting (SMAs) on Enterprise Risk Management for free on its website at www.imanet.org/publications_statements.asp#E.) Risks should be identified holistically and addressed across the enterprise—not just traditional financial risks, but risks such as security, environmental, operational systems, etc.

3. Beyond Budgeting…or just Better Budgeting? Recall the pain points associated with traditional budgeting that I discussed earlier—cycle times that are too long, the process incents gaming vs. stretching for the best possible performance, too much emphasis is placed on internal performance (run rates) vs. external competitive benchmarks, and the (heart-) beat goes on! To stretch your thinking, read the book *Beyond Budgeting* by Jeremy Hope and Robin Fraser, or watch the archived free IMA three-part webinar series focused on planning and budgeting (July-September 2007), which you can find at www.imanet.org/development_webinar_library.asp. The BBRT (Beyond Budgeting Round Table at www.bbrt.org) basically suggests that the budget as we know it should be eliminated because it constitutes a fixed performance contract that doesn't "flex" relative to market conditions, the need for dynamic resources, competitors, etc. See Figure 3 for more detail or the BBRT website as to what BBRT advocates as a replacement for the "fixed performance contract."

The question is: Do we need to replace budgets as we know them (*beyond* budgeting) or radically transform the way we have been taught to create them? In any event, there are several better practices for management accountants involved in budgeting:

- Create the budget only after the broader strategic direction and goals have been set. This generates a context and high-level "screen" for what can or can't be included in the more detailed budget.
- Develop rolling outlooks at a reasonable level of

detail combined with an aligned incentive scheme. This can "force" thinking beyond the in-year budget whose time horizon naturally shrinks as the fiscal year approaches its year end (a six-quarter rolling outlook, for example, continually forecasts another six quarters ahead for key performance measures such as revenue, margin, etc.).

◆ Rely at least as much on *external* benchmarks (metrics like expense to revenue, productivity ratios, etc.) from benchmarking organizations such as The Hackett Group and APQC and vertical industry associations as you do on internal run rates and "what I did last year" plus or minus x%.

4. Predictive and Decision Analytics…There Is Life Beyond Basic Excel. No, you don't need to become a Ph.D. statistician, but knowledge of basic statistical tools and techniques for data analysis and forecasting should be part of the management accountant's toolkit. In Excel, as an add-in option, go to Tools, then Add-Ins, and add in the "Analysis ToolPak." This gives you access to intermediate statistical functions such as correlation analysis (e.g., the "strength" of the relationship between two variables such as customer growth and advertising over a historical time frame) and regression analysis (life is more sophisticated than the straight-line ruler to forecast historical data such as expenses or revenues—*multiple* regression allows you to forecast an "independent" variable such as revenues based on historical relationships with a set of "dependent" or driver variables such as advertising, customers, pricing, volumes, etc.).

Here are three brief examples in which management accountants use predictive technologies and decision analytics (the preferred Google terms) to drive business performance: (a) In an ERM presentation at IMA's 2nd Annual Global Conference in May 2007 in Dubai, Ananth Rao (professor at the University of Dubai) used intermediate Excel capabilities to have workshop participants create risk-adjusted decision scenarios; (b) in his keynote presentation at IMA's 88th Annual Conference & Exposition in June 2007 in Phoenix, Ron Riebe (vice president of KeyBank and most recent winner of the IMA/Robert Half Financial Executive of the Year Award) focused on several practical decision analytic capabilities for management accountants who take on positions in pricing, economic analysis, and business forecasting; (c) the article "Sustainable Performance Improvement through Predictive Technologies" in the June 2007 issue of *Strategic Finance* magazine discusses the emerging body of knowledge called "predictive technologies." (Contact me for ways to view or read the first two presentations.)

Finally, I suggest you read the 2007 book *Competing on Analytics* by Thomas H. Davenport and Jeanne G. Harris. In short, the book's premise (based on 30 case studies) is that analytics—forecasting, data mining, statistical analysis of trends, etc.—is truly becoming the "nextgen" competitive differentiator, requiring that organizations create and imbed an entirely new skill set in their day-to-day activities and planning—yet another opportunity for the management accountant as strategic business partner and influencer in the organization!

5. Communications: Continuous and Comprehensive for all Stakeholders ("C cubed"). Communicating the strategic plan and progress on strategic goal achievement is critical to ensure that all stakeholders are appropriately engaged in executing the plan successfully. *Continuous* communication ensures that the strategic plan doesn't collect dust on the bookshelf. *Comprehensive* communication to all stakeholders—shareholders, investors, customers/members, audit committee, the board of directors, and, of course, ALL employees who have a stake in the success of THEIR strategic plan—is critical.

Two suggestions: Make the communications a bit fun and creative—hold employee meetings and celebrations to kick off the new planning cycle—and be honest and totally transparent with your employees. Don't supply only "smiley-face" happy news. Show the progress on key goals, highlight successes, but also highlight challenges that require all employees to be engaged. Your employees expect nothing less!

PUMPING NEW BLOOD

As I hope you've been able to see, there are exciting possibilities for management accountants in the areas of strategic planning, budgeting, and forecasting that should pump new blood and life into these processes. These are areas that are forward looking, rely on sound analytics and business judgment, require good communications and business influence skills, and relate directly to creating and sustaining stakeholder value. This is a great opportunity for you as management accountants to advance the profession and drive business performance in your organizations! ■

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