Appointing CFOs for a rapidly changing world: the role of the Audit Committee

A recent EY dinner gave audit committee members an opportunity to hear from Mark Freebairn, Head of the Financial Management Practice at executive search firm Odgers Berndtson, who talked about the dynamic market for CFOs and the main factors that are affecting it.

If a CFO from 25 years ago could somehow do a job-swap with their modern equivalent, they would be shocked by how much has changed: the scope of the role, the nature of their interactions with the CEO and the audit committee, even the shape of the typical CFO’s career. As the business world has been revolutionised by the various forms of digital disruption collectively known as ‘Industry 4.0’, so the CFO’s role has also been transformed.

In this environment, appointing a new CFO has become ever more challenging. So the audit committee members who attended a recent EY dinner event on this topic were eager to hear the views of special guest Mark Freebairn, Head of the Financial Management Practice at executive search firm Odgers Berndtson.
Freebairn has over 20 years’ experience of appointing CFOs and other senior finance professionals, so he immediately got the attention of his audience when he said that the past six months have been as busy as he’s ever seen the market for CFOs. A boom in recruitment typically goes hand in hand with optimism about the prospects for business, yet Freebairn said the companies he talks to are generally forecasting flat to pessimistic scenarios.

Although at a loss to explain this anomaly, he suggested two possible contributing factors: a recognition among companies of the increasing value of the CFO to the organisation, which may have triggered a wish to replace existing CFOs with more suitable candidates; and the fact that CFOs are now starting to think about retirement earlier, creating more vacancies.

This busy market should be good news for Freebairn, but there is a problem:

I’m seeing a lack of appetite for taking risks in hiring individuals. Clients are demanding that every one of their criteria for a new CFO are met, and that usually includes experience as a CFO at a company of a comparable size.

He traced this back, in part at least, to the pressure placed on companies to manage investors, which leads boards to insist on a CFO with a proven track record. But there is a limited pool of such people; meanwhile, candidates are becoming frustrated that they are not being given the opportunity to step up a level. Freebairn summarised the current state of play in dramatic terms:

There are two immovable forces coming towards each other at speed: companies that want to hire CFOs with very specific skills and experience, and a pool of strong candidates who don’t meet all those criteria. Something is going to break.

Career choices
The disappointment felt by thwarted candidates is, according to Freebairn, a symptom of the fact that finance professionals today are more proactive in managing their own careers than ever before.

Some of the choices they have to make as part of that process would be familiar to their predecessors; for example, whether to work for a listed company or a private
An ever-expanding role

If the 50-something professional does decide to take a CFO job, they will find that it encompasses an ever-expanding range of responsibilities. As Freebairn said:

“Everything I would have written for a CFO job spec 20 years ago is still there today – but there’s also an extra five pages of requirements.”

This has come about because CEOs, faced with a growing workload of their own, have passed on entire areas to the CFO. Functions the CFO may be responsible for now include IT, operations, back office, facilities, procurement, supply chain, property, security, HR, insurance, risk and legal. Partly as a result of this expanding portfolio, today’s CFO needs emotional intelligence, leadership ability and, increasingly, an understanding of technology such as artificial intelligence.

Given all this, it may not be surprising that the average tenure of a CFO in a listed company is just four years. When asked his opinion of the ideal tenure, Freebairn suggested four to eight years, on the basis that a CFO will typically take four years to achieve what they initially set out to do and will then either move on or find a new challenge to occupy them for another four years at the same company.

The big question

Despite the changes in the CFO’s role and career path, organisations that need to appoint a new one face an age-old decision: whether to promote an internal candidate or hire externally. This question stimulated a lively debate that highlighted the pros and cons of both approaches. For example, one participant said:

“If you bring someone in from outside, it helps to challenge the organisation and make it change its ways.”

But this isn’t a given. Freebairn reiterated that, when organisations brief him to look for a CFO, their starting point is usually that they want someone from a listed company of the same size and in the same sector. A participant pointed out that, when they choose to bring in someone so similar to the current incumbent, “organisations just replicate themselves, and that’s a problem”.

Whichever option the hiring organisation takes, Freebairn asserted that it’s worth looking for a CFO who offers something different: “When you go outside the norm, it’s usually positive.”
A question of succession

The way in which professionals are now thinking about their careers also gives organisations the opportunity for more sophisticated succession planning. Freebairn said that they should be thinking in detail about how they engage with the talent within the finance function and giving them an oversight of how their careers might develop over the next five years or more. This means talking to the people who may be the next CFO, but also those who may be the CFO after that. Among other benefits, this engagement helps to retain talented people within the organisation.

Asking the CFO to oversee the career development of 100 people or more is not practical, though; whilst they can devolve some of that responsibility to the finance leadership, a strong HR partner is essential.

The audit committee also has an important role to play here, in mentoring and advising future finance leaders in a way other people in the company cannot. This also puts the committee in a stronger position when it comes to replacing the CFO.

A crucial aspect of succession planning is ensuring that internal candidates get the appropriate range of experience; for example, through secondments. Freebairn agreed that it’s valuable to give people a short stint – 12-18 months – in areas such as investor relations (the area of the CFO’s role most people struggle to get exposure to), internal audit, tax or treasury. But they need a commitment that they will be allowed to return to their finance role when they want; otherwise, they may get ‘stuck’ and will cease to be seen as a credible CFO candidate.

The hiring process

When it comes to appointing a new CFO, the audit committee chair should be an integral part of the interview process. Indeed, as Freebairn put it, “It’s a brave CEO who vetoes the audit committee chair’s (ACC) recommendation.”

In recent years, he observed, the ACC has become a more powerful voice in the appointment process, overtaking the Chairman in the pecking order. The ACC should also be central to the nomination committee’s discussions that shape the brief for a new CFO. They, more than any other director, should have a clear idea of which qualities are ‘must-haves’ and which are ‘nice-to-haves’.

Conclusion

At the end of the wide-ranging discussion, it was clear just how dynamic the CFO market is. Factors playing a part in this include digital disruption, the CFO’s expanding portfolio, the tendency for finance professionals to plan their careers more carefully, and the options open to them at a younger age than ever before.

Companies that understand the implications of these changes can select from a pool of high-quality, future-ready CFO candidates. The audit committee has a central role to play in this process, both in developing the finance leaders of the future and in helping to select the right CFO for their organisation.
Three questions for audit committees

1. Could you be doing more to mentor, support and challenge the up-and-coming finance professionals in your organisation, as well as your CFO?

2. Have you identified the potential CFOs of the future within the organisation – not just for the next appointment, but for the one after that?

3. When advising the nomination committee on the criteria for a CFO appointment, are you clear on which qualities, skills and experience are essential?

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