The Association of
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Financial Professionals
in Business

# Key Principles of Effective Financial Planning and Analysis

Statement on Management Accounting

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## Executive Summary

Financial planning and analysis (FP&A) is a decision-making platform that includes reporting and analysis, planning and budgeting, forecasting, and financial modeling, and is a big part of the management accounting body of knowledge. This SMA provides the principles of effective FP&A organized into 12 principles and how to prioritize them, and details what the best-run organizations do differently with FP&A. It also discusses the role of technology, the competencies needed, how to get started, and how to "sell" the need for FP&A improvement to top management. Appendix 1 provides survey evidence supporting the 12 principles.
In general, the best-performing organizations take a more rigorous approach to FP&A:

- They have tightly integrated all the components of FP&A.
- They have merged operational and financial planning.
- They track progress of initiatives designed to improve the operational numbers just as closely as they monitor financial results.
- They hold people accountable for delivering results, including linking pay with performance.
- They translate strategy into action and make sure initiatives are properly resourced and accounted for in the budget.
- They are agile enough to make course adjustments when they identify the need.

## Introduction

Financial planning and analysis (FP&A) is a decision-making platform that includes reporting and analysis, planning and budgeting, forecasting, and financial modeling. FP&A is a big part of the management accounting body of knowledge as represented in the IMA Management Accounting Competency Framework.[1] Few processes within the purview of a CFO have so much potential to create—or destroy—business value than FP&A. How a company allocates its resources will impact its success or its failure. Even if an organization has the right strategy, if the budget does not reflect those priorities and properly fund tangible initiatives, the strategy will likely not succeed. Beyond money, if people are not actually spending their time executing the plan, it simply will not happen. Executing the plan requires that people know what the plan is and their role in executing it. While aspects of FP&A may seem routine, such as budgeting or monthly variance reporting, they are all links in the chain of the value creation process. (See Figure 1.)

Unfortunately, many companies are not achieving the full potential of their FP&A activities. A study by American Productivity & Quality Center (APQC) found that just 40% of finance executives from large organizations rated their FP&A as effective.[2] Two-thirds of the executives

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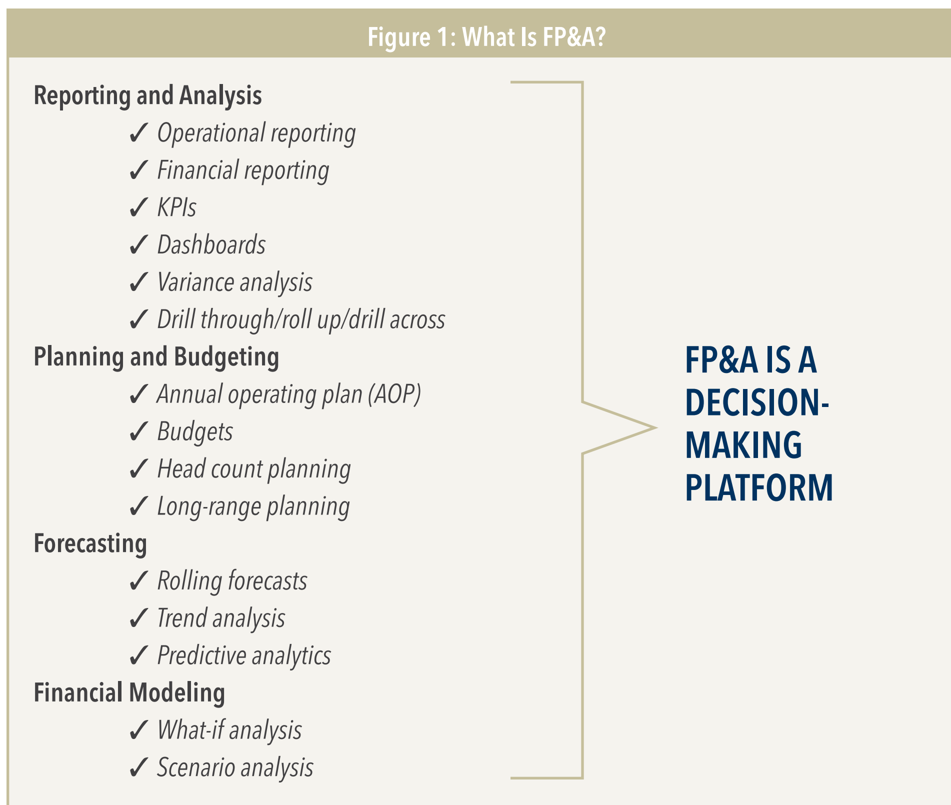
[1] IMA Management Accounting Competency Framework, April 2019, bit.ly/309rjw8.

[2] Mary Driscoll, "Why is Financial Planning and Analysis Falling Flat?" CFO.com, March 19, 2015, bit.ly/2JA8cq0.

said that their finance teams are too busy doing basic financial management duties such as periodic forecasting and actual-vs.-budget analysis. KPMG has published a report suggesting that it is the "financial" in financial planning and analysis that reduces the effectiveness of the FP&A function. Too much focus on forecasting and budgeting within a fiscal year with an emphasis on meeting short-term targets takes time away from the "planning and analysis" that is needed to help the company develop and execute its strategy.[3] Add to that the evolving socioeconomic and competitive issues that companies now face—shifting geopolitics, regulatory environment, consumers' shrinking wealth, increasing global competition, rate of business failures, and technology revolutions—FP&A teams must not only analyze the past business environment but also somehow integrate the changing global landscape into their analysis.[4]

Figure 1: What Is FP&A?




This SMA discusses principles and execution of effective FP&A practices, organized into 12 principles, and how to prioritize them. It details what the best-run organizations do differently with FP&A and also discusses the role of technology, needed competencies of the people facilitating the process, suggestions for how to get started, and ways to persuade top management of the need for FP&A improvements. Appendix 1 provides survey evidence supporting the 12 principles.

[3] David McCann, "Why you should take the 'F' out of FP&A," CFO.com, September 28, 2017, bit.ly/2M6wmdX.

[4] Kasthuri V. Henry, "The FP&A Squad: Financial Agents for Change," *Strategic Finance,* April 2012, pp. 37-43, bit.ly/2VYpymY.

## Scope

As illustrated in Figure 1, this SMA defines FP&A to include reporting and analysis, planning and budgeting, forecasting, and financial modeling. FP&A goes beyond traditional budgeting and forecasting and focuses on planning and execution. Forecasting and budgeting are certainly important, especially in communicating to the organization if it is on track to achieve its business outcomes or to raise warning flags. But forecasting results is not the same as building a plan to actually achieve them. Planning and execution are what will determine success.

