Maximizing Your CFO Network

Venture Capitalists have a powerful, albeit often under-used, tool at their disposal: the Chief Financial Officer "network" that exists among their portfolio companies. At Financial Leadership Group, clients often cite the value of FLG's 16-principal strong CFO network of highly experienced financial executives. FLG's collective 240+ years of CFO experience means that it is a very rare transaction type, accounting issue, tax problem or other company challenge that at least one, if not most, of the FLG principals have not encountered before, and thus on which we possess bona fide expertise. Even the most experienced CFO cannot have assembled this experience. Thus, the value of FLG's experience base, i.e., our ability to apply the power of multiple minds to a single problem, becomes clear. Likewise, Venture Capitalists can benefit immensely by harvesting the collective wisdom of their portfolio company CFOs through fostering the development and care of their own CFO network.

The 90/10 Principle

Starting with the hackneyed "80/20" rule, we would offer a variant with a twist: most experienced CFOs spend their days tackling 90% of issues with deftness and efficiency. This 90% problem set probably consumes just 50% of their time. It's the remaining 10% of the issues that are the thorniest and consume the remaining 50% of time, energy and resources. Yet, it is often in this small 10% universe of challenging problems that the greatest risks lie, because they require the CFO to make first-time decisions and carry out implementation in new areas where experience may be at a minimum.

Of course, not all the issues facing a company are of such draconian nature. Our idealized everyman CFO in this exercise may simply be addressing issues that merely gnaw away at the most limited resources of the start-up and young company, if not well-handled: time and money. Time wasted on even the most mundane of tasks dissipates shareholder resources and is frequently the reason other more important tasks remain unfinished. Every experienced CFO has faced a Board from which he has been assigned high-level tasks and projects, usually with quick turnaround expectations, only to find himself mired in the mud of the daily challenges that relentlessly assert themselves ("Yes, I understand we need to complete the PPM, and we are working toward that end." Translation: I have only been here a month and I just discovered that the AP clerk has been hiding the "hard to figure out" bills in her drawer for the last six months. I also just learned that that the billing clerk decided to bill "his own way" because "it's easier" and now, not surprisingly, we have a number of unpaid receivables that will need a lot of attention from me).

Even the Mundane Deserves Effective Management

It simply makes sense to ask others, even if the effort is only meant to confirm: What I think I know, I do know. When addressing mundane, run-of-the-mill issues through a CFO network, one might find a new method or procedure that improves efficiency. Why not run it through the network to give greater authority and confidence to the approach? Who knows, the participant might even find they learn something. It's no secret that the CFO's job is often a lonely one and its independent nature often leads to some isolation. New governance and independence requirements have transformed previously consultative relationships between CFOs, auditors and outside counsel into somewhat adversarial ones.

Most experienced CFOs have learned their profession through the school of "hard knocks". They have made mostly good decisions, have been lucky in some cases, and made a few bad ones. But we should also recognize, analogously to a stock trader "confusing brains for a bull market", that some past success may have been a product of the context in which it was addressed. Oftentimes, when addressing an issue in a new company in a different timeframe, some of the factors which led

to success in the past may have morphed or are absent. Hey, we CFOs are a careful lot. It doesn't hurt to ask. It's called updating your intelligence.

For example, with the myriad new outsourcing alternatives today, clearly one cannot know them all. What used to be home-brewed is now often available off the shelf at a fraction of the cost of a full time employee. Of course, learning that alternatives are available is just the first stage. Who has experience in using this vendor or another? Does anyone know three or four reliable vendors so I can bid this out? How much does it really cost? Can they really implement it in a week like they claim? And most importantly: What am I missing? What have I not thought of?

The Venture Capital CFO Network

With a portfolio of companies under management, venture capitalists are often sitting on a gold mine of experience waiting to be tapped. Yet, it is also the case that the breadth and depth of that experience varies widely within the portfolio. While some portfolio companies may have veteran CFOs (tried-and-true "rough water sailors," as we often describe ourselves at FLG), other portfolio companies may merely have a controller or, quite often, a controller that has been given the title of CFO. But even those with lesser breadth of experience may possess true depth and expertise in certain subject areas. Each of us is the product of our eclectic past and we cannot all have seen it "all". In other words, it is likely that everyone can contribute in one fashion or another and that everyone can benefit to some degree in participation.

By the way, it is not criticism of venture capitalists to say that they may on occasion have junior, less experienced people in the CFO chair. Often start-ups or young companies are best served by these lower cost alternatives, but history is also replete with over-reliance on cheaper short term alternatives at the expense of unrecognized (or unaddressed) long term costs that most often manifest themselves in the most inopportune circumstances. The lesser-experienced types can clearly benefit from the experience of the more gray-haired, but also can gain from merely interacting in their VC's CFO network on various subject matters on a regular basis with all the players. In effect, it's akin to virtual mentoring.

