

THE SEVEN HATS OF THE FD



Last month we looked at how FDs should be good co-pilots (sitting alongside the CEO) and storytellers (turning the numbers into narrative). This month, **Richard Young** explores the next three ‘hats’ they must wear, and discovers how a mastery of processes and systems, being a business arbiter and acting as trusted counsel are also crucial to the FD role.

Most FDs agree that one of the defining aspects of their role is the ability to see both right across and deep within their organisations, in a way no other director can. Not even the CEO routinely surveys the kind of granular data the FD must – while at the same time taking a strategic view of operations.

Our next three ‘hats’ for FDs – ‘engineer’, ‘magistrate’ and ‘consigliere’ – speak to this breadth of vision. ‘As FD, you see the business from start to finish,’ says Andrew Lewis, group FD of Avon Rubber and winner of Young FD of the Year at the FDs’ Excellence Awards 2011, supported by ICAEW.

‘All those different elements come together in the profit and loss (P&L). Unless you have a handle on that breadth of activity, you’ll only ever know the numbers superficially – and a board is right to expect the FD to know the organisation a bit more deeply than that.’

So while it’s important to be a great engineer – having a feel for the mechanisms that allow the organisation to operate and taking delight in designing them for maximum efficiency – a good FD marries that to broader objectives.

‘You shouldn’t micro-manage processes,’ says Stuart Bridges, CFO of FTSE 250 insurer Hiscox. ‘And it’s not just about delivering a business case – a good FD can make a decent business case out of anything. It’s whether the

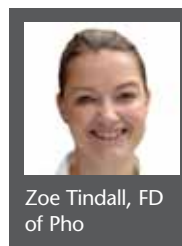
reality of it at a higher, commercial level makes sense.’

So being an arbiter of smart decision-making is also key. A good magistrate listens to the evidence, evaluates it in context and makes judgments that everyone can respect. ‘It’s important to be fair and for people to recognise that,’ Bridges adds. ‘You should be seen as someone with the influence to change a decision if it’s wrong – and be approachable enough to have others challenge your view.’

Finally this month, we have the consigliere – the trusted advisor and close confidant(e) of those in power. The word derives from mafia families – it was popularised in the Godfather movies – and hints at a need for the FD to be a discreet, wise and knowledgeable counsel to both their board colleagues and managers more generally.

The engineer

In many organisations, the FD takes board responsibility for a wide range of departments. And they’re often the only director with formal business training. So understanding how the business functions – how its systems and processes knit together to deliver a platform for value – is an essential part of the role.



Zoe Tindall, FD of Pho

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- Storyteller** – creator of a clear narrative for internal and external audiences.
- Co-pilot** – partner to the CEO with a complementary skill set.
- Magistrate** – arbiter of disputes and enforcer of the law.
- Consigliere** – trusted counsel offering advice at the highest level.
- Engineer** – master of processes and systems; architect of business models.
- Muse** – promoter of fresh thinking and value-enhancing decisions.
- Rescue service** – identifier of problems and presenter of solutions.

The machinery of business has undoubtedly become more complex and fast-moving. The interrelationships between systems and operations, across supply chains and within processes, mean that simply fulfilling your fiduciary duty as a member of the board these days demands a watchmaker-like attention to detail.

For the FD, that requirement to be something of an engineer is even more acute. 'There is a deep desire, for me anyway, to understand how everything works and how the jigsaw all fits together,' says Zoe Tindall, FD at restaurant chain Pho. 'As FD you worry things will fall into gaps unless you can see how all the cogs are meshing together. You want to ensure it's a seamless business operation, that everyone's back is covered.'

In her current role, Tindall is also living out the other kind of engineering FDs are often called in to do. 'In a smaller business, there's no infrastructure to do things for you,' she explains. 'As FD, you have to get out and do it yourself.'

At Pho that's meant building up the finance function, equipping the head office and rolling out technology to support the company as it grows. Tindall has been here before – as FD of the Yo! Sushi chain, and at other private equity backed businesses.

'Good systems and processes are the foundation of everything else you do,' she says. 'If you know that they all work well, you get a confidence – that your numbers are correct, that information is reliable, that risks have been identified and managed. A risk register, for example, is a crucial part of the business machine – engineering isn't just about IT systems talking to each other.'

The engineer, then, doesn't just pull together different parts of the machine, ensure it's well oiled and capable of supporting the business. And it's not just about making sure the back-office functions run smoothly. Good engineering creates value.

'Raising finance and buying and selling businesses comes down to a run-rate and a multiple,' Tindall explains. 'So how do you assess the multiple? Yes, there are comparables and market rates – but you can be at the top end of a multiple range purely because you've been doing all this engineering in the background. That contributes to the quality of what you're doing, of the profit you're delivering.'

So it's a value-enhancing part of the role, too. 'It's about running a continual due diligence process on your own organisation,' she says. 'That's not just being an internal police officer nit-picking. It's about engineering value in your business. Unless all those processes and mechanisms are in place and working together, quite aside from what your business actually does, you simply can't deliver sustainable value.'

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Colin Bramall,
CFO of James
Hull Associates

The magistrate

Managers and employees, customers and investors will rightly ask where the FD was, if the organisation lacks financial discipline. But it's not enough just to hold people accountable or apply the right accounting rules. The FD must also create a context for evaluating decisions and be a fair arbiter of disputes – a true justice of the peace.

'The magistrate role probably comes closest to the clichés about FDs,' says Colin Bramall, serial FD for private equity backed businesses and currently CFO at James Hull Associates. 'But ultimately we are the ones who have to say "no" on a day-to-day basis. And most backers want you to do that, too. They want someone testing the assumptions and the ideas people are coming up with.'

When the magistrate role is lacking, companies can end up in trouble. 'I'm very dull when I start a new job: I always ask whether the balance sheet has been reconciled,' says Bramall. 'Nine times out of 10, when you go into a business that needs attention, someone will have forgotten the balance sheet basics. That's where the real dangers lurk.'

So why does that happen? Usually it's simply that, instead of laying down the law, an FD has been distracted. 'Often, for political reasons, an issue has not been confronted,' says Bramall. 'When that happens, you have to put a line in the sand and say, "no further – here's the reality, now we have to deal with it".' The flip-side, he adds, is that: 'In a business performing badly, people don't recognise that they're doing some of the right things. They're distracted by negative sentiment. As an FD, you can present the numbers and explain performance to get people to react in a different, more positive way.'

If the balance sheet is the statute book, the evidence before the court is usually cash. 'Mike Gifford [FD at Cadbury Schweppes, 1978 to 1983] was one of the best FDs I ever worked with,' Bramall recalls. 'Long before private equity's prominence, he was preaching the message about cash. The presentation of the management accounts was turned on its head to ensure the P&L and balance sheet were focused on it – then the message was spread throughout the organisation.'

The great advantage of cash is that it's an easy law for people to obey. 'I take the P&L down to EBITDA [earnings before interest, taxes, depreciation and amortisation] – everything under that is outside line managers' control,' Bramall explains. 'Then I change the presentation of the balance sheet – removing everything that's subject to financing and tax, so you're left with fixed assets and working capital. The aim for managers is then simple: make that figure as low as possible.'

That simplicity allows the magistrate to keep people on the straight and narrow. 'For example, if you keep

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squeezing marketing people constructively, it can become a real source of invention for them,' Bramall says. If a magistrate can't command respect by showing an understanding of the people over whom they are making judgments, their decisions may be ignored.

So they need to work within clearly defined and well-communicated rules. 'As FD, you must challenge the performance of the entire management team,' Bramall observes. 'Done well and respectfully, it leads to a great working relationship. And if you're a tight group, pressure for better performance will strengthen the team, not weaken it.'

The magistrate role is also vital when an FD is required to explain the business to outsiders. 'It's in a due diligence process that you demonstrate that you're really on top of your brief,' says Bramall. 'An FD gets interrogated during due diligence more thoroughly than anywhere except a court of law. If you're not on top of it, you can be personally responsible for a loss of value in a transaction.'

Bramall has one more lesson for would-be magistrates: get a great financial controller, a policeman to the FD's magistrate. 'Ultimately, as FD, you can't be distracted by the numbers issues the whole time,' he concludes. 'You have to know they're taken care of. It creates the headroom to let you fulfil all the other aspects of the role.'

The consigliere

The Godfather movies and the television series *The Sopranos* offered insights into the tight-knit world of the mafia. Alongside the head of every crime family sits a consigliere – a respected figure who the boss can turn to on the most sensitive matters and biggest decisions. For an organisation to function effectively, the FD needs to play a similar role.

Stuart Bridges is clear: the primary role of the FD is to be a good company director. 'Like it or not, I have a responsibility for everything that goes on in the company, whether it's directly in an area that reports to me or not,' says the CFO of FTSE 250 insurer Hiscox.

In other words, fiduciary duties are paramount. But it's impossible to fulfil them – enforcing strong governance and taking responsibility – without being part of a tight-knit management group. 'It's a given that a CFO gets the finance elements right,' Bridges explains. 'What you're really in there for is the strong challenge – in particular of the CEO. There aren't many other people who can do that.'

If the challenges were always hostile or if the relationship was fraught, it wouldn't work. And that's why the FD has to play the role of the wise counsel who can test other members of the team while keeping their respect; someone they turn to for advice before a decision is taken.



Stuart Bridges,
CFO of Hiscox

'We had a board debate about the common themes of companies that fail,' Bridges says. 'One of them is that there's no-one who can challenge the CEO successfully. If you get one who won't listen, you can't address a problem when it happens. You have to be able to tell a CEO in a frank way when their actions are wrong.'

That demands a degree of authority – and others' trust that, as FD, you know what you're talking about. 'It's good to be right,' stresses Bridges. 'But there's a danger. If you wait until you know you're 90% right, often you're too late. So you need good gut instincts – and to be brave enough to get it wrong sometimes.' So allying an instinctive knowledge of the business and its operations with a toughness of character is the secret to making this role work. But it helps when the finance function is designed – like a mafia network – to keep the FD informed.

'We have a central analysis group here, for example, a small team whose role is to follow up ideas into how we might change,' says Bridges. 'They're constantly benchmarking us against others. And they're able to get the facts to support our ideas and instincts. As CFO, it means a hypothesis can be backed up or destroyed very quickly. It allows for a sensible debate, but one settled fast. A debate where no-one has much by way of facts is often lengthy and gets you nowhere.'

Bridges reinforces this 'wise counsel' part of the role by being an active member of the market, sitting on both industry and non-industry boards. Those external links ensure he can bring outside ideas to the board, enriching the debate and preventing 'groupthink'.

However, dissent among the leadership of a mafia family would be a recipe for disaster. So the FD-consigliere should never forget that even when their counsel is ignored, they must present a united front.

'Once you've tested people's positions and influenced the course of action, there's got to be a united face,' says Bridges. That's not entirely analogous to the mafia concept of 'omerta' – but without such a 'code of silence' about board-level debates, it's much harder for an FD to position themselves as the trusted influencer of their peers.

'The key for me is that both sides of the equation recognise that the challenge aspect needs to be there,' Bridges concludes. 'CFO is one of the positions that can actually provide that, and it also allows you to be a sounding-board for a lot of ideas. It puts you into the role of confidant(e) – and someone who can really shape value creation.'

SAVE THE DATE

Richard Young will chair the ICAEW Finance Directors Conference 2012 on 16 May in London. The programme will reflect the content of this article. For more information see icaew.com/fdconference



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