

Show Me the Money: Accepted Value Costing (AVC) Annotated Bibliography

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For more information or to contribute, please email AcceptedValueCosting@gmail.com.

Anderson, David J., *Kanban: Successful Evolutionary Change for Your Technology Business*, Lean-Kanban University (Blue Hole) Press, 2010.

- Chapter 11 *Establishing Service Level Agreements* describes allocating capacity to classes of service beginning on page 134. Figure 11.3 illustrates the concept.
- “We are building more slack into the system.” Page 136 emphasizes this Lean concept. Furthermore, “capacity allocation is just another strategy of the kanban system.”

Argiry, Paul, “Accounting for Internal Use Software”, January 24, 2018.

- Focused on software development.
- About capitalizing costs and amortizing.

Barton, Brent et al, “Reporting Scrum Project Progress to Executive Management through Metrics”, ScrumAlliance Scrum Papers, 2005.

- A functional WBS is required.
- “In order to represent the Earned Business Value (EBV) of a project and its components, an additive weight needs to be assigned.”
- Total Business Value is determined by some ROI calculation or equivalent.
- Only items of direct business value ... should be other than zero. The other items are the cost of doing business.

Bittner, Kurt et al, “Scrum and Money: Getting Funding with Scrum”, Scrum.org webinar July 20, 2017.

- Lean funding means limiting work-in-progress (WiP) for fund/spend demand.
 - Smaller incremental funding amounts are correlated with smaller overhead amounts.
 - If funding demand amounts are huge, then a high degree of certainty on the product and its features is required
- Practical case of bypassing governance (read: big budgeting/planning cycles) leads to “breaking up into \$60,000 chunks” of funding requests (below the capital review threshold) which, actually, is a good thing; this leads to small batches and that, of course, aligns with Lean.
- The right way to fund is to think in terms of desired outcomes.
 - Avoid bottom-up cost estimating
- “Fund in small tranches” which are functions of risk/reward tradeoffs concerning expected value.

- Microsoft did a cost-per-feature estimating study and concluded that not more than a third of all proposed features ultimately were considered valuable and all the rest were waste. In other words, cost-per-feature estimating is no predictor of ultimate value.
- An “hypothesis testing” mindset was emphasized.
- The importance of continuous planning (inspect & adapt) around the money flow was emphasized.

DeGrandis, Dominica, “Lean Accounting: Does IT Need a Time Out on Time Tracking?”, LeanKit blog , January 23, 2017.

- Focuses on the problem with timesheets, defined as “survey-based activity timesheets used for the management of projects.”
- Makes a Lean argument *against* activity-based accounting [sic] for two reasons: 1) decision making on inaccurate data based on timesheets, and 2) she claims (incorrectly) that the ABC approach emphasizes activity over value.
- “Lean and Agile practices encourage team members to break work down as granularly as possible, to improve predictability, collaboration, and quality, and this makes for an increasingly accurate picture of where time was spent. Metrics on time spent actively working are automatically captured — at no extra cost — and can help teams and organizations learn to improve their flow efficiency. This is something timesheets could only dream of doing.”

Harris, Michael D., “Are Fixed Price Contracts Possible With Agile”, presentation to AgilePhilly on February 20, 2018.

- Measure output (things delivered) and outcomes (value received, perceived). Metrics:
 - Variable = functionality delivered
 - Fixed = delivery standards
 - Price paid = functionality delivered times unit price
- For Agile, define an “aggregation model”
 - X teams times Y sprints [focus of presentation is on Scrum but is XP implied, also?]
 - Which teams on which value streams
 - Monthly or quarterly aggregation points with a “sensible” number of sprints
- Aggregate must be at the “right” level to minimize the amount of work crossing the aggregation boundary. Although we all talk about “releasable code at the end of every sprint” in Scrum, most organizations have a longer cadence for actual releases into production to allow one or more whole features to be released. That makes sense for a “right” level.
- Avoid paying for labor hours for development; use fixed-price model, instead.
- View the backlog primarily through a feature lens, with the top priority features being refined sufficiently to roll up to a minimum viable product.
- Align very closely to the fixedTime-fixedCost-variableScope Lean-Agile paradigm. Form a centralized metrics team. Hold vendors and teams accountable for continuous improvement.
- Use story points for up-front relative estimating in Scrum; use function points for relative value of the result (outcome). An accurate function point model does not exist, but a consistent

function point model is practical, reliable, useful. Consistency of counting practice is very important.

Hope, Jeremy and Robin Fraser, *Beyond Budgeting: How Managers Can Break Free from the Annual Performance Trap*, Harvard Business School Press, 2003.

- Refer to “Activity-based Management Models” starting on page 186. The problem is that because budgets show the costs of functions and departments instead of the costs of the activities people perform, managers cannot see the real *cost drivers* of their business (italics in original). Moreover, it is likely that the budget contains significant amounts of non-value-adding costs that remain invisible to managers looking at the financial numbers.

Horngrén, Charles T., Gary L. Sundem, and William O. Stratton, *Introduction to Management Accounting*, Twelfth Edition, Prentice Hall, 2002.