Making It Work in Practice

The stable of VC portfolio CFOs is a valuable asset, but like many assets it must both be mined and refined. Simply telling people to talk among themselves is not the best means of fostering the relationships upon which valuable network outcomes are achieved. The following is a prescription for garnering the most value out of your portfolio company CFO network:

1. Introduce the CFO network early and often. Consider explaining your network approach as soon as practical, perhaps even in the interview stage. Your CFOs should be comfortable with the concept and should also understand that you expect them to both use it and to contribute to it. It should be understood that it is not a weakness to ask for other perspectives, or in effect, help. Airplane pilots are taught that use of the autopilot is not a weakness, because if properly used it flies better than they can themselves. Of course, it cannot think for itself, so the value of the pilot's contribution is in bringing experience to bear and making the right decisions. Similarly, teach your CFOs to use the network tool, not out of weakness, but to allow them to confidently master the issues and manage their time effectively.

2. Make sure everyone has the tool. Provide your CFOs with a list of e-mail and other contact information for all the CFOs in your portfolio and update it regularly (if your portfolio is particularly large, consider having two or three networks, but don't simply segregate by industry; there is tremendous value to cross-pollination). Use a standard e-mail address to allow easy contact with all of the parties in the network. At FLG we have the standard "all-of-us" which distributes queries to all principals in the Firm. This not only assures that all the participants are being reached regularly (who knows in advance which party has the best

experience on a particular subject) but also fosters learning through "osmosis". By following the thread of queries and responses, not only can all contribute as appropriate, but also all parties can learn and "bank" the information for later use themselves.

3. Establish the basic rules of engagement:

   - First and foremost, inform your CFOs that the network is a tool, but it is not to be abused. It is not a CYA backstop or a crutch. They are to seek the counsel and input of the network, but in the end, they are the ones responsible for the decisions they make. No blame games are allowed.

   - Second, there are no dumb questions. Resist using the network to judge CFO abilities. If it is perceived that someone is monitoring it use or judging the quality of requests for assistance, participants will be very wary of using it.

   - Third, respect confidentiality. *Stay off the network yourself*, as your CFOs will be wary of discussing issues if they suspect you're listening in, especially as the topic relates to you.

   - Fourth, encourage frequent use of the network, but counsel users to do a little homework, too. Encourage them to use it as a "free" tool to advance their own skills and knowledge. It may even prove a helpful tool to VCs when participating in a competitive investment situation. It's just another valuable reason for the CEO to go with your firm. The best use of the network is when some thought has been given to define and understand the issue succinctly, so that time is not wasted on excessive e-mail traffic bringing the issue into proper focus.

   - Fifth, encourage the participants to give credit where credit is due. This approach, as part of human nature, encourages people to participate. When a party receives confirmation of the effectiveness of an approach offered by another CFO, encourage them to communicate its effectiveness to everyone and give credit to the source.

4. Foster use of the network. Whenever you interact with a CFO in your portfolio, ask them: Are you using the network? Follow that with: What has the network helped you address? This tactic not only encourages its use, but also assists in understanding any breakdown in communication. It also fosters more frequent use and helps create the proper atmosphere. You want everyone to participate. Yes, it takes time from their day on occasion to assist someone else, but if they don't contribute, they might not find the help when they need it. It also communicates to them that your view of their value includes their participation in the network.

5. Seek economies of scale from vendors. Encourage CFO network participants to consider taking business in volume to a select few vendors of common services or purchases. Vendors almost always positively respond to the potential of future business, usually with a price break. However, be sure not to force CFOs to use any particular vendor. There may be very good, specific reasons why your CFO may prefer one vendor over another, although the decision requires balancing those specific issues versus the possible cost savings of using the common vendor. In many broad service categories like insurance, employee benefits, banking and HR outsourcing, a single firm may be able to provide all of the essentials to many of your portfolio companies, especially for start-up and young companies who have only basic needs. However, let your CFO network determine who those firms are.

6. Face time. Consider the occasional get-together. An annual meeting, or if practical, semiannual or quarterly conferences, where all the parties are able to meet each other directly and spend some time together helps break down the veneer and build trust. At FLG, we hold teleconferences biweekly, dinners every 4-5 weeks and an annual retreat. Since we see many

problems and challenges in the many companies where we act as interim, part-time or full-time CFOs, this serves our clients and us well. This may not be practical for a VC, but it seems more than practical to have an annual (or semiannual) two day get-together (perhaps regionally in large portfolios). No one wants to waste people's time, but nothing builds relationships better than actually meeting face to face initially and, over time, renewing and rekindling that relationship by meeting face to face on some regular basis. People help people they know and trust. Participants are more likely to contribute when they are helping someone they know, rather than just sending advice off into ethereal e-mail. These meetings can also be used as educational forums; consider bringing in outsiders to spark discussions. Ask a few of the CFOs to put together short presentations on widely faced issues they have successfully addressed, including specific prescriptions for use by others. These should not be pressured off-site strategy sessions.

We at FLG have learned from practice the immense value of our own CFO network. If large enough, VCs can benefit from developing their own network as well. They work best in groups of 10-20, thus allowing for a large enough experience base within the range of a manageable number of relationships. Too large a network often leads to splinter groups or lack of interest because it's just too impersonal or unworkable. VCs might also consider benefiting from FLG's robust, highly developed CFO network as an adjunct to or extension of their own.

June 2006

Financial Leadership Group, LLC is the preeminent CFO and Board consultancy in Northern California, providing unmatched expertise to companies from start-up through $500M, on interim, part-time, project-based, and permanent assignments. FLG serves companies, boards, investors and lenders, with expertise in almost every technology sector.

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