This SMA is primarily addressed to financial and management accounting professionals and executives involved in any aspect of FP&A, from analyst to CEO. It is not an examination of specific forecast modeling techniques or an assessment of methodologies like zero-based budgeting. It focuses on the underlying core principles driving successful FP&A. Unfortunately, many of today's popular FP&A methodologies (such as rolling forecasts, zero-based budgeting, and beyond budgeting) usually bypass these core principles or implicitly assume they are already in place.

## Does FP&A Matter?

The value that FP&A delivers to an organization depends on how well it is performed. If done well, it has the potential to drive shareholder and stakeholder value by:

- Driving planning and execution of the strategy.
- Better management of expenses and risk analysis.
- Generating ideas for new business opportunities.
- Ensuring the optimal allocation of resources (how time and money will be invested for maximum results).

The concept of variability underlies risk management and FP&A concepts. Risk can be defined as uncertainty where at least some of the possibilities involve a loss, catastrophe, or other undesirable outcome.[5] Thus, the degree of uncertainty of each aspect of the business must be considered and may determine the expected variances between actual and budget. Expected profitability for relatively stable industries, such as equipment leasing and universities, is more predictable than for other more dynamic industries, like technology and construction. Thus, there is a greater need for strong FP&A wherever there is greater uncertainty.

On the other side, poor FP&A can lead to undesirable outcomes:

- Waste of the organization's resources (time and money).
- Reduced chance that financial and operational goals will be achieved.
- Increased likelihood that departments will act at cross purposes.
- Reduced chance that the strategy will be properly executed.
- Continued deals with lower to no profitability.

[5] Douglas W. Hubbard, *How to Measure Anything: Finding the Value of "Intangibles" in Business,* Third Edition, Wiley, Hoboken, N.J., 2014.

A controller with a poor-performing company in the media and entertainment industry summarized the consequences of poor FP&A: "Increased chance of misallocation of resources, difficulty analyzing the performance of the company due to misaligned or lack of proper parameters, and increased chance of corruption and collusion leading to undetected fraud." Those companies that have experienced the downside of poorly run FP&A are probably less likely to want to invest more time and attention to it. But the consequence can be a downward spiral. Poor FP&A leads to less time and resources invested in it, which leads to a further erosion of confidence, performance, and results. Rather than stay with the status quo, take advantage of FP&A to create value and consider the core principles, practices, and action items discussed here.

## Identifying Best- and Worst-Performing Organizations

Many of the observations, quotes, and recommendations proffered in this report are based on a research study developed by comparing the survey results of respondents working in best- and worst-performing organizations. To identify best-performing enterprises, we chose organizations that reported they (1) consistently meet or exceed the targets they set for themselves as a company/institution and (2) consistently meet or exceed the results of their competitors. It is important to note that both criteria are met, not just one or the other. Admittedly, this method of classification has limitations, but this criteria represent what virtually every CEO is trying to achieve. The results of the research study are contained in Appendix 1.

## The 12 Principles of Effective FP&A Used by Best-Run Companies

This SMA discusses and recommends 12 key principles of FP&A best practices. While any one principle, if properly implemented, will likely yield positive results, it is the way these principles reinforce each other that will more fully deliver on the promise of effective FP&A. Of course, determining an FP&A improvement road map includes tailoring the key principles to meet the unique current circumstances and state of FP&A in the organization.

Many organizations may say, "We sort of do these principles today." But that is not really the test. The real test is how well the principle has been deployed and with what type of rigor and discipline. Beyond that, the bigger question to answer is: How integrated are the principles as a whole system? Table 1 presents a summary of the 12 key principles of effective FP&A.

| Table 1: Summary of the 12 Key Principles of Effective FP&A | | |
|---|---|---|
| **Fundamental Principles – Building a Firm Foundation** | **Accountability Principles – Building a Culture of Accountability** | **Advanced Principles – Taking FP&A to the Next Level** |
| **P1:** Develop a strategic long-range plan and identify specific initiatives and projects/plans to execute it. | **P6:** Cascade both financial and nonfinancial operational targets down the organization to more specific targets. | **P9:** Identify what drives business success and develop key performance indicators (KPIs) for those drivers. |
| **P2:** Identify resources needed to implement projects/plans and put them in the budget. | **P7:** Hold people accountable for delivering *financial* results and link to financial incentives. | **P10:** Establish long-term and shorter-term targets for the KPIs. |
| **P3:** Understand how operational plans will drive financial results and monitor progress of those plans. | **P8:** Hold people accountable for delivering *operational* results and link to financial incentives. | **P11:** Develop initiatives and operational projects to achieve KPI targets |
| **P4:** Quickly identify the business reasons behind plan-to-actual financial variances. | | **P12:** Monitor results of KPIs and link to financial incentives. |
| **P5:** Make course adjustments when falling behind on financial or operational goals. | | |

## Fundamental Principles – Building a Firm Foundation

The first five principles are designed to provide a firm foundation for FP&A. They encompass translating strategy into actionable plans, making sure those plans are properly resourced, consciously linking operational performance and financial results, quickly identifying variances and the reasons behind them, and making course adjustments. These principles, if properly executed and adhered to, should get an organization started down the path of effective FP&A practices.

### Principle 1: Develop a strategic long-range plan and identify specific initiatives and projects/plans to execute it.

Every company or institution has its own way of creating a strategy. A complete discussion of determining strategic priorities and execution is beyond the scope of this SMA.[6] Strategic planning should be anchored to the organization's mission, vision, and core values. It typically begins with a scan of the external environment using a framework such as Porter's Five Forces, followed by a SWOT (strengths, weaknesses, opportunities, threats) analysis. A gap analysis is performed with respect to where an organization wants to go compared to its current position. Based on these analyses, organizational goals are set and initiatives are put in place. We will begin at the point where an effective strategy has been developed. If an organization is not at that point, it should work on that first.

[6] For an excellent reference on strategy planning and competitive analysis, see *HBR's 10 Must Reads on Strategy*, Harvard Business Review Press, Boston, Mass., 2011; a great way to develop these skills is IMA's CSCA® (Certified in Strategy and Competitive Analysis) Learning Series and certification, available at www.imanet.org/csca-credential.

