

# MANAGEMENT EXTRA

A monthly review of current thinking in the key areas of strategy, human resources, marketing and finance.

FINANCE

IS BEST  
PRACTICE  
WISHFUL  
THINKING?



## Forget silver bullets and focus on a finance framework that delivers for you, says a new ICAEW report by **Rick Payne** and **Philip Smith**. Richard Young explains.\*

First the bad news. Finance directors (FDs) and CFOs hoping that the latest whizz-bang technology or management consultant's wheeze will transform their finance function overnight can forget it. In the words of a new ICAEW report, 'The Finance Function: A Framework For Analysis': 'Sometimes they help and sometimes they don't.'

After looking at dozens of surveys and hundreds of academic articles on what makes an effective finance function, the report's authors have concluded there is no such thing as best practice. 'The core message is simple: there is no perfect answer,' says Dr Philip Smith, himself a former FD and MD and now a turnaround specialist. 'A lot of people will claim there is best practice in finance, but the truth is there is no one-size-fits-all approach.'

'It depends on the skills of the management implementing it – and it has to be adapted or even thrown away as the world changes around it.'

The good news? After undertaking all that analysis, Smith and his co-author Rick Payne (respectively a faculty committee member and its technical manager with responsibility for the FinanceDirection programme), have come up with a different way of approaching the issue. It's a way of framing the discussion around what your finance function does, how and why, in a way that eschews 'best practice' and focuses instead on what your organisation really needs.

'Given the variety of recommendations we unearthed, it occurred to us that a framework was a better option,' says Payne. 'It meant we could design something that would adapt to future changes in the way people do business. Managers and advisors can use it to guide their thinking or discussions on how their finance function is doing and how it needs to develop. And it meant we wouldn't just be issuing yet another survey on the role of the finance function!'

### Not just another survey

That's an important point. There seems to be a never-ending stream of papers, articles and products designed to tackle 'the changing face of finance'. But over the years, a lot has stayed the same. 'The first thing we noticed was that the idea of business partnering, for example, really isn't that new,' says Payne. 'We found commentary on finance working more closely with operating units from reports in 1963 – and even in 1928, there were references to it.'

He points to IBM's biennial survey of CFOs that has data on the time spent on transaction processing, control and decision support from the past eight years. It suggests the balance hasn't changed all that much since

2003, despite some major shifts in technology, accelerating globalisation and a meltdown in banking. Why?

'Automating processes is one thing,' says Payne. 'But it would seem that cost savings are taking priority over staff redeployment so that finance can provide higher-level decision support and more sophisticated analysis.' In many cases, finance function structures haven't adapted and achieved an appropriate balance in their activities.

External drivers are also a key part of the new framework. Rather than try to set out an ideal finance function – which could be rendered obsolete by a shift in technology, a change in regulations or a shift in business model – the framework suggests CFOs and their teams evolve their function to adapt to these forces.

Within the finance function, it's a similar story. The way monthly ledgers are prepared has changed radically. But the need for the finance function to monitor and report on financial performance has not. 'The idea is that you could go back to the 1950s, when some of the earliest work we've collated was written, and find the same activities and interactions between different aspects of the finance function,' says Payne. So there is a foundation which means finance leaders in different sectors, countries and sizes of business will be able to use the model to design their own function.

### Adaptable and appropriate

'Depending on sector and context, differing organisations will have differing management and planning horizons,' says Smith. 'For Rolls Royce, you might assume, the financial horizon of a project like a new engine will be over years or even decades. By comparison, a retailer will tend to have a much shorter financial horizon – with next week's sales of key importance.'

Ultimately, accounting is an articulation of the financial consequences of operational activities, he adds, so it has to be tailored. 'The danger for the finance



Rick Payne leads the faculty's FinanceDirection programme.



Dr Philip Smith is a member of the finance and management faculty committee. He specialises in improving financial management systems.

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## 'The idea is to map your own finance activities and business model on to the framework to arrive at the most suitable way of implementing them for your organisation'

function is looking at the numbers detached from what's actually happening.'

