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## **The Finance Director and the Treasurer Transcript**

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## The Finance Director and the Treasurer

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My qualifications to talk on this subject rest mainly on the fact I have served in both positions; and that to some extent my career has reflected my conclusions. When in 1976 I was appointed Group Treasurer of Unigate, I was sent for after a few weeks by the Chairman, a business grandee called Sir James Barker. 'Good morning Hodson', he said, 'I've seen you wandering about. What do you do?' 'I'm the Group Treasurer' I replied, rather pleased with myself. 'Group Treasurer, Group Treasurer', said he, 'What does that mean?' Deflation of eager young party, and strong indication of ignorance on the part of great and good person.

Over the next five years I watched no less than three finance directors, accountants all, collect their cards and depart, increasingly realising that I somehow was not CFO material at least in the eyes of the Board, despite getting to grips with the treasury side of things. Friendly headhunters continuously told me that you had to be an accountant to be a finance director, and I therefore thought that I was the victim of a cruel joke when Sir James's successor summoned me and asked whether I wanted to drink from what was clearly a poisoned chalice. He was serious, although my bout of hyperventilation took a few moments to subside, but I thought privately (and still do, truth to tell) that the board had simply run out of options. I was also lucky that they could find my office. It was indeed a stroke of luck, but I must have done something right because I survived six years in the job and departed of my own volition. And I subsequently had the best part of four years in the same job at Nationwide Building Society, again exiting quite unaided. . FD's role only marginally about beancounting

Ten years a finance director is some people's idea of purgatory, but I thoroughly enjoyed it. And my headline conclusion is that, whatever else it is about, the job is only very marginally about beancounting, or, in other words, the physical business of accounting. This may seem entirely counterintuitive, but it's worth pointing out that the title is Finance Director, or Chief Financial Officer, or sometimes Director of Corporate Finance. It's quite unusual to come across a board position called Accounting Director. In fact I rather think that they are a mythical species.

Before you conclude that-rve-taken leave of my senses, let me say that the position is in part about the presentation and interpretation of the results of basic accounting. I never had any difficulties with this, not least because of early business training as a credit analyst in New York, under the guidance of a gentleman who rose to be the head honcho at Mellon Bank of Pittsburgh. His opening line at his first seminar was 'All accountants are liars', and he then proceeded to ensure that all us boy and girl bankers were given the firmest possible grounding in the theory, practicalities and, most importantly, range of possibilities of financial accounting, so that we would not be taken in by the antics of accountants.

I found what I learned at the knee of the master quite enough for the complexities of the CFO's jobs that I subsequently held, and I am not aware of any weaknesses on the accounting level that developed during my tenure of such positions. I make this point, not to deride or denigrate the importance of accounting as a financial profession, but only to say that a thorough knowledge and analytical understanding of financial accounting is the essential ingredient for a successful CFO. I conclude that the ability to undertake the more detailed requirements of an accounting qualification and of professional accountancy is a bonus but not a sine qua non.

What is perhaps far more important for an FD is to appreciate what dashboard instruments each level in the organisation needs to drive the body corporate forward - to learn from the past and make decisions for the future. This management information, summarised in the form of Key Performance Indicators (KPIs) may be in part but not exclusively based on standard accounting techniques and books of account. In particular the provision of appropriate management information is of huge importance to boards, as I have argued in an earlier lecture.

Nonetheless it is my experience that the issues which really earned my corn were rarely about accounts, accounting and/ or the provision of management information, or even their concomitant, control and compliance. The world of financial and regulatory management is full of talented accountants, controllers, internal auditors, and compliance officers: the CFO's skill will be to select and subsequently to manage them successfully. This responsibility should be entirely routine for him; in terms of the successful fulfilment of his office, there will probably be no upside, but only downside things go awry. It is devoid of brownie points..

