

CUSTOMER ACCOUNTING AND FREE RETURN POLICIES OF RETAILERS

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- Case study -

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ABSTRACT

This case study deals with a retail company. It illustrates how the use of customer accounting can improve its profitability and reshape customer relationships. The case also discusses parameters of appropriate transfer pricing and incentive systems. Students can use this case as an illustrative example in class and use the open-ended questions to reflect on the managerial implications.

Keywords: Activity-based Costing; customer profitability; target setting; teaching notes; transfer pricing.

1. INTRODUCTION

SEND is a catalogue-based fashion and decoration retailer. The company sends glossy catalogues to its customers several times a year. Customers can order using a standardized list that they mail to SEND, or via phone. SEND puts a strong emphasis on creating lasting customer ties through extensively long order calls by phone. There, trained phone personnel try to establish a very personal and deep connection to the customer, digitizing information about their lives, such as the customers' favorite leisure activities, or their pets' and family members' names and birthdays. For this, SEND provides a toll-free phone number. Cost of goods sold (COGS) are on average 75% of the retail price. Customers pay by debit card. To match online retailers, SEND offers free shipping, refunds any returns, and even pays for the return shipping charges. Overnight shipping incurs additional processing costs for SEND.

2. CUSTOMER ACCOUNTING (approx. 40 minutes)

Recently, SEND worries about an increasing amount of manufacturing, selling, distribution and administration (MSDA) costs. SEND currently allocates MSDA costs based on net sales. Now, SEND wants to re-assess its profitability per customer group using activity-based costing (ABC). SEND has clustered the following customer groups:

	Customer Type 1	Customer Type 2	Customer Type 3	Customer Type 4
Gross sales [EUR]	900	1,200	3,200	4,800
COGS [%]	75%	75%	75%	75%
Items returned [#]	-	6	3	36
Items returned [EUR]	-	275	750	2,300
Orders per year [#]	1	7	6	18
Phone orders per year [#]	1	-	-	18
Time spent on phone placing orders [h]	0.50	-	-	9.00
Overnight deliveries [#]	1	-	-	15
Regular deliveries [#]	-	7	6	3

SEND has also discovered the following activity cost driver rates for its MSDA costs: