of the size of the shipment. All such costs are termed "invoice costs." The cost for billing, filing, sales statistics, accounts-receivable records, etc., fall in this class of expense.

Other expenses increase in proportion to the number of items or lines on the invoice. These are called "item costs." A part of the expense of the cost department, stock records and shipping room are examples of this type of costs.

All sales, administrative, office and shipping expenses not included in either of the above classes are grouped under "financial costs" and allocated on the basis of dollar volume.

All direct selling expenses including salesmen's salaries, commissions, bonuses and traveling expenses are placed in a separate group called "call costs."

All distribution costs are thereby divided into five groups as follows: (1) Order costs; (2) invoice costs; (3) item costs; (4) financial costs, and (5) call costs. The total order costs are then divided by the total number of orders, the total invoice costs by the total number of invoices, the total item costs by the total number of items, the total financial costs by the total dollar volume of sales and the total call costs by the total number of calls. This gives the cost per order, per invoice, per item, per dollar volume and per call.

With this information available, it is a simple matter to determine the minimum size of order which can be handled at a profit. For example, one manufacturer found that his costs were as follows:

Overhead and routine cost of handling the customer's order	$0.55
Overhead and routine cost of handling the shipping order and invoice	2.60
Cost of handling each item or line on the invoice	.15
Financial cost per dollar of volume	.08
Total cost for a dollar order (assuming the order came in by mail and required no solicitation by salesman)	$3.38

With an average gross margin of 28 per cent, the loss on a one dollar order was $3.10. If a call had been made by a salesman to obtain the order, at $4.25 per call which was the average cost for this concern, the total cost would have been $7.63 or a loss of $7.35.

Now let us assume that a mail order was received for $20. The order, invoice and item cost would remain the same as before, but the financial cost would be $1.60 (or $.08 times twenty), making the total cost $4.90 or 24.5 per cent of the sale, thus leaving a profit of 3.5 per cent. It is therefore evident that the minimum order which this manufacturer could handle at a profit is somewhat less than $20 or approximately $17. When a salesman makes a call to take an order, the minimum profitable order is increased to about $35.

By the use of this score card it is a simple matter to determine the cost of filling an order of any size, for any number of items, shipped in any number of shipments. It also shows why large orders are more profitable than small ones and how much more profitable they are. For example; to apply the score card to a $500 order to be filled in two shipments and made up of ten items, the method would be as follows:

Overhead and routine for handling order	$ 0.55
Overhead and routine for handling two invoices at $2.60 per invoice	5.20
Handling cost, ten items at $0.15	1.50
Financial cost ($0.08 per $1.00) for $500	40.00
Cost of the salesman's call	4.25
Total cost	$51.50

The total cost is 10.3 per cent of the sale. The gross margin is 28 per cent, which leaves a profit of 17.7 per cent or $88.50 on the $500 order. This same manufacturer just broke even on a $35 order.

It should be clear from these figures that the average size of order received from a customer is a very important factor in determining whether or not the customer is profitable. To illustrate: We will take two customers with annual purchases of $1,000 each. One sends in one hundred orders averaging $10, the other ten orders averaging $100 each. Assume a salesman calls on each customer ten times during the year. Based on the score card given above, the total cost for the first customer is $452 while the total cost of taking care of the second customer is $161, or a difference of $291.

Small average orders usually come from small customers. In every analysis I have made the average size of order received from the group of large customers, who supply around 90 per cent of the total sales volume, are from seven to ten times greater than the average order received from the multitude of small customers, who supply the remaining 10 per cent of volume. However some large customers are buying on such a close, hand-to-mouth, basis that in spite of the large volume their business is very unprofitable. It is therefore necessary to analyze every account.

Who Is Responsible?

Who is responsible for all of these small orders and unprofitable customers, and what can be done about them? Are these conditions which have been forced upon us; over which we have no power of control? Or are they of our own making and is the control in our own hands? Personally, I believe the latter is a true statement of the case.

I believe that sales executives and salesmen are very largely to blame. The great aim of many sales executives has been to obtain what they termed a "one-hundred per cent distribution" of their product. Salesmen were required to call on every potential customer regardless of how small his potential volume might be. In some cases the objective has been practically reached, but instead of finding a pot of gold at the end of their rainbow, they found only increasing costs and decreasing profits.

In general salesmen have spent far more time with small customers than their business warranted. For example, the salesmen of one manufacturer spent 41 per cent of their time with customers from whom they obtained only 4.3 per cent of their sales volume. In another concern, 40 per cent of the salesmen's time was given to customers supplying only 6.4 per cent of the sales.