Shaping corporate and financial strategy and decision making

Where I believe I made my greatest contribution was in helping to shape the organisation for today and for the future. If, as I have regularly argued throughout this lecture series, a key role of the Board is to determine and ensure the implementation of corporate strategy, it is clear that a vital ingredient of the latter is bound to be

financial strategy. Financial strategy is not about the past; it is about the ongoing relationship between debt and equity, target and maximum, about the source of that equity, and the structure of the debt, about the hurdle rates of return for projects and acquisitions, and the organisation's willingness and ability to accept financial risks generally, and the steps to be taken to mitigate them. Such matters lie at the heart of corporate strategy and boards will look to the CFO to make the dominant contribution in their determination. It is a totally forward looking task. His other key roles stem for the most part from the various elements of financial strategy set out above. For instance, the quality and depth of project and investment appraisal is of great importance to the organisation and it almost always falls to the CFO to create and maintain the project appraisal framework, ensure adherence to its rules, and in particular to safeguard the integrity of the financial projections and assumptions implicit in it, and to verify, criticise and support the financial analysis. It requires an FD of grit and courage to stand up to a Chairman and/or CEO with the bit between his teeth, the sap rising, and the opportunity there for the taking - with only the time needed for careful and thorough appraisal between him/ them and capturing the prize. But it's a vital task. Although I have to say that even the most assiduous of FDs would probably not have prevented the fate of the printing business who did their appraisal of a new hitech piece of printing machinery beautifully - except for the relative height of the machinery and the shed in which it was intended to reside. The resultant factory with a form of church tower at one end became a joke local landmark and a constant reminder of how things can go unwittingly wrong.

It is this role of counterpoint which can be enriching and creative. I am great believer in top executive teamwork, my example usually being modern soccer teams where all positions bar goalkeeper are to a degree interchangeable, although to my pleasure I find that the simile can now be applied to the English Rugby Union XV. So it is with boards, and the most effective will contain an FD who will be supportive, but will at times display his specialist skills, those of financial analysis, and who will ensure that the appropriate decision, control and governance framework is in place and adhered to, and who will be, as it has been so aptly put, 'the conscience of the organisation'. In this regard I am close to an FD who had to threaten to put the excessive use of a helicopter to travel to and from a CEO's home on his PI ID (a mere increase of some £50k) in order to persuade him to kick the habit; the FD found it particularly uncomfortable to have a friendly onsite investment analyst's Friday lunch disturbed by the whirring of the rotors and the vision of the betweeded CEO, racing off for a sporting weekend. The dog and the guncase were the real giveaways.

The combination of these should produce a healthy and productive dialectic discussion at executive and board level, and in these the FD will be at his best. But there will be extreme cases where he will feel it necessary to say, as Charles de Gaulle was wont famously to do, 'NON'. I find myself constantly wondering as yet another corporate disaster unravels where the FD was and the extent to which he allowed himself to be overridden.

#### Risk perception and management

A key part of the skill is his perception and understanding of risk as well as his ability to assist in its mitigation. Although seen, at first flush at least, as a bureaucratic burden, I believe that the current strong movement towards risk identification and analysis is one of the most useful items that has come out of the increasingly prescriptive governance environment in which we live. This should bring out the CFO's prime skills, both in ensuring that the risk review is regularly and appropriately undertaken, and probably in most corporate organisations being responsible for it, but also as a strong contributor to its content, both in extent and detail, and well beyond his natural territory of financial risk. Getting the best out of financial markets

Another vital contribution will be in his understanding of financial markets, debt and equity, cash and derivative: how they work, who the key players are, how to get the best of them, and how to communicate with them. There was a time not so long ago when the FD's function in this regard would boil down to 'corporate finance' - in reality not much more than working with the merchant bankers on acquisitions and rights issues; and 'investor relations' that is chatting up financial journalists and investment analysts and ensuring that the latter were suitably close to the mark in terms of forecast results, and also keeping the major investing institutions happy and informed. It is a far more complex world these days. Rating agencies, focussed on debt, are just as powerful as analysts and journalists, focussed on equity, debt markets are increasingly securitised, relationship banking is under great pressure and multibanking is the norm, derivatives markets' exchange traded and OTC, are providing ever more sophisticated methods of balance sheet and financial risk management. Quite simply FDs face a vast range of products, from a vast range of markets, offered by a vast range of intermediaries and principals. Understanding, selection, communication at many levels, and focus are key skills in the FD of today. Internal financial literacy and structure