Whatever the strategy, the best-run companies:

- Have a long-range plan with a differentiation strategy (such as a cost leader).
- Identify specific initiatives to achieve the strategic plan (for example, continuous improvement initiative, reducing scrap and defective products to reduce waste, and launching a new product.
- Translate those specific initiatives into shorter-term operational projects that can be executed over the coming fiscal year (for example, streamlining the delivery process, Six Sigma, and root cause analysis).

This principle makes a difference in an organization's success. A customer support professional from a small "best-performing" chemical facility in the Middle East commented, "Effective FP&A can help management to measure the profitability of transactions through any level of projects, per customer, per sector, per product, or per line of production, to find more than one alternative to improve the profitability." On the other side, an internal auditor from a "worst-performing" media and entertainment company said, "FP&A should be more connected in terms of dealing with different divisions/departments and more involved and aggressive in terms of communicating the financial impacts of each operational project, especially if the plan is misaligned from the beginning."

### Principle 2: Identify resources needed to implement projects/plans and put them in the budget.

Many well-conceived projects that could in fact drive the desired outcomes of the plan do not come to fruition. The most common reason is insufficient resources, including both money and people's time. This happens when those people developing or leading these projects fail to identify the specific resources needed to do the project. Instead they say, "We will just do it."

Another common pitfall is that the budgeting process is often disconnected from the strategic planning process. Management may develop great plans during a retreat and "commit" to a project. But it is during the budget process when real decisions about the allocation of resources actually get made. The best-performing organizations:

- Identify the resources (money and people) needed to execute the operational projects that will drive results (such as investment in new technology to improve the processing time, consulting fees related to design and implementation, and staff time required).
- Incorporate those resource requirements into the budget.

A respondent from a best-performing manufacturing company commented, "[FP&A] effectively motivates resource management applications, putting both financial and human resources in the right place and in the right amounts." Another said, "Effective FP&A can guide the efficient usage of limited resources in the best way possible. [It] can control the behavior of approving parties to have a mind-set of evaluate and analyze rather than approve only."

**Principle 3: Understand how operational plans will drive financial results and monitor progress of those plans.**
The best-performing organizations know that operational decisions and actions will impact their financial results. What is different is that these organizations make those connections explicit: They clearly understand how their operational projects will impact their financial results, and they monitor the progress of those projects.

Typically, there is a monthly review process that compares financial performance to planned performance. But that monthly review process should also include an update on key projects to make sure they are on schedule. If a project is delayed, find the business explanation for the delay. An FP&A professional in a small food and beverage "best-performing" company in China mentioned how strong FP&A "provides sound support for business decisions, timely measuring of output making it easy to adjust, and the ability to estimate project impact before it is carried out."

**Principle 4: Quickly identify the business reasons behind plan-to-actual financial variances.**
While variances are often seen as something to avoid, they can be extraordinarily helpful in understanding what's happening in the business. Comparisons, however, rarely tell the whole story. Without a real business plan, all the financial analyst can say is something like, "We have a -2% variance in revenue because we did not sell as much as we forecasted." There's very little business insight offered in that statement.

In contrast, the best-performing companies quickly and confidently:

- Identify plan-to-actual financial variances.
- Identify the business reasons for plan-to-actual variances.

For example, suppose there was a real plan to grow revenues by 8%, but a key marketing campaign launch date was delayed and a promotional event did not draw the response rate anticipated. Best-performing companies delve much deeper into those issues. What caused the delay in the marketing campaign? If it was an advertising agency issue, maybe the company needs a new one? If the root cause was that the marketing person leading the campaign left the company on short notice, perhaps there is a succession planning issue. The analysis can reveal real business issues and facilitate continuous improvement in the enterprise. One respondent commented, "Diving deep into the numbers gives you a detailed picture of the company. Mostly FP&A helps me understand where we currently stand. The environment is highly dynamic, however, so your plans are dated soon after accomplished."

Again, the frequency of variance analysis depends on the degree of controllability and variability of the results. Investing in systems that support this type of analysis will provide many benefits, even for smaller firms.

**Principle 5: Make course adjustments when falling behind on financial or operational goals.**
Rather than just adjusting their expectations downward, the best-performing firms are agile. They are not just focused on financial progress but also on the progress being made on

operational goals as well. They are proactive about getting back on track. On the other hand, FP&A reporting at the worst-performing firms is often just financial reports showing variances. A respondent from a worst-performing company said, "FP&A needs to disseminate not only accurate information but 'actionable' information—meaning, not only provide quantitative data but qualitative as well. Moreover, the reports are based on historical data with no qualitative or quantitative information besides the 'slap on the wrist' if you are going over your budget. They do not understand there is a difference between being proactive vs. reactive."

An agile company does more than just forecasting. Planning for success is what drives value; merely forecasting success does not. Of course, forecasting is still a vital function that serves as an early warning system and should provide an unbiased projection. Gaps between the forecast and the plan should prompt a dialogue regarding the underlying business issues causing the gaps.

Keep in mind that forecasts should not focus exclusively on the financials. The progress of the initiatives and project plans should also be assessed. This type of analysis requires an understanding of the business and the initiatives, which goes above and beyond the understanding of financial models and may require additional training and development for FP&A staff.

## Accountability Principles – Building a Culture of Accountability

The next three principles are designed to help foster a culture of accountability. As good as any plan is, it takes people to implement it. People do care if the organization achieves its goals, but they care even more about achieving targets they own, especially if there is economic incentive to do so. In this section, we discuss how to foster a culture of accountability.

### Principle 6: Cascade both financial and nonfinancial operational targets down the organization to more specific targets.

The best-performing organizations integrate financial and operational planning. This extends to the cascading of goals down through the organization. Higher-level goals (such as growing sales by 1,000 units) are broken down into incrementally smaller goals and potentially further broken down to an individual level (so the 1,000-unit sales growth cascades down into regions, districts, and salespeople). Cascading of goals is a critical element of building accountability. While some companies cascade financial targets, the best-performing organizations cascade operational targets as well.

The study found that public companies are more likely to cascade financial goals from high to low organizational levels than privately held companies or nonprofits. One reason could be that public firms have an especially high need to reach financial goals for stockholders and analysts. On the other hand, they are not more likely to cascade operational targets than private companies or nonprofits.

**Principle 7: Hold people accountable for delivering *financial* results and link to financial incentives.**

The best-performing organizations translate strategy into actionable initiatives and then further refine specific projects. They hold people accountable for delivering financial targets but go a step further by linking those results to financial incentives. So "being accountable" in these organizations takes on deeper and more personal meaning than simply being called out for failing to deliver on a commitment. More specifically, the best-performing companies:

- Clearly identify those people who are responsible for delivering the financial targets in the annual plan or budget.
- Hold these people clearly accountable for delivering on those financial targets.
- Provide those same people with financial incentives that are tied to achieving their financial targets.

