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The Diverging Roles of the CFO: Broadening Expectations

Growing private companies need more from their CFOs than accounting precision.

by Mark D. Working

It is getting tougher these days for chief financial officers to meet the expanding performance expectations associated with growing private companies. Owners and executive managers of privately held businesses rely on their CFO for traditional financial leadership, as well as guiding the company's strategic planning efforts and preparing the company for potential public ownership. The expertise required to lead the company in all of these areas has become quite broad, often beyond the capabilities of a single person. This makes for interesting challenges in defining and staffing the financial organization of the future.

CFO TRAINING GROUND

The traditional training ground for CFOs has been public accounting (as high as 90%, according to some sources), where skills related to accounting, systems and compliance are developed and honed. These accounting, as opposed to finance, skills and processes must, to varying degrees, be supplemented by planning expertise necessary for the development of operating and capital budgets that define management objectives and support external capital providers.

CONGRESS PASSES SOX

In the past five years, a rather sweeping transformation has occurred in public accounting, brought about by the deficiencies in financial disclosure that were thought to be at the root of the public company scandals (Enron, Worldcom, Tyco, etc.) that bloomed in the aftermath of the dot-com bubble burst. In a fit of "we're the government and we're here to help you," Congress passed Sarbanes-Oxley (SOX) to improve the accuracy of financial reporting and make public company (and private companies aspiring to be public) CFOs, CEOs and Directors personally responsible, under the weight of onerous penalties, for the accuracy of corporate disclosures. The fever for adherence to the requirements of section 404 of SOX has been a boon for accounting firms, and they have refocused their businesses on auditing and compliance. These firms have added staff by sopping up all accounting talent out of universities and elsewhere, and have directed these resources towards technical auditing tasks and reporting compliance. Non-compliance-oriented services that were in vogue in the late 90's have been scaled back or shed. It remains to be seen whether these changes will ultimately enhance corporate transparency and performance, but it has, however, shifted the skills and expertise of the people that are being trained and developed in public accounting. It is only a bit of a stretch to say that accountants seem to have gained a more intimate understanding of leaf structure, but have become less able to discern the overall forest. This change has significant implications for the talent pool that private companies draw from for financial staff.

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IMPACT OF INSTITUTIONAL INVESTORS

While the energies of accounting firms have been focused on the business of compliance, a countervailing economic force, institutional private equity investors, has been remaking the ownership landscape of privately held businesses. Private equity firms now own a significant chunk of middle-market businesses in the U.S. With steadily increasing resources at their disposal, this trend is likely to continue, if not accelerate. While institutional investors have an interest in financial compliance and transparency, their overriding objective is building corporate value. For an investor-owned privately held business, the CFO has a central role as the protector of value creation and the guiding force in the allocation of capital resources. In a well-functioning executive team, the CFO is expected to provide insight into the value implications of customer relationships, products and markets, investments in equipment and plant, and acquisitions. As we've written in this publication before, the emphasis on growth and value creation that has become the norm for investor-owned businesses makes a CFO who provides a forward-looking economic perspective on the business, is willing to ask the hard questions, and backs conclusions with rigorous analysis, an exceptionally valuable resource.

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STRATEGIC ORIENTED CFOs

In today's world, the regulatory environment demands highly specialized accounting technicians who can faithfully apply complex

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rules with appropriate precision. At the same time, a highly competitive and dynamic business environment places a premium on strategic-oriented CFOs that are analysts, planners and leaders who can help drive value creation. This role requires a proficiency in finance and an understanding of business economics that is difficult to acquire in the day-to-day work of public accounting. Rarely does this combination of skills reside in a single individual and the challenge is how to find or develop these people. It is becoming more likely that accounting and finance are separate roles requiring different people with complementary backgrounds. How companies source the financial expertise that they need and organize it within the business is changing. Putting the right people in the proper roles is an important element of a successful strategy. No matter how important the compliance function, our advice is to not sacrifice financial leadership in favor of accounting precision. ❖

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ABOUT ZACHARY SCOTT

Zachary Scott is an investment banking and financial advisory firm founded in 1991 to serve the needs of privately held, middle-market companies. The firm offers a unique combination of in-depth knowledge of the capital markets and industry competitive dynamics, sophisticated analytical capabilities, and proven expertise in structuring and negotiating complex transactions. For more information on Zachary Scott, please go to ZacharyScott.com.

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