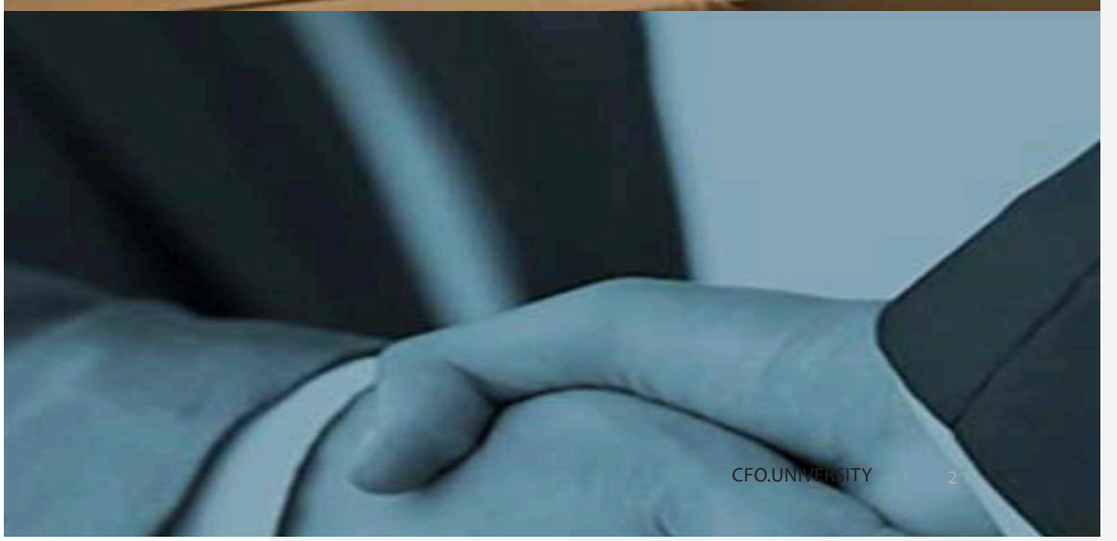
THE FOUR PILLARS OF CFO SUCCESS

CFO.UNIVERSITY



The 4 Pillars of CFO Success

Website: CFO.University
EMail: info@cfo.university

Enhance your career opportunities and gain greater financial security with CFO.University.

Click one of the pillars below to begin.

Accounting | Finance | Treasury | Leadership

ACCOUNTING

A key pillar supported by governance, recording and reporting.

Do your Governance, recording and reporting systems lend solid controls and transparency to your business? Is your corporate structure and governance process in line with your size, goals and culture? Is your business effective at recording transactions that impact key aspects of your business? Are the reports prepared by your department forward-looking or historical in nature? This first pillar to defining the attributes of a successful CFO, explains the importance of accounting, as key in the house of the Chief Financial Officer. The accounting pillar is supported by the core competencies of governance, recording and reporting.

1. Governance: Governance includes the initial and ongoing legal documents that give structure and rules to an entity as well as internal controls to protect corporate assets and reduce the risk of incurring unanticipated liabilities. Businesses that don't address these areas early on are more likely to fail.

Unless we happen to form the business, we inherit the governance rules and governance culture for the companies we go to work for. This may lead us to overlook the value in understanding the framework the company was built on, including the current rules of governance. I encourage any senior financial officer to read the documents that formed the company and the current rules of governance. It's possible you'll find outdated rules, expired schedules and conflicting items that have arisen over time.

By reviewing these documents, you'll have a good understanding of the rules of engagement. Internal controls are the policies and related principles that a company uses to strengthen its internal guidance system. A comprehensive framework for internal controls has been developed by The Committee of Sponsoring Organizations (COSO) of the Treadway Commission. It's a very good tool to benchmark your internal control framework against.

Like many of the defining attributes of a successful CFO, Governance is tightly linked to another attribute, risk management - which is a core competency under our treasury pillar. More about risk management in the treasury section.

