The role of cost management in network relationships

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Abstract

Recent years have seen rising interest in network economy. The first reason is globalization. The world has been shrunk by information technology and open economies. The second reason is that companies have to take care of costs to meet the descending price rate of the market. Competition in the mature lines of business especially requires continuous productivity improvements. This leads to narrow competencies and extensive outsourcing. Cost accounting has been a widely discussed issue during the last years. Traditional cost accounting is changing to cost management. Target costing, value engineering and design-to-cost are becoming more and more common. The aim of the paper is to find out what kind of challenges networking relationships present for cost management. This paper concentrates on two-party relationships only. Cost information management across the supply system of business as a whole is ruled out. The results of the study show a wide gap between supplier side quality of cost information and customer side expectations. Networking places a number of demands on cost management. Firstly, a company should know the costs of its own operations. Secondly, a company should share part of the cost information with cooperating firms. Thirdly, part of the information flow should be open to all the companies in the network. Companies rarely know the full costs of each product. This is also the case with the companies analyzed. A lot of development work with suppliers' cost accounting systems is needed. A win–win relationship creates a need for open book accounting. Only two out of seven suppliers are ready for this. There is also a need to create mutually accepted accounting practices. Furthermore, in networking economy the following features of cost management are needed:

- accurate customer profitability information,
- accurate information on the influence of volume on profit,
- ability to cost new activities.

These findings do not present totally new challenges for cost management. However, networking relationships seem to emphasize these features more than traditional relationships.

Keywords: Cost accounting; Cost management; Supply chain management; Supply network

1. Introduction

1.1. Background

Networking is more intensive cooperation between companies than before. In a true partnership the customer has made the supplier a complete and open participant in the detailed, long-term conduct of his or her business. According to Drucker [1] networking changes business control because of scratching and mixing the ownership of the economic units. Nowadays companies do not own their business; the business is rather based on common objectives, strategies and teamwork with other competence groups.
Globalization is a widely discussed topic of today’s business environment and it can be seen either as an opportunity or a threat to companies. Industries actually vary a great deal in the pressures they exert on companies to sell internationally. The structure of some industries favors companies that operate on a large scale. Multinationals are seeking to exploit global scale economies.

The machine and metal product industry is experiencing the same trend that the automobile industry went through earlier: decreasing price rate [2]. This can be seen when comparing production volume development and price levels. The production volume of the Finnish machine and metal product industry has risen by 79% from 1990 to 1998 and the gross value has risen only by 49% in the same time period [3, pp. 9–11]. Hannula [4] states that to maintain a certain level of profitability a company has to achieve productivity improvement that is higher than that of competitors. Profitability consists of productivity and price recovery. Product and resource prices are the components of price recovery [5].

The main reason to networking is to find new competitive advantage. Networking can also be seen as a means of responding to the challenges set by globalization and decreasing price rate. The role of cost management in network relationships can be justified by the importance of managing price recovery.

1.2. Objectives and method of the study

The aim of the paper is to find out what kind of challenges networking economy poses for cost management. This paper will concentrate on two-party relationships only. Cost information management across the supply system of business as a whole is ruled out.

The research is conducted with an overview of the literature and the method is conceptual analysis. The objectives are also approached by a case study conducted by interviews in the Finnish equipment manufacturing industry. The case study consists of eight companies that have defined themselves as a network.

2. Networking

2.1. Definition

Networking can be defined in many ways. According to Ollus et al. [6,7] networking is competition by short throughput time, information management and capacity and competence flexibility. Another definition is given by Raatikainen [8]. According to them networking is operation between partners who commit themselves to each other’s long term future. Fig. 1 describes networking as it is to be understood in this context. The network has a certain structure that consists of customers’ and their direct and indirect suppliers’ who possibly have supply relations to each other. Partnership is a widely used typical term for a certain development stage of companies’ cooperation (see e.g. [9,10]). The difference between partnership and network relationship is the context of companies’ cooperation. Network relationship is a supply relation between companies taking part in a network and having one or more common objectives.

2.2. Competition and the buyer–supplier relationship

Porter [11] identified four major methods to become a leading supplier in any business. These

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1 Gross value includes turnover, change in stock, manufacturing for own use and purchasing not related to company’s business.
include partnership with the most demanding customers, partnership with customers with the most complex products or services, doing business in the most regulated and competitive industry and choosing the most developed suppliers.

Matujainen [12, p. 19] introduces a model for efficient governance of the interorganizational business relationship. The model shows that a company has an opportunity to choose between creating sustainable partnership and confidence or continuous controlling of the suppliers. Bensaou's [13] analysis gives support to the classification of suppliers also mentioned by Matikainen. According to this effective supply chain management requires choosing a type of relationship appropriate to product and market conditions and adapting management practices to that relationship. Both Matikainen and Bensaou use the Porterian perspective on customer and supplier power over each other (Porter [14]). Original model is the five-force model in which two forces are customer's and supplier's power over each other. Matikainen handles the forces by the production or sales volumes and Bensaou by the investments made for the relationship. Supplier classification can be seen as an agent promoting the networklike reorganization of the supply chain.

Lear-Olimpi [15] refers to a study of 200 warehousing companies of which 95% are going to build new partnerships. These companies are intended to share more information with the partners. The conclusion of these studies is more intense effect on the partner's way of doing business. This works both from the customer to supplier and vice versa. The basis for modeling the business environment in these contexts is the contractual side of a company.

2.3. Industry structure change

The major trend in recent years has been the centralization of the industry. The creation of big corporations has been worldwide and the companies created are global both in their operations and in their customers (see e.g. [16–20]). For example the Finnish based companies Valmet and Rauma have merged. European car manufacturers, medicine and food industries have concentrated into bigger companies. Even such a decentralized industry as paper manufacturing has seen fusions like the one between the Swedish Stora and the Finnish Enso. Big corporations concentrating on their core business outsource a lot of functions (see e.g. [10,15,21]). Parker [19] states that one of the major trends changing logistics business is consolidation of the industry.

The centralization of purchased volume can be studied through a number of suppliers and volume purchased from them [21, pp. 84–89]. For example, Sandvik Tamrock, a Swedish-Finnish mining and construction equipment supplier, had more than 600 direct suppliers in 1996 and today they have only 160 [22]. Finnish electronics manufacturers have reduced their number of direct suppliers by more than 22% from 1990 to 1994. The amount of partner suppliers has risen at the same time from 8% to 14% of the whole supplier base [23, pp. 31–35]. IBM uses 50 suppliers for 85% of its production requirements; Sun Microsystems uses 40 suppliers for 90% of its production material needs [24]. Diet Coke derives 80% of its sales from 13% of its customers. Taster's Choice reports 87% of its sales come from 4% of its customers [25]. Thus there is in progress a huge transition from subcontracting to system suppliers and fewer first line suppliers (see e.g. [9,10]).

The Finnish Ministry of Trade and Industry [26] studied the structure of supply chains and the reasons why certain companies end up as system suppliers’ while others continue as subcontractors in a networking environment. The study consisted of 33 Finnish metal and electronics industry SME’s. The system suppliers were defined as first-tier suppliers (see Fig. 1: Supplier). They were more developed and they were responsible for larger volume than the subcontractors. Of the system suppliers' net sales 80% were over 10 MFIM while 56% of subcontractors' net sales were under 10 MFIM. Willingness to commitment with customer side, good financial situation, ability to take risks and development capabilities were named as the most important reasons for a company becoming a system supplier.

2.4. Networking in practice

Examples of successful Finnish networks are Ahlström, Nokia, Puustelli and Nordberg. The
Ahlström network consists of paper machinery suppliers and was created in 1991. Since then the personnel employed has risen from 100 to 300 and the turnover of network partners has risen from 60 to 150 MFIM. Only one company has experienced a bankruptcy [6]. An U.S. automaker has given an adhesives supplier a significant role in product development and gained cost savings up to 25 FIM per vehicle [27].