One issue to address is how to handle events that affect financial performance but are out of the control of those accountable for meeting the targets. To remedy this, make controllability a key consideration for performance appraisals and financial incentives. For example, do not hold the sales director responsible for returns based on quality failures. Another example is not to over-allocate executive overhead to departments for performance evaluations. It is important to select appropriate performance measures. In general, good individual performance measures should:

- Align employees' goals with that of the organization's key success drivers.
- Yield relevant information about the actions or decisions of the employee (i.e., high controllability and low interdependency).
- Be easy to understand, measure, and communicate.
- Be available on a timely basis.

Keep in mind there are no perfect performance measures. There are always trade-offs. Ideally, it is optimal to tie incentives to goals that are specific, measurable, actionable, relevant, and time-bound (SMART).

Further, "accountability" should mean responsibility for leading the way to reaching financial targets. Those given this responsibility should be in the best position to enable the organization to reach the goals and, if they are not achieved, be most knowledgeable about what happened and why. Companies that use accountability to blame and penalize those who do not achieve their financial goals are creating an environment of distrust and responsibility-shirking, and encouraging finger-pointing. It is critical that incentives avoid "gamesmanship," or motivating managers to optimize their own performance at the expense of the organization. Best performers foster a culture where those accountable feel free to report what really happened so the organization can learn from the experience and reach its goals in the future.

Generally, incentives should be based on both financial and nonfinancial targets and include both individual and company-wide metrics. Also, targets could be adjusted to the relative performance of other companies in the industry.

### Principle 8: Hold people accountable for delivering *operational* results and link to financial incentives.

This principle goes back to the theme of operational and financial plans being tightly integrated in the best-performing organizations. Accountability is not just about hitting the financial targets, it is also about achieving the operational targets that ultimately drive the financials. Because operational changes drive financial performance, the best-performing organizations:

- Identify people who are responsible for delivering specific operational targets (for example, give the head of manufacturing responsibility for delivering a 5% productivity improvement goal).
- Hold them accountable for delivering the operational targets (for example, assign milestone delivery dates to key members of a project team to review progress on their goals).
- Provide them with financial incentives tied to achieving their operational targets (such as meeting operational targets is included in the bonus calculations).

Companies can use a strategy map to ensure operational goals are clearly linked to financial outcomes in a cause-and-effect linkage. Metrics should include both leading and lagging indicators of performance that ultimately lead to desired financial outcomes.

## Advanced Principles – Taking FP&A to the Next Level

The last four principles focus on business drivers and integrating them into FP&A. An organization's strategy should focus on moving the key drivers in the right direction. To do that, an organization must have a firm understanding of what drives success in the business, define measures for those drivers, and establish targets for them. At that point, strategy becomes "practical" in the sense that it is focused on those things that will drive its success.

### Principle 9: Identify what drives business success and develop key performance indicators (KPIs) for those drivers.

The best-performing organizations codify or formalize what drives success in their business with associated measures so they become widely shared and understood. More specifically, these companies:

- Identify what drives success in their business.
- Develop clear measures for those drivers.

For example, in the high-tech industry, innovation is considered a driver of success. The best-performing organizations take that driver and develop a clear measure for it, such as the percentage of sales coming from products introduced in the past two years. These measures are often referred to as key performance indicators (KPIs). KPIs should be tracked not for the sole purpose of having something to put on a dashboard or scorecard, but because they have been determined to drive success. The best-performing organizations also have specific actionable plans for achieving success on those KPIs.

Each industry has unique KPIs that drive success in that industry. For example, in the hotel industry, customer loyalty, occupancy, and achievable room rates are frequently cited as drivers of success. The question then becomes how to measure those drivers. Customer loyalty can be measured by an index used to assess to what extent a customer would recommend that hotel. Combining the occupancy rate and average room rate determines revenue per available room, another common way to assess the hotel's success.

**Principle 10: Establish long-term and short-term targets for the KPIs.**

As discussed in the previous section, the best-run organizations do a better job of identifying and measuring what drives their success. Instead of loosely configuring aspects of FP&A, the best-performing organizations tightly integrate them. To leverage their KPIs, these companies:

- Establish long-term targets for KPIs.
- Establish short-term (usually annual) targets for those measures.

In doing so, they develop a path between where they are now and where they want to be. Further, they put those drivers to work by establishing both long-term and short-term targets for those drivers. They have a vision of where they want to be on those measures in the long term but also "make it real" by establishing short-term targets.

**Principle 11: Develop initiatives and operational projects to achieve KPI targets.**

Once best-performing organizations have defined their drivers and set targets, they:

- Establish strategic initiatives to achieve the long-term targets.
- Identify operational projects and plans to achieve the short-term targets.

This underscores the theme that the likelihood of achieving a goal increases with clear plans, rather than simply wishful thinking. It is critical to both develop strategic initiatives to achieve organizations' long-term targets and establish actionable operational tactics to achieve related shorter-term targets.

**Principle 12: Monitor results of KPIs and link to financial incentives.**

Lastly, to help build accountability, organizations should:

- Monitor results of KPIs for progress toward their documented goals.
- Tie incentives to achieving the goals.

To avoid gaming the system and motivating managers to optimize their own performance at the expense of the organization, incentives should be based on both financial and nonfinancial targets and include both individual and company-wide metrics. Unfortunately, compared to the other principles, relatively fewer organizations tie incentives to achieving goals. Again, it is optimal to tie incentives to SMART goals.

# Support for the 12 Principles

Appendix 1 provides demographics and results of the study and shows support for the value of the 12 principles. We found the best-performing companies are much more likely to be following the principles and related practices compared to middle- and worst-performing groups. The best performers are following more of the specific practices on average than the other groups: best (9.1), middle (7.4), and worst (5.1). The practices that most distinguished the best performers from the rest are:

- Variances: quickly and confidently identify plan-to-actual financial variances (Principle 4).
- Responsibility: clearly identify people who are responsible for delivering financial targets in our annual plan (Principle 7).
- Accountability: hold these people clearly accountable for delivering the financial targets (Principle 7).
- Operational: provide financial incentives to those who have responsibility for delivering operational targets (Principle 8).
- Targets: establish long-term targets for KPIs (Principle 10).
- Initiatives: develop strategic initiatives to achieve the KPI long-term targets (Principle 11).

