exceeding his standard, because he does not want to wait until the chief executive receives his statement and sends for him. This is another advantage of working against standards made in this way.

The opportunity for attributing differences between two periods to the differences in the periods is done away with. The chief executive is assured that his costs will be maintained substantially at the standard or he will be informed of the fact while he is still on his way "to Tarrytown," as it were, and he still has an opportunity to speed up and make up the lost time. Without this business speedometer he would have to wait until his hour was up, and then it would be too late.

If I have made clear the use of the standard and the monthly report by the department heads, we can now go on to the statement which the chief executive himself receives. This statement, as already explained, is merely a tabulation including the last line of each of the monthly statements of the separate organization units.

Exhibit K—Conventional Operating Report

Before showing the final statement under these methods, I am going to show you, for purposes of comparison, the conventional Operating Statement. There are many modifications of this statement but I think this one is typical of the large majority of the best.

With this statement, how is the chief executive to know whether or not the results are satisfactory in proportion to the conditions under which the business was done, or how to appraise the accomplishments of the separate organization units?

Assuming that he does not consider the results satisfactory, and he secures from the bookkeeper an additional statement giving further details, how is he to appraise the expenditures for one item as against those of another? About the most that he can do is what is usually done, namely, to compare the results of the month in question with the preceding month and with the same period for the preceding year, and even then he only knows how one compares with the other. He does not know how either compared with a reasonable expectation. If the conditions between the two periods compared are different, if prices have gone up or down, if the firm has done more or less business, or if materials cost more or less, how is he to reconcile these differences?

His expenditures are arbitrarily divided among a variety of responsibilities, and even if he determine that his production, sales, delivery or some other item

TYPICAL OPERATING REPORT
(Expressed in Thousands)

OPERATING STATEMENT	Current Month		To Date	
August 31st, 1921	1921	1920	1921	1920
GROSS SALES	2,500	3,000	16,000	18,000
Discounts and Allowances	230	250	1,600	1,800
NET SALES	2,270	2,750	14,400	16,200
Cost of Goods Sold	1,600	1,850	10,000	10,700
GROSS PROFIT	670	900	4,400	5,500
Administration and Selling	520	550	3,500	3,700
OPERATING PROFIT	150	350	9,000	1,800
Depreciation and Fixed Charges	40	40	285	285
NET PROFIT	110	310	615	1,615

NOTE: This example is intended to indicate the character and form of the usual operating statement rather than the degree of detail in which it may be made. K

Exhibit K

of cost is high, how is he to fix the responsibility for the high cost without endless analysis which is impracticable as a current procedure?

There is an interesting fact in connection with industry, and especially the job of the chief executive, which is not generally recognized or understood; it is that *most of the undesirable results come from lack of knowledge as to where the trouble lies rather than in the difficulty of removing it, once the source is definitely located.*

Exhibit L—Recommended Operating Report

You will notice that the last column on this exhibit is exactly the same as the last column on Exhibit H; in other words, it is the *standard* per cent Variable Cost to sales for each of the different organization units or groups of responsibilities.

The column immediately preceding it is the *actual* per cent of Variable Cost of sales.

The difference between the footings of these two columns shows at a glance the total difference between actual cost and what it should have been. In this case the actual Variable Cost has been \$.0114 of each dollar of sales in excess of the standard. Multiplying this by the volume of business done—\$16,000,000—we see that the variation from standard in terms of dollars and

cents is \$181,000 to the bad. (Difference between footing of third and fourth columns from right).

Please especially note that this statement is literally made up of the last lines of the statements of the individual organization units, brought together. There is no reason for an uncertainty on the part of the chief executive as to where to turn his attention for the cure of the condition that he finds. All he has to do is to let his eye run up the column "Bad" for variation and he will see exactly which responsibilities have fallen below the standard. Having determined this, he knows exactly for whom to send, and when he comes before him all he has to do is to refer back to the budget for that responsibility—that is, the sheet corresponding to Exhibit G—to see in just exactly what item the excess expense was incurred.

If actual expenditures are subdivided under the three headings suggested in Exhibit G—payroll, physical things and outside service—so that they are comparable with the standard, it will not be difficult to find out whether the increased expense is justifiable or not.

It may be justifiable for the current period but may not be justifiable in the future, in which case the standard would not be changed. The chief executive would simply say to the manager that the additional expense was justifiable in this case but should not recur in the future.

If it was not justifiable, he would point out to the manager wherein he had been remiss.

If, on the other hand, it was not only justifiable but would probably recur in the future—if, in other words, there was a mistake in the standard—he would make the necessary change in the standard.

The question has been raised whether a statement made up in this way will check with the financial books. Let us see just what we have done. First, we have divided our expenditures according to the organization unit authorizing them. Secondly, we have left every penny of expenditure where it was first charged. There has been absolutely no diverting of expense from one account to another. Therefore, instead of complicating things, *we have simplified them.* All that we have to do is to add up the gross revenue, add up the expenses, deduct one from the other, and the difference is necessarily our profit or loss. (See foot of first column).

What I have shown you may at first impress you as involving a great deal of detail work. This impression can be only if you are not familiar with the vast detail work involved in making up statements as they are usually made. It is safe to say that there is less paper work involved in the procedure which I have outlined than in any other procedure which makes even a pretense of giving accurate monthly figures.

It is impossible in one evening's talk to answer all the different questions that will occur according to the character of the industry in which you happen to be experienced. For simplicity, I am sticking close to the one particular enterprise previously described. I think, however, I should explain what we must do if the amount of goods produced and those sold do not happen to be the same.

If production has been say \$100,000 list price in excess of sales, we should add the excess production at inventory cost to the profit as shown:

Profit as shown on Operating Statement..........	\$616,000
Value of goods produced in excess of those sold \$100,000 × .55..............................	55,000
	\$671,000

If sales had been say \$100,000 list price in excess of production, we should deduct from the profit as shown the value of the goods sold in excess of those produced, at inventory cost:

Profit at shown on Operating Statement..........	\$616,000
Value of goods sold in excess of those produced \$100,000 × .55..............................	55,000
	\$561,000

Having shown the Operating Report compiled with a view to showing the operating effectiveness of the organization and the placing of responsibility for good and bad results, I shall now recapitulate these same figures, compiling them with a view to furnishing information with reference to matters of policy; whether a change in price might be advantageous to the company, and the relative merits of groups of commodities, territories, methods of selling, advertising appropriations and the like.

Exhibit M—Commodity Report

This exhibit gives you the following information under two separate commodity classifications. There may be one or a dozen commodity classifications as circumstances may make desirable.

Inventory Cost	Net cost of commodities available for distribution.
Basic Sales Cost........	Inventory cost plus the cost of general sales organization.
Branch Sales Cost......	Total cost of commodities sold through company's own branches.
Jobbers Sales Cost......	Total cost of commodities sold through jobbers.
Export Sales Cost.......	Total cost of commodities sold for export.