So the framework emphasises explicit analysis of the interrelationships between the business and finance; and between the different parts of the finance function. 'The boxes all have to be in balance,' says Smith. 'If one part changes, you have to look at how the others need to be reconfigured.'

These connections fall into two categories, information and influence, which also highlights the fact that not every scrap of data generated by the function is necessarily helping the business. If there's too much data flowing out of one part of the function – compliance, for example – it runs the risk of swamping the attention of the management and control function. That, in turn, unbalances the business because it has its own influences over operational decisions.

### Putting it into practice

Because the framework is not itself revolutionary – merely an attempt to distil a context for an effective finance function – it's not uncommon to see the principles it espouses in many organisations already.

A great example is Pitney Bowes. Helen Jesson, its recent past VP and group financial officer for Europe (now senior VP and CFO EMEA and Asia Pacific for leading pallet and container pooling group CHEP) took part in the launch of the programme back in April – she's a former chair of the Finance & Management Faculty – and says she'd already been through this process in all but name back in 2009.

'We redesigned the finance function, in part because it was getting increasingly frustrating for me to manage the balance sheet,' she recalls. 'Every time something surprising cropped up, there would be three or four people involved and it was impossible to get proper answers and quick resolutions.'

In other words, the interrelationships had become faulty, and there was insufficient accountability within the function's different activities. Add in a need to reshape the function to meet a new group structure – keeping it aligned with the business, a core tenet of the framework – there was ample reason to undertake a redesign.

'We split the teams between the people handling the historic stuff from those looking to drive future results,' Jesson explains. The back office functions were centralised, increasing efficiency. Those aspects of the framework can still evolve – but it's much easier to manage their skills, influence and deliverables as a single unit. And their outputs – the framework's interrelationships – are stable for every other part of the finance function.

'Then the forward-looking group, broadly decision support, were distributed around the business units,

where they could be most responsive and effective,' adds Jesson.

The project, she admits, was 'substantial'. But the result is a finance function that's efficient, well matched to the new global structure and flexible enough to evolve with both local and global changes. It's been so successful, the design was also implemented in the US finance function.

### Where next?

The framework is an evolving concept. So the faculty is keen to hear additional input on the factors it picks up, how they might be treated by CFOs in the field and where the project might go next. 'Examining what "successful" finance functions look like in different contexts is probably the next step,' says Payne. 'The framework provides an excellent way of structuring such analysis.'

And it's worth remembering that not every activity – and certainly not every driver – sits exclusively within the finance function. In many businesses, taking a holistic view is going to mean bringing in other departments, too.

'The point of the framework is to make people ask questions,' says Smith.

'When you're looking at your finance function, especially when you're changing it, you can refer to the framework and say, "hang on – there's a mismatch here". It's about keeping it all balanced. It's no good having a world-class accounting function and a perfect record on compliance if finance is completely disconnected from the business.'

That's something Jesson endorses. 'You have to adapt to the way the rest of the organisation works,' she says. 'If there's a strong culture of strategic thinking, it's not that critical for the finance function. But if no one else is planning three to five years out, maybe your team needs to up its game in that part of the framework.'

And, Payne stresses, this isn't about doing more or getting bogged down in ticking boxes. 'The key is to look at the whole picture – even if you then decide you can de-prioritise certain areas based on your particular situation,' he says. 'The finance function can't do everything. It can't be all things to all people at all times. And the CFO is not a superhero.'

### How the framework comes together

There are three core elements to the framework for the effective finance function – activities, interrelationships and drivers (see Figure 1, opposite). The idea is to map your own finance activities and your own business model more broadly, on to the different parts of the framework to arrive at the most suitable way of implementing them for your own organisation.

First are the finance activities themselves. These are familiar to any accountant and must be clearly aligned

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to operational activities outside finance. So under management and control, for example, you include the processes for generating financial and non-financial information; internal audit; and applications – like cash management and investment appraisal.

Second, there are the interrelationships between these activities. Sometimes that’s a one-way flow of information or influence; but in most cases, there’s a free exchange between activities which, if ignored or undermined, can threaten the ability of the finance function to operate effectively.