# The People Side of FP&A

People manage the FP&A process, and, in many respects, the process is only as good as the people managing it. Key FP&A skills and capabilities include:

- Understanding the underlying business.
- Building effective working relationships outside of finance and accounting.
- Understanding the specific area or department they are supporting.
- Communication skills.
- Technical skills (for example, accounting, working with spreadsheets, and so on).

## Understanding the Underlying Business

If FP&A staff are to become trusted advisors and partners in the business, they need to have a firm understanding of the underlying business. They need to know how the business is run, the major influences or levers of the business, who the customers are and how they buy, and the strengths and weaknesses of competitors. For example, one of the authors was hired as a new cost analyst at a factory making expensive food-processing equipment. One of his assignments was to track the costs of each project and estimate the final profitability. Although each project was specifically designed by engineers, there were always parts of the manufacturing process that could take more (or less) time than planned or parts of the product that were more (or less) expensive than planned. It was imperative that he understand the manufacturing process and employees to know what questions to ask.

Crucial to the business-partner role of FP&A employees is a solid knowledge of the business and its operations. This is how they can earn trust and build credibility. That trust and credibility are shattered when employees are perceived as having only superficial knowledge and, conversely, built up when they demonstrate in ways small and large that they are students of the business.

As we have seen in the 12 principles outlined in this report, the best-performing organizations fuse together the operations and the financials of the business. That means it is not enough for FP&A employees to understand the financial side; they need to know the operational side as well if they are ever going to be able to connect the two. A respondent from a worst-performing company lamented, "FP&A needs to better understand the underlying business; moreover, they need to understand the cost drivers of the development process and try to come up with solutions instead of delivering problems."

## Building Effective Working Relationships Outside of Finance and Accounting

To successfully build working relationships, it is essential to establish credibility. The people on the front lines know better than anyone else what is going on in the business, and it is the FP&A professionals' job to learn and communicate that. They will be able to offer a real business explanation and insight if they have built good working relationships and are connected to and aware of what is going on around the company.

It is not enough to know that profit came in less than expected because cost of goods sold was higher than planned. That is an accounting answer. Instead, discussions with the production manager might reveal the company faced a stock-out of a key material that had to be air-shipped at considerable cost to meet customer demand. Further business analysis may reveal that the demand forecast was off. To help safeguard that this does not happen again, the analyst might meet with the sales manager and determine this is another reason to implement the new sales and operational planning process proposed the previous month and currently under review. All of these findings are more probable through good working relationships with those outside of the finance department.

## Understanding the Specific Area or Department They Are Supporting

Besides understanding the business, FP&A professionals also should understand the issues and language of the departments they support. For instance, the challenges of the logistics department are quite different than those of marketing or human resources. Each functional area needs FP&A professionals to understand its unique challenges and how it runs its side of the business.

Many of the more successful FP&A professionals will take practical steps to get to know the department they serve, such as attending weekly staff meetings or facilitating monthly reviews of plan vs. actual results. That way when the plan (or forecast) cycle starts up again, they are already part of the team.

## Communication Skills

FP&A professionals need to be able to communicate effectively with the rest of the organization. Consider the monthly management reporting package that provides variance analyses to help executives understand what happened in the business and why. Ask yourself: How clear are the variance explanations? Could anyone in the organization read it and understand what is being communicated? Consider all the exhibits, reports, and templates used in the annual plan or monthly forecast. Do people outside of the finance department understand them and what they are used for? Are there actual business decisions being made based on these reports? If not, is that an indication of their lack of utility? To find out, ask the report recipients.

Verbal communication also happens while gathering facts. For example, to find an explanation for a financial variance, asking the right questions in the right way and avoiding ambiguity and forcing clarity can make all the difference in getting the best explanation. Likewise, using verbal skills to clarify an information request can avoid a lot of misunderstanding and rework. FP&A employees should take responsibility for communication and ensure all sides understand what is being asked and why.

FP&A staff members often make presentations during the planning process, as well as during monthly reviews, comparing actual results to the forecasts for the period. How those presenters express this information can either help executives grasp the issues quickly or leave them confused. One common complaint is that an FP&A staff member will display a chart crowded with data in small font and begin by saying "As you can clearly see…" The presenter has not adequately provided context for what is on the slide nor explained what is on it. They have jumped right in, assuming the audience knows much more about what they are looking at than they actually do.

## Technical Skills

The number of technical skills that all management accounting professionals are expected to have keeps increasing. Excel, financial modeling, forecasting and budgeting, variance analysis, cost and profitability management, data analytics, return on investment (ROI) and net present value (NPV) development and analyses, accounting, and reporting are just the start. Other emerging technology skills include process automation, artificial intelligence (AI), business analytics, data security and storage, and data visualization.

Another emerging technical skill is project planning. This includes knowing how to develop a project charter (defining the goals, scope, approach, team structure, and so on) and a project plan (like a Gantt chart) with activities, tasks, resource estimates, milestones, and dates. A respondent from a best-performing company said, "Effective FP&A can ensure coordination of initiatives, projects, and programs." While FP&A professionals might not be leading the project, they may be tasked with managing it from a reporting and control perspective. Project management skills include being able to update the project plan as necessary, manage the progress reporting process, and facilitate meetings.

Beyond traditional financial modeling, the ability to develop a business case is another skill that is increasingly required. A business case includes how the investment would advance the strategy of the organization, the resource requirements, the estimated implementation timeline, alternatives considered and why the team chose a certain path, and how to package and present the plan.

### Key Competencies

In the study, we compared the best-performing organizations against the worst-performing in six key FP&A skill areas. We found the following key competencies that most distinguished those in the best-performing group from the other groups (in order):

- Building effective working relationships outside of finance/accounting.
- Understanding the specific area/department they are supporting.
- Written communication.
- Verbal communication.

A study participant from a large best-performing financial services company in the U.K. described their people with these competencies: "The business partners in our organization are the key to everything—they know how to complete the annual planning requirements for marketing, they can get letters of intent through for mergers and acquisitions, they understand the systems and processes and people necessary for human resources, they do the revenue walks (modeling) to calculate growth, etc."

For more on specific key competencies of FP&A professionals, see the "Strategy, Planning & Performance" domain section in IMA's Management Accounting Competency Framework.