- Activity-based costing and traditional costing are compared starting on page 139. Exhibit 4-5 on page 141 makes two-stage activity-based costing clear in graphical form, and a two-stage ABC system is defined on page 142.
- Page 144 asks: “Why do managers prefer ABC systems to traditional costing systems?” The answer provided is: “... its capability to support cost control – the operational control purpose.” Lean-Agile can take this further by emphasizing decision making as the primary purpose, with operational cost control as the by-product of good decision making.
- Exhibit 4-9 on page 150 is a process map. This is closely aligned to the Kanban Method within which workflow mapping is used in a knowledge worker context to enhance visibility and full transparency while making all work visible.
- Page 153 defines value-added and non-value-added costs. Eliminating the latter is a lean objective. The authors state: “Value-added costs are necessary (as long as the activity that drives such costs is performed efficiently).” *Efficiency* is the point of Lean-Agile practice patterns. Tying proportional cost allocation of indirect labor expense to best practice patterns of team-based behavior creates a positive feedback loop.

Maskell, Brian H. and Bruce L. Baggaley, “Lean Accounting: What’s It All About?” AME Association for Manufacturing Excellence, 2006.

- Derived from Lean Accounting Summit held in Detroit, MI in September 2005.
- Few understand the reports coming out of traditional accounting systems.
- Using standard product costs for decision making is misleading with respect to product rationalization, among other criteria.
- The word “activity” never appears in the article. Instead, the “tools of lean accounting” in figure 1 include:
 - Value stream mapping
 - Kaizen
 - PDCA problem solving

- Box scores showing value stream performance (these are analogous to the relative measures in Scrum and Kanban, particularly the trends over time)
- Simple, cash-based accounting
- Incremental impact of capital expenditure (CapEx) on the value stream maps
- In the section on “Financial Impact of Lean Improvement” the key point is made: “... lean accounting tools are used to understand how the changes taking place in the value stream will affect the operational performance, the financial performance, and also how the capacity usage changes within the value stream.”
- This paper and Lean Kanban both emphasize that reducing waste is valuable because it *creates capacity*. In Scrum and Kanban, we call this “creative slack”.
- Note this important statement: “By understanding this true nature of lean, we change our question from, ‘How large a cost will we save?’ to, ‘How can we use our newly-created capacity to increase customer value and make more money?’ “ Translated to knowledge work, this says: “How can we encourage better value flow and acceptance by exploiting creative slack and eliminating indirect labor accounting wasted effort?”

Olesen, Anders, “The Case for Moving Beyond Traditional Budgeting,” Beyond Budgeting Institute, July 2015.

- Beyond Budgeting is a revolutionary approach.
- Makes the case against budgets used to set performance targets, year-long financial plan forecasts, and maximum labor spending and headcount constraints.
- Promotes relative value measurement, holistic performance evaluation, unbiased expected outcomes, decentralized decision authorities, KPI targets, and trend monitoring.

Poppendieck, Mary and Tom Poppendieck. *Implementing Lean Software Development: From Concept to Cash*, Addison-Wesley, 2007.

- Exclusively focused on software development problems and practices.
- Pages 60 – 61 compare and contrast the funding profiles of projects and products. Page 63 (bottom) draws vague conclusions based on Agile patterns of behavior that, now in 2018, are commonly accepted.
- Pages 240 – 241 describe how a software development business case can drive project funding. The authors emphasize the following (*italics in original*): “... only realistic business cases should be used to justify development, and that it will be necessary to *follow-up by measuring the actual results*.” The authors provide no guidance for this. On the top of page 241, they make an important statement, again without providing guidance: “... every development team we talk to would be delighted to understand the financial objectives of their efforts, make tradeoff decisions with those objectives in mind, and experience the sense of accomplishment that comes from having met those objectives.”

Rickards, Robert C., "Beyond Budgeting: Boon or Boondoggle?", *Investment Management and Financial Innovations*, Volume 3, Issue 2, 2006.

- Critical evaluation of Better Budgeting, Advanced Budgeting, and Beyond Budgeting.
- Figure 2 on page 70 shows the relationships among the various budgeting concepts. Beyond Budgeting is positioned at the top of the pyramid as involving the most radical changes and affecting the smallest relative number of potential users.
- Page 74 enumerates the building blocks for rolling budgets:
 - Concentrate on the critical business processes
 - Remove the budgeting system form tactical planning
 - Set market-oriented goals
 - Rely on quick preview of information instead of detailed, budget-based calculations
 - Abandon the calendar year as the budget cycle, transitioning to rolling budgeting
 - Reduce manual data entry, organizational structure duplication
 - Simplify the budgetary process
 - Decentralize oeprrational planning

Sirkiä, Rami and Maarit Laanti, "Lean and agile financial planning." Officially published as "Adaptive Finance & Control: Combining Lean, Agile and Beyond Budgeting for Financial and Organizational Flexibility", 2015 48th Hawaii International Conference on System Sciences.

- Specifically tied to SAFe and Beyond Budgeting.
- Page 6 near figure 2 says: "Even though it is hard to estimate the total cost per project beforehand, it is easy to track the cost once the PSI (potentially shippable increment) gets done. You simply need to see from the team backlogs how many days each individual spent on which feature."
- Page 3 under "An Agile Approach to Financial Planning and Control" makes good points but with no guidance on *how* to do these things:
 - We simplified the cost center planning by taking it to a higher level of granularity.
 - We downplayed cost center planning and implemented visibility for deliverables.
 - Our company had already earlier separated forecasting from target-setting which allows for more realistic forecasting and more ambitious target setting.
- Page 7 under "Results and Conclusions":
 - The paper suggests a new way of doing adaptive finance and control in an agile enterprise. The suggested method requires abandoning detailed cost center accounting, approaching uncertainty using agile and lean planning, and moving to task fluidity.
 - The agile concept provides good tools to control software portfolio and resource allocation in a modern, more rational way.