Networking is more typical in high growth and fast changing industries than in slow growth and static industries. However, the focus of networking seems to depend on the growth of the industry. In high growth businesses, for example the telecommunications or software industry, networks concentrate on product. In slow growth industries, for example pulp and paper or metal processing, they concentrate on process [7, pp. 116].

According to the study by Karjalainen [28] outsourcing extensively affects the creation of networks. The authors studied 57 Finnish metal and electronics industry SME’s. Factors relating to costs were the second most important reasons for outsourcing production (45% of companies asked) while the strategic choices were the most important reasons (65%). Cost accounting gives a dual answer to outsourcing. Of the companies 33% stated that costs were an important reason for not outsourcing production. Lack of trust was mentioned as the third most important reason for not outsourcing (20%). The price level of suppliers was the third most typical problem in outsourcing (20%).

2.5. Networking as an answer to challenges

Literature covering the areas of networking refers to clear change in supply chain structure: Customers are organizing the suppliers into different levels (see e.g. [9,26,28]). However, networking includes four main characteristics when compared to traditional competition:

- profound commitment to partners and diversified communication on all levels of the organization,
- transfer of competencies to decentralized, flexible and independent units,
- end product and customer approach for component and system suppliers,
- speed of change and operations increases.

The trends introduced in previous sections lead towards networking. Supply chain management is easier through close relations to suppliers. Innovation power transferred to suppliers cannot be utilized without reliable relationships. End product cost reduction demands customer influence in the supplier product and process development. Consolidation of industries leads to multiple buying volumes, which also will be concentrated on some competent suppliers. These reasons will make intense networking flourish in the near future.

3. Cost management

3.1. The important role of cost management

Dealing with today’s competition is challenge enough, even when we have all the right information. However, if we respond to the wrong information, we could be losing a battle [29]. Cost accounting offers very important knowledge for management both at strategic and operational level. In a world of nonsustainable competitive advantage costs have to be managed both aggressively and intelligently. A firm that fails to reduce costs as rapidly as its competitors will find its profit margins squeezed and its existence threatened. The competitive environment demands the development of sophisticated cost management practices to keep costs down.

The poor state of management accounting is a well-known fact. Johnson and Kaplan made the state of affairs known as early as in 1987 with their Relevance Lost book. ‘Today’s management accounting information, driven by the procedures and cycle of the organization’s financial reporting system, is too late, too aggregated, and too distorted to be relevant for managers’ planning and control decisions. The management accounting system also fails to provide accurate product costs’ [30].
Effective and appropriate modern cost accounting systems and information should [31]:

- Provide a multi-dimensional focus on a multiplicity of cost objects such as customers, products, services, functions, processes and activities.
- Focus less on cost tracking and reporting and more on cost planning and control.
- Support every key business decision, including sourcing, pricing, investment justification, efficiency and productivity measures, product elimination and new product introduction.

3.2. The many faces of cost

Accountants usually define cost as a resource sacrificed or foregone to achieve a specific objective. The basic problems are closely connected to the nature of cost accounting: the problems encountered emanate from four fundamental problems. The problems are: of scope, measurement, valuation and assigning.

The problem of scope entails ascertaining which variables should be taken into consideration. The measurement problem entails a search for suitable variables to measure. The essence of the problem is that what cost accounting needs is monetary units, but the object of scrutiny consists of physical units. Valuation problem means searching for an appropriate way to evaluate resources used. For example the following options are useful: original cost, market value, replacement value and opportunity cost. The division of total cost into parts implies a problem of assignment. Costs should be assigned to cost objects (product, customer, time period, etc.). Any choice among assignment methods of costs is a choice among different ways to divide the whole into parts. Using the cause and effect criterion, managers identify the variable that causes cost objects to incur costs. Most often the principle of causality is used in cost accounting. Direct charge and causal tracing should be used wherever possible. Allocation is the last resort. Allocation is the indirect assignment of cost. Allocation is a 'dirty word' in cost systems – something to be avoided if possible. It implies arbitrariness of measurement and a limit to the meaning of the resulting information [29].

