



## PKF Texas' Profit Enhancement Services Realize Lost Revenues

*For the last several years, Better Bags, Inc. (BBI) aligned its organization to meet international competitive forces, while still serving its growing customer base, at a profit. As part of its plan, Byron Hebert of PKF Texas was brought in on a specific Profit Enhancement project that would help BBI Bags identify basic accounting practices. These practices would reliably reflect BBI's current level of financial performance more effectively in order to find root causes and immediately improve its systems.*

### Expenses Greater Than Revenues

Through PKF Texas' Profit Enhancement Services, Byron Hebert, CPA, began his work with BBI by structuring a decentralized cost accounting system that was non-existent. Once completed, he focused on root causes and specific actions to be taken to reduce expenses. Hebert continually communicated his findings and immediate next steps to the management team – a very critical interaction because he knew he would require their input, under a different costing model, to develop and implement a new one-year forecasting model.

While going over these action items, Hebert could clearly determine that the mix of products BBI worked with had drastically changed over the last 12 months.

“We were working on an assumption of a 70/30 percent product mix, but the percentage was more like 30/70,” says Rafael Alvarado, BBI's president and CEO. “The overall average price of our product had dropped like a bullet – more than 15 percent! The existing accounting system calculated numbers on a consolidated basis, so the system hid subsidies and excessively low-priced items

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that weren't being noticed because BBI had been working on an average cost and average return.”

### Intervention Proves Worthwhile

When Alvarado called Byron, his objective was to carry out a basic needs analysis of BBI's financial function and determine the most important areas for improvement. Hebert found out that there was an urgent need to develop and implement a

decentralized cost structure to clearly show the hidden costs drivers that were then too difficult to find.

“I gave Byron specific instructions,” says Alvarado. “I wanted him to look at the financial system as a whole, and

understand how we were accounting for the revenue and expense sides of the company. Were the systems the most effective ones for us, and if not, what should they look like?”

For Hebert, who has worked in Profit Enhancement for a number of years helping clients through similar opportunities, the analysis was an easy one to make

“It was a classic situation – BBI had been increasing its capacities in the



Mexican and Far Eastern sources in an environment of decreasing prices; its U.S. production in Houston was negatively impacting BBI's financial performance because the company carried a higher cost structure than what its customers could bear," he says.

### **The Plan**

Once he had designed and implemented a decentralized cost accounting structure, Hebert assisted the BBI team and put together a plan involving restructuring the balance sheet, looking at options to dispose of fixed assets, and expanding more aggressively its global production capability. This plan would allow BBI to provide the customers with the right cost structure while still meeting their needs. As a result, profitability would improve.

Offering solutions like these characterize PKF Texas' Profit Enhancement Services. In working with Hebert, Alvarado says facts and figures began to come to the surface. "We realized that the cost-accounting system needed to be reviewed so that it would be practical for our accounting department to ensure a proportional weigh-in of all the expenses based on the different sales centers and cost centers we had."

### **Results Prove Profitable**

To date, the recommended and implemented processes are assisting the company on making more educated decisions from the financial side, while reducing its cost drivers to the hilt.

"While we need to continue making more painful decisions and shift the production to where the competitive advantage is, we have to swallow a bitter pill," says Alvarado. "A good number of our

loyal workforce is being reduced; however a new, stronger organization will come to fruition and higher skilled positions may become available. The work done by PKF Texas and Byron led us to understand a scenario much greater than the geographic boundaries of Houston. With international trade or globalization, no longer can we be protective of our own turf. In places such as Asia, there are hidden subsidies to manufacturers."

The holes may be filled, but the tank is slow to fill. Still, the change to the cost-accounting system has made an impact on the business.

"Dramatic results do not happen overnight," says Alvarado. "We started this process in December 2003, and just began to see a minor impact in June and July of 2004. August is going to be much better. We not only streamlined our systems; we also reallocated our production loads."

Hebert says that the disconnect for BBI is not an uncommon scenario. PKF Texas sees it daily, and part of his job is to help bring about a change.

"We want to be a catalyst for positive change in a company. If the client isn't making money and distressed in a turnaround situation, we can help them not only restructure the balance sheet and find money, but as importantly, figure out *why* they are not making money. We guide them through making some of the tough decisions."

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