My final pillar of the FD's job description, and one which I felt both personally and corporately rewarding, is to ensure that his executive colleagues are financially literate to an appropriate level, and that the internal financial structure optimises the incentives for something in which I keenly believe in the context of corporate groups - what was for a while called, rather horribly, 'intrapreneurship'. So far as financial literacy is concerned he has to be a proselyte, or at least employ one, as I did, taking the view that what they-would not believe or take it from me, would be easily assimilable from a folksy (and looking back very nonPC even by the standards of those days) academic like the one that I found for the purpose. It was so successful at Unigate that at least the top 100 executives in the business had, by the time I left, a working knowledge of accounting, balance sheet management, the financial aspects of project appraisal including required rates of return, and cash flow management. This made the second, internal structure aspect of the task much easier. Some organisations,

even very large ones, are so integrated, even though very large, that an internal structure with self accounting profit centres is difficult to achieve. Most in my experience however lend themselves to a number of such units. In their context, internal structure and targets become a fascinating part of the FDs job: provision of notional equity, particularly in financial service organisations where capital requirements play such a large role: targets rates of return on equity; cash flow targets etc. In creating and supervising such an internal structure, an FD will be greatly assisted by a high degree of financial literacy on the part of each of the unit management Contrast the Treasurer

In summary the FD will inevitably be called upon to record and present the past, but his principle requirement will be to manage today in the light of his view of the future, particularly in terms of market developments and risk. In short he must both a decision maker in his own right, and a participator in decision making, always looking forward, not back. What is so interesting about this analysis is the extent to which the requirements parallel the job description of the Treasurer. Briefly, the latter's role is about the management of the balance sheet (the level and structure of debt, equity and investments) of cash (liquidity, transactions and flow) of currency (arising from export, import and overseas holdings) and of financial risk generally (a combination of all these facets as well as the use of the insurance market). In this he will make ever increasing use of technology, and particularly intelligent systems, emphasising the critical and strategic decision making nature of the role. He should (but not always will) have significant commercial interaction with his corporate colleagues, particularly at board level as his role affects financial strategy, and at many managerial levels as it affects their commercial activities, and specifically in respect of currency exposure. Stated in broader terms, treasury management is about the use of financial markets, banks, OTC and exchange traded, to the benefit of the organisation, as well as managing the relationships inherent in them; and about financial risk management; but above all about a view of the future and making decisions in respect of it.

At the same time, the Treasurer will, by professional training, have more than a working knowledge of financial accounting, and, as a decision maker, he will be more than familiar with the need for effective management information; very often his job description will include investment appraisal; his job is already intertwined with financial strategy; and his understanding of financial risk will give him more than a head start in the identification and mitigation of risk generally. Without a doubt therefore he potentially has the bulk of the professional, managerial and personal requirements required of a successful FD. It is this recognition that has meant that, in the US, the Treasurer himself is usually designated the Chief Financial Officer, whereas the Controller is seen principally as the head of the accounting and control function, without the broader responsibilities. He may be an accountant but the chances are equally that he will have come from some other financial profession, and quite probably banking. This is in stark contrast to the UK where the CFO is conventionally an accountant from the accounting/control arm of the financial function, or direct from practice.

Why not the Treasurer as FD?

The first and most superficial reason for this discrepancy is convention. Nobody thought of me as a potential FD in my capacity as Treasurer of Unigate until they had run out of options, and I do not believe that the position has moved very far forward since. The conventional wisdom amongst headhunters, senior executives, and directors, both executive and nonexecutive is that CFOs should not only be accountants but should come immediately from an accounting background. This trend is complemented by what might be called professional momentum, the natural advance of a corporate career based on accountancy towards the FD role. The accounting profession is geared towards two parallel pinnacles, senior audit partner or CFO. Put another way, if you want to be an FD, get an accounting qualification, and convention and your profession will support you in your upward progress.