There are several good solutions to every problem. It is not possible to say that one solution is better than another. The solution is somehow a subjective notion. The presence of four basic problems and several options to solve them are the main reasons for the following:

- In a multiproduct environment it is not possible to achieve final certainty of accuracy of results.
- If two persons counted the costs in the same firm without knowing anything about each other, they would not get the same results. The difference between results could be great.

The accounting situation has great influence on options chosen. If the decision situation is well known it will automatically limit the number of options. Networking environment will present a certain kind of accounting situation. The following sections include an analysis of what kind of challenges a network economy creates.

3.3. Cost accounting and supply chain management

Supply chain developments demand the introduction of new management accounting techniques alongside traditional reporting systems. Supply chain developments require the contribution of ideas from management accounting and management accountants, both internal to the firms and in interfirm relationships. The poor state of management accounting from the supply chain perspective is well known: Total cost models are generally not currently available either within individual companies or across company boundaries, cost information across supply chains is currently limited and target costing processes are not well understood [32].

For the majority management accounting practice has limited its scope to the boundaries of the firm. This limitation makes it difficult for the firm to take advantage of any cost-reduction synergies that exist across the supply chain. Such synergies can only be achieved by coordinating the cost-reduction activities of multiple firms. The objective of interorganizational cost management programs
is to find lower-cost solutions than would be possible if the firm and its buyers and suppliers attempted to reduce costs independently. Coordinating the cost-reduction programs at the firms can help reduce costs in two ways: Firstly, it can help to identify ways to make the interface between the firms more efficient. Secondly, it can help the firm and its buyers and suppliers to find additional ways to reduce the manufacturing cost of products. This coordination requires the firms in the supply chain to extend their cost management programs beyond their organizational boundaries [33].

There are only few examples available of accounting techniques being used in partnership situations. Most of the interfirm relationships are only taking place in terms of dyadic or two-party relationships. Little evidence of management across the supply system of businesses as a whole has been found.

Cullen [34] provided examples of accounting techniques being used in partnership situations. The key features were: dyadic nature of the partnership, implementation of open books for both supplier and purchaser, target costing, common and shared cost reduction activities, common development activities, maintenance in each firm of familiar cost accounting and management accounting procedures, and proactive managerial roles of the management accountants. Management accountants worked in multifunctional teams and they were developing their broader managerial and personal skills, commercial capability, as well as their financial knowledge. Much of this work was being done through ad hoc projects alongside the normal accounting systems, which remained unchanged. Only slight impact on the routine structures of financial planning, budgeting and reporting was found. This reflected the fact that there were few organizational changes. Costs were still being reported in a traditional mode.

The study of Karjalainen [28] also includes customers’ contribution to suppliers’ cost reducing efforts. Forty percent of suppliers had contracts demanding decreasing price level. Twenty-seven percent of suppliers did cost reduction work together with their customers. In price negotiations thirty-four percent of suppliers were credited because of capital investments made to improve customers’ products and 24% were granted long-term production volume if they made the investments needed to improve customers’ products. Five case companies’ outsourcing short-term history was analyzed deeply. Three companies used cost accounting to help the decision and two stated the outsourcing decision as a strategic choice not necessary to be backed up by cost analysis. Two companies ended up to open cost accounting with their customers’.

In the partnership relation firms are legally independent entities. Firm policy has no power beyond organizational boundaries. As companies focus on their core activities and outsource the rest, their success increasingly depends on their ability to control what happens in the value chain outside their own boundaries. The scope of cost accounting in that sense is wider in partnership.