## Selling the Value of Improved FP&A Practices to Top Management

Convincing top management of the value of improving FP&A can be more difficult than expected. It is difficult to measure the benefits of most administrative initiatives, such as improving the FP&A process. Most leaders consider the benefits of "intangibles" to be too difficult—if not impossible—to measure, so they do not measure them, which leads to little to no improvement in the FP&A process. Like other more tangible operational improvements, they want to see the ROI first.

So how do we measure the expected value for investing in FP&A? If we define measurement as "a quantitatively expressed reduction of uncertainty based on one or more observations," virtually anything can be measured.[7] By defining specifically what an improvement in FP&A would look like, we can estimate the operational and even financial benefits. Here are four steps to do so.

[7] Much of this section is based on two sources: (1) Douglas W. Hubbard's book *How to Measure Anything: Finding the Value of 'Intangibles' in Business* and (2) "Measuring the ROI on FP&A," a presentation given by Gavin Black, Bill Sayer, and Amber Bowden, at the Association for Financial Professionals (AFP) Annual Conference, October 27, 2013, Las Vegas, Nev.

**Step 1. Decide to measure the benefits of better FP&A.**

There are several potential direct and indirect benefits of improved FP&A. *Direct* benefits, in which something should noticeably improve, include (1) identifying improvement projects, (2) determining if planned improvements were accomplished, (3) identifying process strengths and weaknesses, and (4) establishing priorities for future investment. *Indirect* benefits can include increasing communication between the FP&A team and the rest of the organization, better understanding of the potential value of the FP&A function, and more effective FP&A outputs.

To measure the benefits of better FP&A, identify likely benefits, who will benefit, and from whom you need buy-in. In other words, make a case for the improvement with supporting evidence. You will need to estimate the cost in people's time and money, as well as what current practices could be reduced. Be aware from the start of expected challenges and how to address them. Common challenges include lack of support and resources, time constraints, measuring the value of "intangible" benefits, and defining the scope of the measurement. If all this sounds doable, proceed to the next step.

**Step 2. Define the measures and collect data.**

Defining the measures means agreeing on what improved FP&A would look like and how it can be observed (for example, improved speed, cost, quality, satisfaction, motivation, influence, and engagement). A good place to start is talking with all the key players and asking them to identify ways that better FP&A could help optimize the decision-making process. Talk about current and past management decisions and how the various FP&A principles discussed in this SMA could make a difference.

In his book, *How to Measure Anything*, Douglas W. Hubbard recommends that before we decide how to measure something, we first must clarify the measurement problem by asking the following questions.[8]

a. *What is the decision this measurement is supposed to support?*

Before deciding what to measure, the first step should be to identify the problem and decision for which you intend to use the measurement. For example, if you want to measure employee engagement, first decide why you want to measure it. Is the purpose to help improve quality of work or change hiring and development practices? Or if you want to measure the value of a proposed FP&A improvement initiative, is the purpose to decide whether to implement a new FP&A system or to improve the staff's data analytics skills?

b. *What specifically would the thing being measured look like as it relates to the decision being asked?*

The key to measuring something that seems hard (or impossible) to measure is to ask what it would look like specifically. For example, if your decision purpose is to measure employee engagement to help decide whether to improve hiring and development practices, what would be observable signs of improved employee engagement? Potential answers could be less

[8] Hubbard, 2014.

absenteeism, more ideas generated, fewer defects, or other specific observable actions relating to engagement and strategic or operational goals.

If the purpose is to measure the value of a proposed FP&A improvement initiative to improve the staff's data analytics skills, potential measures might be the before and after impact levels of FP&A reports, process improvements identified, forecast accuracy, and new business opportunities identified.

Unfortunately, the contributions of the FP&A team are often not readily apparent. They are more commonly noticed when there is a mistake or lack of information rather than when they are helpful and accurate. But to measure the impact of a potential FP&A improvement initiative, we need to be specific about what we would be looking for. What does improved FP&A look like? Here are some examples of observable items.

**Accurate and timely financial reporting:**

- Impact of FP&A reports for the monthly executive business review meeting.
- Timely internal and corporate parent close.
- Effective compensation support.

**Process improvement analysis:**

- New ways to improve efficiencies and cost savings.
- Identifying waste, fraud, and abuse.
- Terminating expired or ineffective contracts and expenses.
- More or better metric reporting.

**Business support and analysis:**

- New business development opportunities identified.
- Improved forecast accuracy.
- Better cash management to achieve net positive interest cash flows.

Once you agree on what better FP&A would look like and how to observe it, you next need to identify how to collect the data. Potential sources of data include the various information systems, human resources, interviews, minutes of meetings, focus groups, surveys, and so forth. It may also take a different mind-set among the key players. Unfortunately, not every measure has readily available data such as units produced. But if you have defined what you are looking for, then observing that thing becomes a measure. For example, how often have we observed the FP&A team identifying new business development opportunities? To measure the impact of FP&A reports for the monthly executive business review meeting, the observation may be answering the question, "Are we using FP&A analysis more in our strategic decisions?" Or "Are more/deeper questions being directed toward the FP&A team?"

*c. What is the value of additional information?*

Information adds value to the extent that it reduces uncertainties in decision making. Knowing the value of the information helps us to not only identify what to measure but how to measure it. Sometimes just a few observations can reduce the level of uncertainty significantly, and collecting

additional observations may have diminishing benefits. There is also the cost-benefit side of collecting additional measurement information. If the decision outcome relates to deciding whether to invest in an opportunity that could net $1 million per year, it would probably make sense to spend $10,000 to collect the additional information to help reduce the potential risk of making a poor decision. On the other hand, if the potential outcome is $10,000, then it would probably not make sense and a simpler way should be found to reduce the risk of a poor decision.

**Step 3. Calculate the net value of improved FP&A.**

Calculating the value of intangibles like the potential value of an FP&A investment is easier said than done. An important contributor in this area was Enrico Fermi.[9] The Fermi method means to decompose the measurements into specific questions leading to a quantitative decision model. We break up the estimated costs/benefits into things we can observe, such as "Is it more than X?" The monetary values for each benefit or cost by year can themselves be decomposed further into more variables.

Applying the Fermi method to calculate the value of improved FP&A analysis, such as an efficiency improvement, could be done by multiplying the number of people working in the improved process, the cost of each person per year, the percentage of time spent on some unproductive activity, and the percentage of that unproductive time that was eliminated. Appendix 2 provides an example of estimating the net value and ROI for an FP&A improvement initiative. Remember that the first year for most initiatives includes up-front investments that lower the net value for the first year. Thus, the analysis should extend beyond the first year depending on the time frame of the expected benefits. To get the needed buy-in from the key players on the estimated benefits and costs, the analysis should be logical and the estimated benefits should clearly exceed the expected costs.