If the salesman is awake to his possibilities, he can do much toward increasing the size of his average order, building up more profitable accounts, and avoiding a waste of time on small customers. Let us take a concrete example. A manufacturer had two salesmen covering the New England territory. Salesman "A" was given the north shore and the states of Maine, New Hampshire and Vermont. Salesman "B" was given the south shore and the states of Rhode Island and Connecticut. Accounts in metropolitan Boston and western Massachusetts were divided equally between the two salesmen. As near as could be determined, sales possibilities were about equal in the two territories. Both salesmen had been working their respective territories for several years. At the time the analysis was made, salesman "A" was soliciting 170 accounts but spending 75 per cent of his time with his sixty-five best customers. Salesman "B" was soliciting 245 accounts and spending only 50 per cent of his time with his sixty-five best

customers. "A's" sales were practically double those of "B's" and his average order was $105 compared to $30 for "B." The analysis showed salesman "A" to be worth approximately $25,000 per year more to his company than was salesman "B."

Experience is teaching that the *kind* of customers is more important than the number. The idea of selective distribution is receiving more attention and being more generally recognized as an important factor in reducing distribution costs. However, it must not be accepted as a panacea for all the evils of distribution. Its adoption calls for caution and for a definitely worked out plan.

Steps in Developing a Plan for Selective Distribution

The chief steps in the development and adoption of a plan for selective distribution may be listed as follows:

1. Analyze sales and selling costs by commodities, items, orders, customers and territories. Determine the minimum size of order that can be filled at a profit and the smallest account which can be profitably carried.

2. Prepare a list of customers representing the maximum volume of business and the minimum number of accounts. Include in this list all potentially large customers not being sold at the present time.

3. Prepare a second list including all customers found to be worth soliciting but not appearing on list one.

4. Make contracts or other special arrangements such as discounts, commissions, terms, exclusive territories, agency franchise, etc., which will result in mutual benefits and insure good-will and special attention to the particular products in question.

5. Develop a staff of salesmen specially trained and prepared to deal with the star customers.

6. Stop soliciting accounts which are not potentially profitable and avoid making too frequent calls on customers in the second list mentioned above.

7. Except in the case of sample orders, refuse to accept orders which call for items or units in less than standard package lots.

8. Make arrangements to take care of incidental business which comes in unsolicited from small customers, so as not to give offence or create a spirit of hostility, but aim to reduce such business to a minimum.

In any plan of selective selling, due consideration must of course be given to decent business ethics and restrictions imposed by law.

The adoption of such a plan has resulted in a stronger, more efficient sales organization and at the same time has brought about a substantial reduction in distribution costs. I believe that the general adoption of the principle of selective distribution, based on more accurate and detailed cost and market information will do much in helping to solve many of our distribution problems. *Paper presented before a meeting of the Taylor Society on Marketing Costs, arranged by the American Marketing Society, New York, December 9, 1932.*

(Comment continued from page fifty-two)

to their apparent disadvantage. In the face of this dilemma they will undoubtedly decide gracefully that their prospects are better if they make contracts accepting a variable portion of social income, especially if by making the basis of mass purchasing a constant, the range of variability is likely to diminish or even tend to disappear.

We have so far emphasized the changes in historical and natural conditions referred to in the quotation from Professor Clark, and the inevitable accompanying changes in mental attitudes. There is more to it: we are actually taking steps toward making labor costs a fixed overhead, and capital and profits the variable.

At this point let us make a clarifying statement which should have been made at the beginning. Labor has always been, and is today, a fixed *social* overhead. So long as through charity, made-work, anticipated work, work-sharing and unemployment compensation schemes we refuse to permit workers to starve, we have established labor as an overhead charge on social income. But this is a social rather than a recognized industrial overhead. It is part of the social accounts which we do not keep, but not a part of the commercial and industrial accounts which we do keep. And by adhering to the fiction that maintenance of labor is not an overhead because we keep it from being an overhead in the accounting of individual enterprises, we deceive ourselves, destroy the morale of workers and make the task of achieving social progress more costly and otherwise more difficult. In talking tonight about the reversal of capital-labor relations, we are talking not about a reversal in what fundamentally exists but in our recognition of and organized provision for what exists.

In point of time the first feeble but significant steps already taken toward organizing labor's overhead status is in legislation relating to accident compensation and to old-age pensions, and in the efforts of a number of individual concerns to compensate for unemployment out of reserves established for that purpose. The actual steps have been feeble but their influence has been considerable and it is safe to assert that we have entered the path which leads to universal accident and unemployment compensation and old-age pensions.

The second and more recent step is in provision of the Industrial Recovery Act and associated acts which establish minimum wages and maximum hours, and promote labor's opportunity for organization to advance its claims to a revised status. To be sure, there is no compulsion to employ; but such compulsions as are involved are an expression of so new a point of view that subsequent steps leading to a compulsion to employ may come without the difficulties one would have expected a year ago. At the least it seems clear that current evolution is in the direction of making labor's income an overhead on industry and of assigning capital and ownership to "second table." Probably many of us will live to see the day when we rewrite the forms of our contracts in such wise that the claims of capital as well as of ownership are equities instead of mortgages, and the claims of wages—of management as well as of detailed execution, of those unemployed as well as of those employed—are fixed charges with priority rights.

(Comment concluded on page sixty)