Cost accounting practices are seldom exactly similar in different companies. In the cost accounting area there are no formal rules and regulations as in the financial accounting area. Mainly to assist internal decision-makers, accountants develop customized reports designed on the basis of the specific information needs. Different methods create a need to somehow compile information before it is in useful form. Differences between accounting practices easily create ineffective practices. If numbers are difficult to understand people will spend lot of time in arguing about secondary things like the proper way of defining the hourly cost for a machine center. If so, a lot of valuable time for creating something new and improving performance will be lost. Creating widely accepted accounting practices between partners is one of the challenges partnership sets for cost accounting.

As already mentioned, firms are concentrating more business on fewer suppliers. This automatically means further expansion into new functions, and into new product lines for the suppliers. Firms are even buying final products from suppliers. In some cases this means that the supplier has the total responsibility for the product except marketing. This kind of development creates new activities in the firm. May be components for new product should be ordered from abroad, for example. If such activities are new for the firm it has to learn to cost these activities too.
3.4. Customer profitability

Fewer customers and suppliers press for knowledge of customer profitability. The problem is that accountants are not very good at measuring customer profitability. According to a survey of more than 400 chief financial officers, 57% said the inability to measure product and customer profitability is the biggest constraint on their businesses [35]. Large customers tend to be either the most profitable or the least profitable of the entire customer base. It would be unusual for a large customer to be in the middle of the total profitability rankings [36].

Recent research has shown that, once the full cost of supporting customers is taken into account, the majority of customers (usually around 70%) are not profitable at all. In fact the studies carried out by Cooper and Kaplan at the Harvard Business School have led them to the so-called 20–225 rule, which states that in some companies 20% of customers account for 225% of profits, which of course means that the other 80% ‘lose’ 125% of profits. Others have suggested a 25–50–75 rule whereby 25% of customer segments produce 50% of sales and 75% of profits. The problem is that accountants have no idea which customers make up the 20–25% and which make up the 75–80%. Nor must we examine customer profitability over the short term only. The important measure is the lifetime profitability of a customer. Research has shown that customer profits rise with the length of the trading relationship. Satisfied customers spend more, attract other customers, are easier and less costly to deal with, and become less sensitive to price [37].

3.5. Customer specific costs

The difference between product costs and customer-driven costs is the resource-consuming activities that trigger them. Customer driving costs derive from specific customers and their buying characteristics. A number of cost factors are easily identifiable with specific customers and are directly traceable to the respective customers. The most rational system of tracing other customer costs to customers is likely to be based on activity-based costing (ABC) principles. By focusing on activities and the different activity requirements placed on the organization by different customers, ABC provides insight into the activity cost structure of customer-driven costs.

Costs are attached to different types of cost objects at different levels. The number of levels of cost attachment varies from one company to the next. For customer-driven activity costs, there are usually five levels: order level, customer level, channel level, market level, and enterprise level.

Customer specific costs can be calculated with following ABC procedure:

- specify levels of cost attachment,
- specify activities needed by cost objects,
- specify resources needed,
- calculate the total cost of resource,
- determine the cost driver for each resource,
- add together activity costs for each activity,
- determine the cost driver for each activity,
- determine the unit cost of each activity,
- determine the bill of activities for each cost object.

Calculating the total cost of resource includes all four problems of cost accounting. All the other steps have something to do with the assigning problem: the total is divided into parts through different methods.

3.6. The win–win relationship

If customer and supplier are going to share profit there is a necessity for open book accounting. The need to share information must be two way. There is also a need for the customer to open his books to the supplier. Cullen et al. [34] reported profit sharing arrangements in partnership situations: If the project is completed at a cost less than the original budget, then the profit is shared between the parties on an agreed basis.

Buxton [38] also reported similar arrangements: If the cost for a project is below the agreed estimate, both parties share the resulting profit according to a formula. If the costs are above the agreed estimate, they share the loss. For open-book costing to work, however, there needs to be trust between the
parties and this need for trust is important in understanding the whole philosophy of supply chain management [39].

One typical feature of partnership is that some of the improvement efforts are made together. Cost information of high quality is very useful in identifying improvement opportunities. Good descriptions and understanding of activities and processes creates a solid base for improvement. Facts instead of intuition create a good base for defining opportunities for improvement. Improvement efforts made together are one of the main reasons for sharing cost information between partners. Different kinds of profit share agreements between partners also increase the need for reliable cost information. Profit sharing agreements and common improvement efforts together also create a demand for cost information. Before profit can be shared it must determined. One of the simplest definitions for profit is total income minus costs. Determination of incomes and costs may be simple, but it may also be terribly complicated. In the most difficult situation all of the four basic problems concerning both incomes and costs are present.

Concentrating more business on fewer suppliers may also mean higher production volumes for a supplier. Typically the customer is interested in getting some price discounts based on high ordering volume. In a win–win relationship the supplier should be able to calculate how much cost savings higher volume will create. If the supplier has identified a clear understanding of behavior of unit level costs, he or she will be able to answer the question.

4. A case study

4.1. Network description

The network studied consists of an equipment supplier (customer) and seven of its suppliers. Two of the suppliers are service companies providing components, technical support and design service. Five companies are manufacturers, two of them middle sized and three small ones. If the annual net sales exceeds 100 MFIM, the company is categorized as middle sized. Fig. 2 shows the current supply relations of the network.

Cost management challenges in the case network were analyzed as follows: Analyzing and describing the present cost accounting practices of suppliers gives a realistic view of opportunities. To identify targets for the partnership the needs of customers were analyzed. The gap between the present situation and the targets creates a challenge that will be partly described as follows.

The present state of the network’s cost accounting was surveyed by two questionnaires. The first was directed at seven persons in supplier side top management and the second was directed at seven persons responsible for purchasing in the customer side organization. The questionnaires included both open and closed questions. All the qualitative data were gathered by open questions and quantitative data by closed questions. All the scales of closed questions were from one to five.

The following results are based on the answers given in the questionnaires and interviews. The three new challenges found for cost management have arisen from the case study’s open questions, thereby confirming the notions to which the authors were guided by the literature.

4.2. Cost management practices

Top management and accounting professionals were interviewed for the supplier’s survey. General attitudes towards cost accounting were measured regarding importance and level of satisfaction. All those interviewed felt that cost accounting is very
important. Most of them were satisfied with current practices. More detailed results of satisfaction are presented in Fig. 3. Cost information is divided there into seven variables.

Typically cost information is needed in the pricing and offering process. Costs should be presented with the information on items, products, cost centers, projects and customers.

The people interviewed were interested in knowing manufacturing related costs such as materials and salaries of employees. Only two firms used job order numbers to identify different jobs. The use of job order numbers makes it possible to identify, direct materials and salaries used to manufacture the product. Only one firm is recording the actual material consumption of the job.

Overhead allocation did not seem to be interesting for the firms. Typically, the sales price of the order should be high enough to cover the job’s variable and fixed costs and to generate a profit. Only one company used an overhead multiplier for direct work hours. Another company had an overhead multiplier for indirect material costs.

Questions concerning costs per hour per employee were also asked. The aim of this question was to measure the level of cost consciousness of the firm. The question was formulated as follows: How much is the cost per hour per employee and what will it cover. The variation of answers was quite large. It was easy to see that the firms do not see the relevance of this kind of question. It was also easy to see that some people cannot see the difference between cost accounting and pricing.

The understanding of fringe benefits, social security and unemployment payments was also very limited.

4.3. Cost management objectives of the customer

Seven persons responsible for purchasing in the customer organization were interviewed. The primary goal of this project is to increase competence and decrease costs. Secondary goals are to increase openness, business-oriented thinking and co-operation.

When selecting suppliers most of the attention is paid to the following characteristics in descending order of importance: delivery accuracy, high quality, low costs and short delivery time. However, costs are placed only third.

Cost information transfer happens only occasionally between the customer and supplier. The sharing of cost data is therefore insufficient compared to the networking the literature demands. Product development and purchasing were named as the most important customers for cost information. Cost information would be used in trying to influence and decrease the cost level and to increase the cost awareness of these groups.