**Step 4. Refine and evaluate the measurement process.**

Estimating the costs and benefits of FP&A improvement initiatives can improve over time through periodic reviews, satisfaction with the process, post-project audits, and continued working together with other departments and upper management to refine the estimation process. Estimating skills can be improved through calibration techniques.[10] If estimates of benefits are shown to be reliable over time, top management is more likely to sign off on future improvement initiatives.

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[9] Fermi (1901-1954) was a physicist who won the Nobel Prize in Physics in 1938 for his work on nuclear energy. He was also a master estimator with a knack for finding intuitive ways of measuring things that seemed too complex to measure.

[10] Hubbard, 2014.

## The Role of Technology in FP&A

FP&A is a decision-making platform, and technology needs to enable this platform. It should meet reporting and business intelligence needs, as well as planning and budgeting, in an integrated system. One respondent in a best-performing company said, "Due to the real-time, interconnectivity of our systems, we know exactly where we are at all times." In the study, we found the best-performing organizations are slightly more likely to use dedicated FP&A tools than the worst-performing organizations. And those firms primarily using an FP&A application are significantly more likely to identify plan-to-actual financial variances and the reasons for them than those firms primarily using Excel. The rationale behind this could be that the FP&A process on the whole is more rigorous and operationally focused in the best-performing organizations. Technology that enables the process would help free up FP&A professionals to focus on those value-added activities.

Table 2 provides some guidelines to help identify technology enablers required to support the 12 principles.

| Table 2: Guidelines to Help Identify FP&A Technology Enablers |
|---|
| **1.** System should integrate with or natively include project management software (such as MS Project). |
| **2.** System should accommodate both long-term and short-term planning. |
| **3.** System should support the use of nonfinancial or statistical/operational data. |
| **4.** System should support the use of narratives to capture the business reasons behind key variances. |
| **5.** The system should support scenario planning and what-if analysis to model key potential changes in the business. |
| **6.** The system should support predictive analytics to anticipate key changes. |
| **7.** The system should make it easy to "zip or unzip" goals at any level. |
| **8.** The system should capture both financial and operational goals. |
| **9.** The system should integrate with human resources and performance management systems to capture individual goals, track achievement, and calculate rewards. |
| **10.** The system should integrate with or provide dashboard capabilities. |

## Where to Start

The easiest place to start is with an assessment of the current state of FP&A in your organization. Appendix 3 provides the same survey questions used in our study of FP&A practices. It will not only help you assess your company's FP&A practices, it will also provide guidance for making improvements to the process. For comparison, Figure A2 reports the specific practices within the 12 principles that most differentiated the best performers from the rest in the study.

In addition to the assessment, below are some specific action items to consider for getting started:

- Redesign the planning calendar to better synchronize strategic planning with the annual operating plan.
- Facilitate a workshop for executives to document "what drives success in this business" and follow up with proposed measures for those drivers.
- Take preliminary steps to document the linkages between those drivers and the business's financial model.
- Establish annual operating plan objectives by identifying outcomes and timing.
- For the first year, "start small." Incorporate just two or three significant projects into your annual operating plan/budget and use these to build up experience and confidence in linking operations to financial outcomes and tracking the project progress.
- Establish a real follow-up mechanism (at least quarterly, if not monthly) to evaluate progress answering the question, "Are we doing and achieving what we set out to do?"
- Work with the human resources department to understand the current variable compensation structure and open up a dialog regarding incorporating relevant principles.
- Download the IMA Management Accounting Competency Framework and use it as a starting point to understand what a competency model is and how to apply it to your FP&A organization.
- Institute a rotation program to bring operational people into FP&A (and vice versa).
- Train staff in basic project management (for example, how to develop a project plan with activities, tasks, and milestones).
- Provide training for finance staff with FP&A responsibility in building effective working relationships with those outside the finance department.
- Develop or join an FP&A principles roundtable group to share and learn from others' experience.

## Conclusions

The question "Does FP&A add value?" is a little like asking "Does marketing add value?" Marketing itself is neither useful nor a waste of time: It is how well marketing is done and how effective it is that matters. Likewise, the value FP&A delivers to an organization depends on how well it is performed.

In this SMA, we have discussed 12 principles of effective FP&A supported in a related study. The best-performing organizations tend to take a much more rigorous approach to FP&A:

- They integrate all the components of FP&A.
- They merge operational and financial planning and have a deep understanding of how operational metrics drive their financial results.
- They track progress of initiatives designed to move the operational numbers in the right direction just as closely as they monitor financial results.
- They hold people accountable for delivering results and link pay with performance.
- They translate strategy into action and make sure initiatives are properly resourced and accounted for in the budget.
- They tie incentives to SMART goals.
- They make course adjustments when they identify the need to get back on track.

If nothing else, FP&A professionals can benefit greatly by honing their relationship skills. Building effective working relationships outside of the finance department—and understanding the underlying business and the departments they are supporting—will go a long way in becoming business partners. Further, the burden is on FP&A staff to learn how to communicate effectively with the rest of the organization. Without it, decision makers will go elsewhere to get the information and analysis they need. Ask those outside the finance department if they understand the purpose of the exhibits, reports, and templates used in the annual plan. If so, do they use them in managing the business? If not, find out why.

FP&A has the potential to provide valuable decision support for the many decisions made during the planning process and as the strategic plan is executed. But it takes investing time to get to know the specific areas it supports, develop relationships, and build trust and rapport to provide business analysis specific enough to make a difference.

# Appendix 1: Survey Demographics and Results

### How We Conducted the Study

In April 2017, IMA® (Institute of Management Accountants) sent survey invitations to more than 25,000 global financial executives and managers with experience in their company's FP&A practices. We received 839 responses, a 3.3% response rate. We eliminated 139 incomplete responses, leaving 700 usable responses from a wide variety of industries. Both large and small companies were represented, with 20% having more than $1 billion in revenue, 26% between $100 million and $1 billion in revenue, and 54% below $100 million in revenue. Almost half had more than 500 employees and 19% had more than 5,000.

### Survey Demographics

The survey covered both for-profit companies (87.6%) and not-for-profit institutions (12.4%). The majority of the not-for-profit institutions were colleges and universities (42%), 501(c)(3) (20%), and nongovernmental organizations (13%). Roughly two-thirds of respondents were in finance/accounting/FP&A, with the rest from other areas including executive management (9%) and manufacturing/operations (7%).