One fundamental problem is that the treasury profession ranks alongside the actuarial one in obscurity and also, deliberately perhaps, obscurantism. For many corporate executives, the physical output of asset, liability and currency management is clear, but the methods of arriving at it are totally opaque; for them it is a 'black box' profession, and some treasurers rather like to keep it that way. There is no real external understanding of the detailed aspects of the job, and of the skills and qualities needed, particularly by those who have the dominant influence on the selection of FDs: nonfinancial senior executives, the general cadre of NEDs, and, dare one say, headhunters. In this the professional treasurer is to some extent a prisoner of his position, but he also to a degree has himself to blame. It is not his fault that his natural relationships tend to be more outside the organisation, with for instance his suppliers in financial markets, than with his corporate colleagues; he may be and often is naturally gregarious but this trait tends to be saved for those with whom he deals outside the organisation. Nor is it his fault that the board rarely see the treasurer; unlike say the company secretary, the corporate lawyer or the financial controller. In short although he may be naturally transparent in the way in which he discharges the role externally, his internal perception may be the very antithesis of transparency. Education and evolution the keys to the future

But the fundamental issue is one of education, for all those involved in the selection of FDs, and at two levels: the nature of the job itself, and the suitability of a professional treasurer to fulfil it. Here serving FDs, corporate treasurers and the treasury profession itself have a key role to play. It is vital that the FD is not seen only to be a risk averse, safe pair of hands, with a control mentality-though these may be characteristicsthat he may have,' inter alia and from time to time, to exhibit: but rather forward looking, a team player, but with a critical decision making role, and a detailed understanding of risk management and financial markets. At the same time the

professional treasurer should be increasingly presented and seen to have these qualities, and more: of analysis, persuasiveness and leadership, not just in decision making but in management; of communications (Is not talking to rating agencies, for instance at least as skilled and as subtle a role as talking to analysts and the financial press? Is he not potentially at least as skilled in spin as his accountant colleagues): of gregariousness; and the personality and drive to do the job.

Some will inevitably fail the test. The nerdish, techie loner is no more typical of today's treasurer, than the desiccated numbercruncher is of today's accountant, although there are undoubtedly a number of treasurers who do have that characteristic. But the basic fact is that the corps of professional treasurers makes a rich but basically unmined seam of talent, many with the ability to bring a different dimension of skills and insight to the CFO position. How will the change occur? I would argue that the real nature and value of the role will be increasingly appreciated as a normal evolutionary process, and as the pressures of 21st century business hone the perceived requirements of every member of the top team. And treasurers can help too, by taking on far greater responsibility in increasing, if you like, the treasury literacy of their colleagues at every level - communicating in a far more proactive way what the function does and its importance to the organisation, in the context of a fresh view of the key responsibilities of the finance function, and thus their potential to discharge the latter at the highest level.

I can only conclude, more in sorrow than anger, that in not using more of the skills and talents of the corporate treasury profession, a great opportunity has been and continues to be missed. I do not deny accountants their place in the sun, nor do I underestimate their magnificent contribution to British industry. But in continuing to hand them a virtual monopoly over the FDs role, a great and potentially costly mistake may be being made. My main points then, again:

The FD's job is only marginally about accounting, and then principally about presentation and interpretation. More important is the FD's responsibility for the availability of appropriate management information at all levels in the organisation, and particularly to the board, much of which will not be based on books of account.

The key functions however are in helping to shape corporate and specifically financial strategy; board level decision making; risk management; the use of and communication with all financial markets; enhancing internal financial literacy; and setting an appropriate internal financial framework

Treasurers potentially have most of these skills, the function being embedded in financial decision making and risk management, as well as the in depth understanding of financial markets.

Whereas in the US the CFO is likely to be the Treasurer, he is likely in the UK to be drawn from an accounting background. It is a matter of convention, professional momentum, perception and education.

Treasurers are an underestimated and underutilised source of top financial talent. It is essential for the benefit of board level UK financial management, and inevitable too, that treasury management skills are seen to be an appropriate background for CFOs and that more Treasurers move up to be CFOs.

As one noted commentator, writing in Financial Director a little while ago, predicted for the year 2014: 'CAEW members will be the second largest institution represented by FTSE 100 FDs. They will be overtaken by the Association of Corporate Treasurers.'