2. Recording: Transaction recording and closing the books are the foundation for creating useful internal information about your business. The architecture behind excellent recording systems and processes prevents errors, minimizes inputs and is time sensitive. Over the years, I have learned when employees in the recording process have a sense

Globalization and big strides in technology continue to put pressure on companies to make faster and better decisions.

of urgency, other CFO responsibility areas can thrive. This is because CFO operations start with effective record keeping.

In the recent past, this competency has been cast in a dark light. The term "transaction processing" and the misconception that this admin work is not value added has been interpreted by many to mean this area isn't important or doesn't deserve our attention. That thinking could not be further from the truth. (For those of you outside Canada and the United States, I apologize for the following American football analogy.) The employees responsible for recording at your company are like linemen in the Canadian or National Football Leagues. Without them, we'd never get a snap off. To be a successful CFO, you need highly effective people, processes and systems in this core competency.

3. Reporting: Financial and managerial reporting should result in information you can trust. It should create transparency and insight into business operations. It should also help you make great choices. Efficient, timely and accurate reporting systems lead to better and quicker decisions. This clarity is crucial for each of your stakeholders - shareholders, creditors, customers and employees. Timely, accurate business information is more important for decision making today than ever. Globalization and big strides in technology continue to put pressure on companies to make faster and better decisions. Here are some tips on how to improve your recording and reporting process:

- Record transactions when the activity occurs,
- Simplify entry,
- Eliminate systems,
- Enter only what you need and what you will use,
- Monitor and correct entries immediately after input, not during the month end close,
- Reconcile accounts when you can, not just during the close,
- Innovate your closing process – ask, "Is there a better way to do this?" often,
- Ask what information your team needs to make the best decisions and act on the answers,
- Include key non-financial information in your management reports to give context to the financial statements and vice versa,
- Historical (think last month) financial information is a decaying asset with a very short half-life. Try to have your reports ready for management review within one week of the end of the business period, and
- When it comes to managerial reporting it's better to be almost right quickly than to be perfectly right slowly. (If you are a practicing Chartered Accountant or Certified Public Accountant, I expect your heart rate just went off the charts). Remember - these reports have a short half-life.

FINANCE

A seamless handoff between the accounting and finance departments is critical in creating and executing an effective strategy.

Finance uses the discipline and data from a strong accounting team as the launching pad for planning and creating their company's future. A seamless handoff between the accounting and finance departments is critical in creating and executing an effective strategy. The Finance function is about creating the optimum analytical framework to make strategic decisions.

There are three core competencies that make up a highly functioning finance department:

1. Budgeting and Planning: The first building block of a finance department is to provide the financial roadmap for the company based on the direction agreed to by the Board of Directors and the executive team. Companies frequently refer to this as the budget or plan. The link between what has been and what we expect is the critical handoff that occurs between the accounting and finance teams. For continuity and understanding, the financial reporting structure between the historical financials and budget systems should be the same. You'll know this link is broken when the budget or plan can't be explained in the same terms you narrate your actual results.

Companies use many techniques and tactics to develop their plan and build a budget. The important products from this process are:

- A narrative that explains the direction the company is headed.
- Forward looking financial statements (budgets) with enough detail and at the right intervals to add insight and allow for course corrections as the business environment changes. (Imagine how your GPS corrects your course when a road closes or a traffic jam lies ahead.)

Even the most robust planning process contains uncertainty. Therefore a sensitivity analysis to help stakeholders understand the expected or potential volatility in financial performance or position is

"The finance pillar uses fuel from the accounting and treasury pillars to guide the company's financial future and that's just as important as it sounds!"

critical. Tap into your risk management competency under the treasury pillar to complete the sensitivity analysis.

- Key performance indicators (operational and financial) and other ratios of critical importance (bank covenants, bonus targets, "caution signs", etc.)
- Support for the major themes included in your business plan. Confirm the premise of the plan is reinforced by facts and outside expectations.

2. Forecasting: You may have heard this in the past, especially if you have been heavily involved in the planning process, "The budget is stale the day after it's published". Unfortunately, that is often the case. Worse, sometimes it's stale before it's published. The implication in the statement is that the budget process isn't worthwhile. We don't believe that. The process the company goes through to plan for the next year or five years is extremely important. It means we need to create the business discipline and expertise that allows us to adjust our operations to real time. This leads us to the second building block of Finance, the forecast.

To develop the forecast the finance team integrates the company's current performance relative to budget with the real-time business environment. The budget to actual comparisons highlight where we have exceeded or not met expectations. Learning what is creating these differences is one of the most valuable insights we can give the company. The objective of the forecast is twofold:

- first, to build an understanding of how internal and external forces are changing the company's business opportunities, and
- second, to assist the company in taking advantage of or providing a remedy for those changes.

The cornerstone of forecasting is the forecast model. It should be robust enough to capture the major moving parts of your business but nimble enough to be updated quickly. Scenario building and sensitivity analysis are an important component of the model. To do this requires inputs such as historical data, trends, opinions, known ensuing variables and projected growth rates in terms of sales, expenditures and financing. Forecasting to ensure your company is on track for future success should be an ongoing process. One way to build this discipline into your routine is to include a review of the forecast in your monthly management meetings.

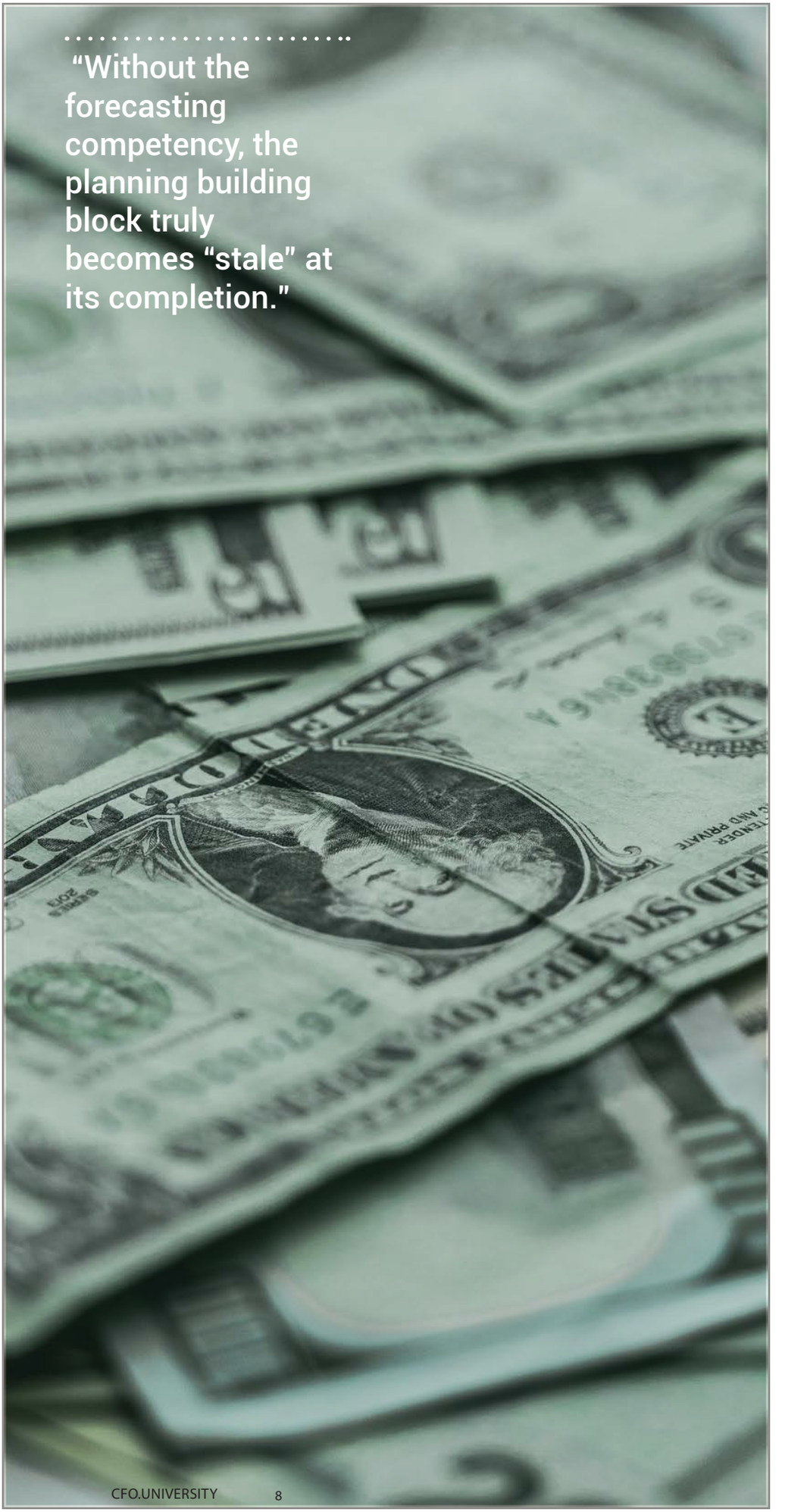
3. Investment Analysis: The third building block of Finance is creating the framework to analyze new opportunities as they present themselves. Capital projects, such as an acquisition, building a new plant or licensing technology should be evaluated under a common set of financial criteria to make capital spending decisions effective over time.

This area of finance is where the deep analytical skills are housed.

Company policy on investment criteria originate in this area. The corporate cost of capital, return hurdle rates, tools to communicate investment opportunities, cash flow models to develop returns and the financial analysis of investments/ divestments are prepared here. The resources in this part of finance are typically focused on the asset side of the balance sheet and must work closely with Treasury to be aware of the capital limitations the company may have.. The key message in the finance pillar is how each piece is connected to the others. Here are a couple examples:

- Without the forecasting competency, the planning building block truly becomes "stale" at its completion. With forecasting, the finance process becomes a dynamic, near real-time tool to make your business better.
- Without the capability to effectively and consistently analyze new opportunities the plan, as it pertains to growth, is stymied and corporate investment appears arbitrary, or worse.

The finance pillar uses fuel from the accounting and treasury pillars to guide the company's financial future and that's just as important as it sounds!



TREASURY

This key pillar of the CFO function provides the fuel and discipline to manage and grow a company's capital base.

This next section covers the "show me the money!" attribute: treasury. Treasury encompasses three critical aspects for long term business success: cash management, capital raising (funding) and risk management.

A successful CFO has the capabilities to effectively lead each of these core competencies.

1. Cash Management: The lifeblood of any company is cash. Without cash or the belief that cash is quickly available, the stakeholders of a business will flee to businesses they believe are more sustainable. Cash management is the discipline designed to provide comfort to stakeholders that cash is being handled and monitored in a manner that will allow the business to operate normally. It includes daily activities such as balancing the check book, processing credit card transactions, and reconciling cash accounts. Unreconciled bank accounts are a red flag that a business is not operating effectively.

Forecasting cash requirements is another key responsibility that falls under cash management.

Know your ground zero. Ensuring cash is available to cover payments is a top treasury responsibility. Ground zero for any company is the minimum short-term cash needs. For this exercise let's define short term as three months. Do you know your company's ground zero? A frequent tool used in the turnaround industry is the 13-Week Projected Cash Flow Report.

If you don't have one, we strongly urge you to take the time to build one. Even if you don't believe you "need" it at this time, the learning that will take place in terms of process, capabilities and systems will be well worth the resources you invest in it. If you have a finance team maintaining plans and forecasts, they will be a great resource and interested party in developing a 13-Week Projected Cash Flow Report.

2. Capital Raising (Funding): Know your options. Funding can come in many different forms; operating cash flows, terms with suppliers or customers, loans or lines of credit, and raising equity. Each form has different costs and risks, but the objective is the same – provide the company with enough liquidity to execute your plan with some cushion for variability. Having cash, either on hand or available, will not only help avoid a liquidity crisis or even bankruptcy, but will also position your business with adequate resources to capitalize on growth opportunities as they come about.

The funding aspect of Treasury starts with a capital plan. The following is a list of items to include in a capital plan.

Current financial position:

- Capital structure,
- Cost of capital,
- Leverage, and
- Liquidity.

Prospective items:

I. Corporate funding targets and red flag levels

- Leverage
  a.Debt/EBITDA
  b.Debt/Equity
- Normal bank covenant ratios
- Borrowing capacity
- Cost of capital

II. Liquidity policy (13-Week Cash Flow Report and minimum cash requirements)

III. Dividend policy

IV. Potential New Funding options

- Debt funding sources and pri
  (may require asset appraisals)
- Equity raise sources and

pricing (company valuation required)

- Alternative sources of capital

V. Requirements for the maintenance of a Financial Forecasting model (See Finance Pillar).

3. Risk Management: The importance of capital and readily available cash drives companies to implement risk mitigation measures to protect their capital base. Therefore, the risk management function is a natural fit for the treasury attribute. Many internal controls are designed to protect against cash shortfalls. These controls include preventing cash from being misappropriated, monitoring bank covenant compliance to preserve liquidity and executing an effective capital policy to maintain a reasonable cost of capital. The demands and rigor associated with effective cash management are a natural extension to solid risk management practices.

Risk management also includes insurable risks, for example; property and casualty, business interruption, employee benefits, labor strife, cyber-attacks and fiduciary risk. In addition, there are uninsurable risks, risks that can't be underwritten by a normal insurance company. Examples of uninsurable risks include:

- Profit margins,
- Raw material pricing in a commodity driven business,
- Logistical costs incurred due to weather or other circumstances,
- Planning errors made by the company,
- Company reputation,
- Regulatory changes, and
- Pandemic events.

Identifying these risks for your company and assessing the resources required to manage them comes at the intersection of the accounting pillar, governance (defining corporate rules and establishing audit procedures), and the treasury pillar, risk management (identifying and managing insurable and non-insurable risks). Much like the baton exchange described in Pillar 2 between accounting and finance, governance and risk management are deeply connected with the actions of one having an impact on the other.

Treasury, like all the pillars in the house of the CFO, requires great people, processes and systems to be world class. If you're not quite there yet, CFO.University's practical learning framework can help you and your team.

LEADERSHIP

"The ability to lead leverages the other CFO pillars of success."

Leadership seems to be one of those traits defined by, "You know it, when you see it." I have met a CFO who was the brightest lightbulb in the room but could not lead their business to the light switch. I have also met a CFO who didn't seem to work that hard and wasn't a rocket scientist but was able to move mountains in their job. Why could one get things done while the other struggled? Leadership.

The fourth pillar in CFO.University's course structure is leadership. The ability to lead leverages the other CFO pillars of success, allowing the CFO to bring tremendous value to their company while creating a broader pool of options for their career.

We approach leadership in three progressive stages:

1. Internal - Self-Awareness
2. External - Using your leadership style to build teams
3. Strategic - Leadership that motivates people to follow you

Some of you may recognize the internal and external focus as the way Stephen Covey divided habits 1-3 from habits 4-6 in his book, *The Seven Habits of Highly Effective People*. Learning about ourselves and how others perceive us is an important first step in learning how to lead. Once we overcome that hurdle, we can apply that learning to building teams within our organizations. The last step is creating or sustaining a sense of common purpose for the stakeholders of our organization.

1. Internal - Self-Awareness:
How often have you been surprised by the way somebody described you? While walking with a friend I'd known quite a while, he stopped me, looked me in the eye and asked if I'd ever been a preacher. I enquired why he asked. He responded by telling me he thought "I had a gentle, caring way of dealing with people". I wasn't sure I liked that description of me and certainly wasn't immediately buying it. Now, in those days, I thought of myself as a hard-nosed financial professional, delivering the facts and respecting my staff but not being of unusual kindness. I was never hired as the "hatchet man", but I was often in positions where the business required significant overhauls.

How I perceived myself and how my friend viewed me, were very different. Over time, I have come to hope he was more right about me than I was. And for some odd reason, since then I have tried to prove him right. (Maybe that was his intent all along).

The point of my reflection is to underscore the way we see ourselves is going to be different than the way others view us. Narrowing that gap is a huge step to improving relationships and expanding your influence. Think about all the time that could be saved resolving issues if we could perfectly describe them, have all parties perfectly understand them and resolve them in perfect harmony. How often have you written an email and after seeing a response you reply, "Oh, that isn't what I meant, here is what I meant to say." We are individuals seeing the world and ourselves through our lens. If we can't see part of it through the lens of others, we are going to live in a pretty small space.

The brilliant inventor, with great ideas, learns quickly that if their vision is going to succeed it needs to be described or explained in a way the rest of us can understand.

The first step in developing your leadership skills is to bridge the gap between how you see yourself and how others see you. In Covey's language this is self-mastery or independence.

2. External - Using your leadership style to build teams:
Learning who we are, especially to other people, can be an empowering and frightening experience at the same time. Early in my career a colleague told me a story that has stuck with me. He was the manager at a facility in Portland, Oregon. A new employee working in the office had a significant personal hygiene issue that was making

it difficult for other employees to work with her. She was finding it difficult to complete her work due to the lack of cooperation she was getting from other employees. The easy path would have been to mostly ignore her and let her go after her 30-day probationary period expired. Instead, my friend took her for a walk and delicately mentioned the issue others were having with her. She was aghast and terribly embarrassed. But she cleaned up the problem and eventually grew into the role of a facility manager herself.

She learned a tough self-awareness lesson, for sure, but think of the courage her manager displayed in addressing this directly with her. It would have been easy to punt the issue to the human resource manager or let her go at the end of the probationary period. Instead, he displayed compassion for her situation. Before he spoke with her, he considered the possibility she would quit, leaving him with a staffing problem. He cared more for her as a person than as an employee and had the conversation with her before he was prepared for the potential consequences. He chose preventing her from further embarrassment over extra work that would be required of him if she left abruptly. Instead of quitting she thanked him. He also gained a trusted colleague/friend for the rest of his career/life.

This same concept applies to team building. Building trust and creating a safe space for members of a group to practice and refine their discipline is foundational to developing a well-functioning team. That doesn't mean all is harmonious. In fact, contention is a requirement for real learning and growth. An effective leader helps the team debate and learn in a respectful, benign atmosphere. The only way to do this is to know your team members, what inspires them about work and, more importantly, why they chose to work at your company. Covey refers to this as interdependence, where our success is dependent on others and their success is dependent on us.

Having members of an organization recognize common goals while emphasizing their individual contributions are important components in building well-functioning teams.

3. Strategic – Leadership that motivates people to follow you:
Many times, the position we hold in a company gives us certain authority. That authority often gives us certain power over others. It can be easy to confuse authority and power with leadership.

A CEO at a local company recently went out of her way to explain why the company's annual bonus was the same dollar amount for all employees. She said, "People are already paid different salaries based on if they are an engineer or a technician, a CEO or an office assistant . . . every role in a company is important to meeting the goals, or it shouldn't be there in the first place." The bonus plan is simple, 10% of net profit is put in the bonus pool and divided equally between each full-time employee, prorated if they were hired during the year.

That is a serious company team building exercise. I have been involved in many different types of compensation schemes, but never have I seen one that is so commonly shared throughout the organization. Imagine the potential for creating a singular focus from its employee base if the company's leadership can express its vision and work plan effectively. The sky might be the limit. However, this isn't a story about compensation as a leadership tactic, it's a story about how employees in a company feel they fit in, how important they are. This CEO said, "I view the

"Know your company's Why, the reason it exists, and use it to lead."

annual bonus as an extra benefit for helping to contribute to the success of the team." And in doing so she made everyone feel they were a contributor. Simon Synek, in his book Start with Why, identifies the ability to inspire people with a sense of purpose or belonging as the key to great leadership. Corporate executives have many ways to motivate their workforce. To truly inspire an organization requires a vision and communication that rallies folks behind a common cause. We may not be called on to be the leader of creating the Why at the companies and organization we serve, but to reach the Strategic level of leadership, we must understand our purpose and champion it. Know your company's Why, the reason it exists, and use it to lead.

A professional community of member scholars, companies and trusted advisors committed to the development of Chief Financial Officers.

CFO.UNIVERSITY