Opening the books was believed to increase competitiveness of the firm, to help in identifying development objectives, to create a logic base for decision, to create high level business understanding and to increase production volume and trust between partners.

The increase of competitiveness was believed to originate from the following three factors:

- reliable cost information helps to concentrate on fundamentals, mainly on product and process development,
- knowing the present state well enough gives opportunities to evaluate the consequences of actions taken,
- the win–win principle can be implemented correctly only by having reliable cost information.

In summary we can say that the state of cost accounting and cost management in the network studied is poor. The customer is at the development stage in his ideas on utilizing shared cost information.

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Fig. 3. Customer and supplier satisfaction with cost information.
information. The utilization requires at least the next fact: suppliers know their costs and are willing to share the information with the customer.

No supplier is able to deliver cost information that would be at a satisfactory level for the customer. To reach the goals set by the customer side it is necessary to develop the cost management practices of suppliers. If the firm has no information on costs available for internal use, it is totally impossible to share it with anybody. There is nothing to share. The willingness to share cost information with others represents a complete new way of thinking in the metal product industry. According to the preliminary questionnaire only two out of seven suppliers were willing to share cost information with the customer. The suppliers’ interest in sharing cost information could be increased if the customer could specify more exactly what information is wanted.

5. Conclusions

The main reason for networking is to find new competitive advantage. Networking includes following four main characteristics: profound commitment to partners, decentralized and independent units, end product and customer approach for system suppliers and increasing speed of change. Big corporations are concentrating on their core business and outsourcing the rest. Their success increasingly depends on their ability to control happenings outside their own boundaries. The scope of cost management in that sense is wider than earlier.

The poor state of management accounting even in a traditional environment is well known. A new accounting environment demands the introduction of new cost management techniques. Traditional cost management practice has limited its scope to the boundaries of the firm. There is only little information available on accounting techniques used in the partnership situation. Only a few organizational changes have taken place and costs are still reported in a traditional mode.

Firms are concentrating more on doing business with fewer suppliers. Larger customers tend to be either the most or the least profitable. Concentration creates pressure to know customer profitability. In a win–win relationship a supplier should also be able to calculate the influence of volume increase on profit. Partnership also often means a bigger responsibility for the supplier. Instead of separate components they are delivering complete products and systems. This easily means totally new functions for them. This also implies the need to cost these activities.

In a win–win relationship there is a necessity for open book accounting. Openness is needed if customer and supplier are to share profit. Cost information is very useful in identifying improvement opportunities and prioritizing them. It is also vitally important when determining profit. Firms are legally independent entities in partnership. Creating mutually accepted accounting practices is one of the challenges partnership poses for cost management.

The case network consists of one customer and seven suppliers. Increasing competitiveness and decreasing costs is the primary goal of this network. Increasing openness, business-oriented thinking and cooperation are secondary goals. Low cost level of supplier is not said to be the most important criterion in selecting partner.

Suppliers feel that cost accounting is very important but the state of cost accounting is very poor. The suppliers do not seem to see this poor state. Only two firms are really able to control direct costs. Typically the sales price is assumed to cover overheads and profit. Ignorance of employee’s costs and cost information transfer in the network takes place only occasionally. Open book management is a totally new way of thinking and only two suppliers have been able to accept this principle at the moment. Willingness to share information is not enough, the ability to produce the needed information is also necessary. A great deal of development work with suppliers’ cost accounting systems is needed.

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Cost information transfer in the network takes place only occasionally. Open book management is a totally new way of thinking and only two suppliers have been able to accept this principle at the moment. Willingness to share information is not enough, the ability to produce the needed information is also necessary. A great deal of development work with suppliers’ cost accounting systems is needed.

The challenge is huge. A lot of work should be done before there can be open book management circumstances in two-party relationships. The challenge is even greater in interfirm relationships involving several firms.
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