Finally, there is a series of drivers – factors that will help determine the design of both the activities and the relationships. For example, with private equity ownership, cash flow generation and debt management become more significant, and that’s going to change both the information flows and need for finance to influence operational behaviours. Equally, a change in regulation is going to mean the finance function has to shift its monitoring and reporting capability.

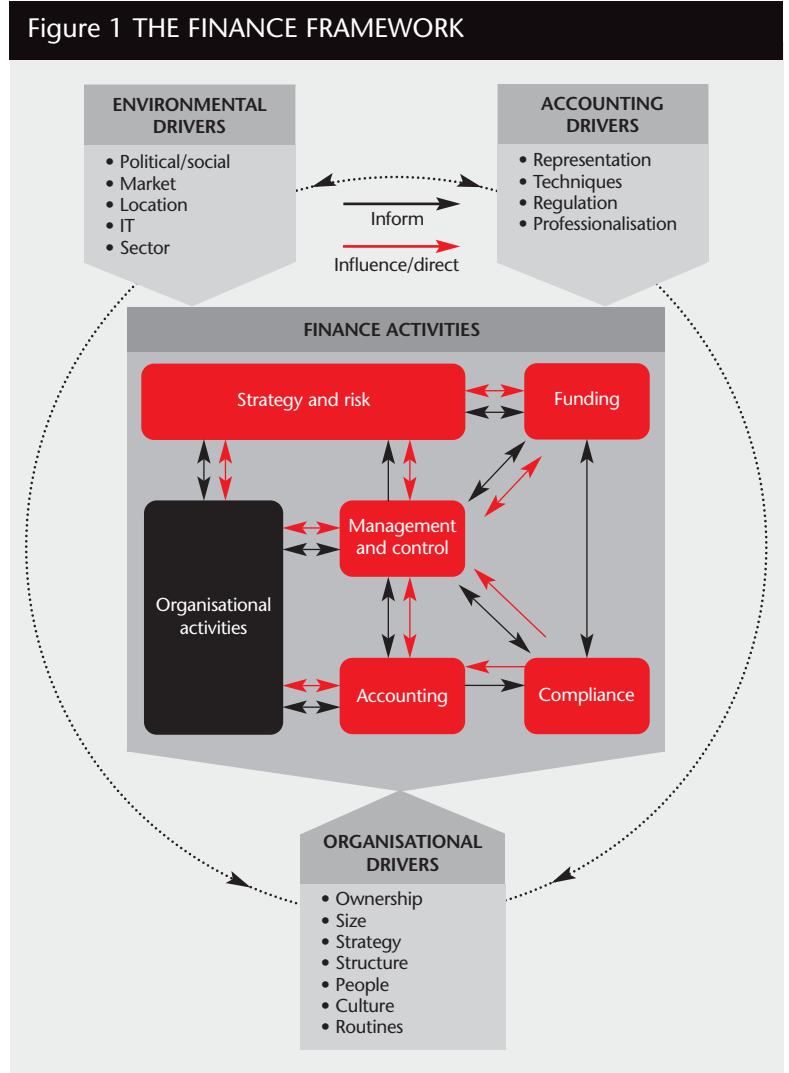
None of the elements works in isolation – indeed, the point of the framework is to ensure that none of them is treated out of balance with the others. And every organisation will have its own pressure points and need to emphasise different areas depending on sector, locations, size, ownership structure and so on.

‘The point is to create a link between financial performance and organisational activities,’ says Smith. ‘You’ll only get the outcomes you want if it’s working well. You have to design your own processes within the context of the framework, processes that map on to your business.’

‘The key thing is the interrelationships,’ he continues. ‘Each part of the finance function impacts every other part. While the framework itself is a constant, how the activities within it are implemented will change over time.’

‘That’s why it’s so important that the people overseeing it understand how they’re working,’ Smith concludes.

‘That doesn’t mean they need to be deep functional experts. But they need to know what questions to ask and how to ensure that the activities in any given box don’t create problems elsewhere in the business or the function.’



‘The Finance Function: A Framework For Analysis’ forms part of ICAEW’s Finance and Management Faculty thought leadership programme, FinanceDirection. Copies of the report can be obtained by emailing [rick.payne@icaew.com](mailto:rick.payne@icaew.com)