In terms of industries, manufacturing was well represented, as was retail, financial services, and technology (see Table A1).

**Table A1: Industries**

| | No. | Percent |
|---|---|---|
| Manufacturing: *Aerospace, Automotive, all other Manufacturing* | 110 | 16% |
| Retail: *Apparel, Consumer Packaged Goods (CPG), Wholesale/Retail* | 41 | 6% |
| Financial Services: *Banking, Insurance, Brokerage, Investment* | 67 | 10% |
| Technology: *Biotech, Computer, Software, Technology, Telecom* | 72 | 10% |
| Construction and Real Estate | 41 | 6% |
| Utilities and Transportation | 68 | 10% |
| Business Services: *Advertising, Consulting, Legal, Publishing* | 51 | 7% |
| Healthcare: *Facilities, Payers, Providers, Supporting Products, and Services* | 48 | 7% |
| Other | 116 | 17% |
| No response | 86 | 12% |
| Total | 700 | 100% |

### Survey Results

We defined the best-performing enterprises as those that reported they (1) consistently meet or exceed the targets they set for themselves as a company/institution, and (2) consistently meet or exceed the results of their competitors. Of the 700 usable responses, 367 were from organizations that met the criteria for "best performers." We defined the worst-performing firms as those organizations that reported just the opposite. They both (1) consistently fail to meet or exceed the targets they set for themselves as a company/institution, and (2) consistently fail to meet or exceed the results of their competitors. There were 138 organizations that fell into the "worst performers" category. The remaining 195 were categorized as "middle performers."

Table A2 shows that best performers overall outpace the other groups on revenue growth rates, profitability, and market share.

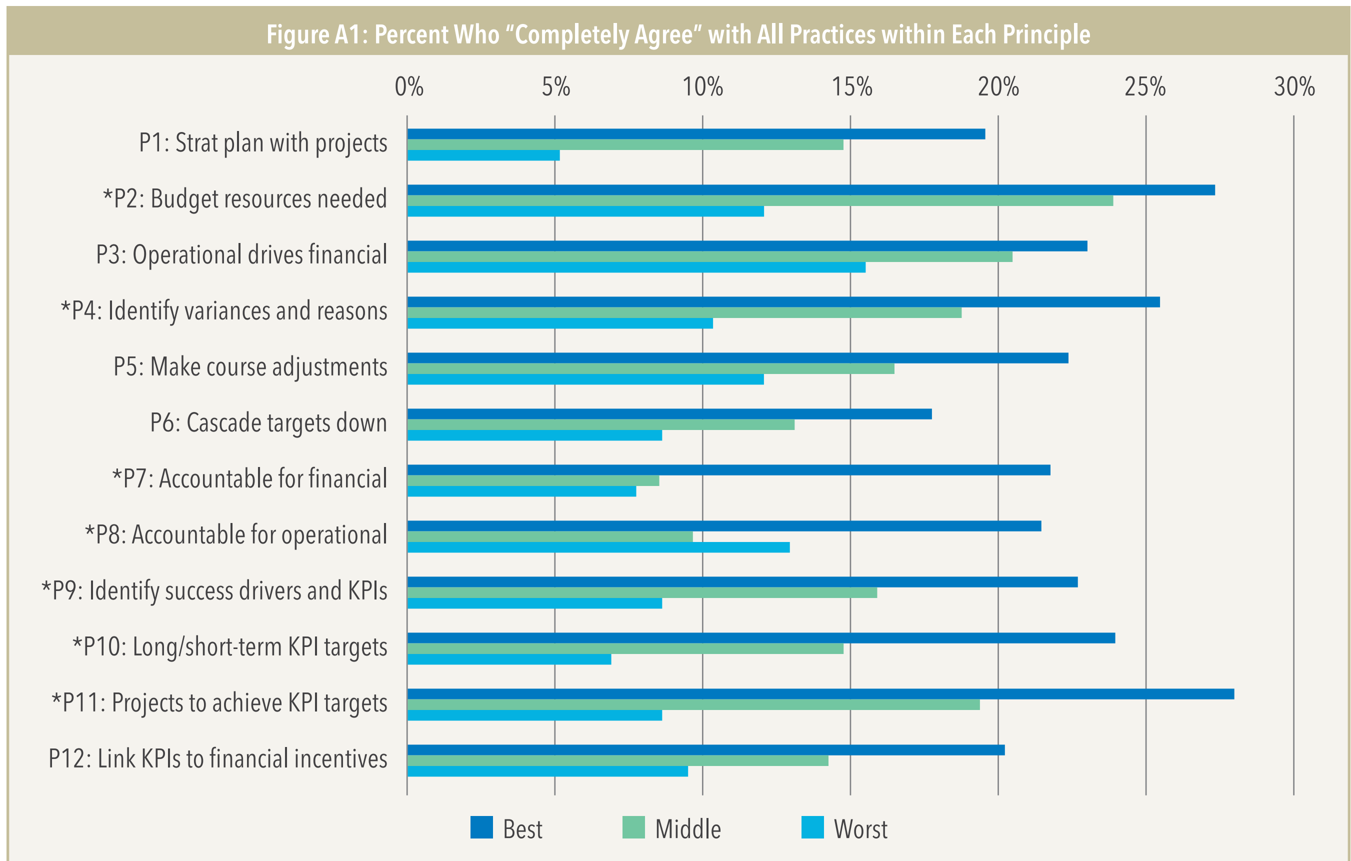
**Table A2: Growth Rates, Profitability, and Market Share for Best vs. Worst Performers**

| | Best Performers | Middle Performers | Worst Performers | All Companies |
|---|---|---|---|---|
| **Total number of respondents** | 367 | 195 | 138 | 700 |
| **Over the past five years** | | | | |
| Average revenue growth rate | 10.5% | 9.5% | 7.5% | 9.6% |
| Revenue growing faster than competitors | 94.1% | 90.1% | 71.7% | 88.5% |
| Profitability better than competitors | 79.0% | 56.9% | 36.8% | 64.3% |
| Market share better than competitors | 72.5% | 53.3% | 35.9% | 59.8% |
| Realizes the full potential of FP&A (1-100; mean) | 65.6 | 58.2 | 46.5 | 59.7 |

Medium- to large-sized companies were more likely to recognize the value of FP&A. Further, those companies primarily using FP&A software rather than spreadsheets were also more likely to recognize this value of FP&A.

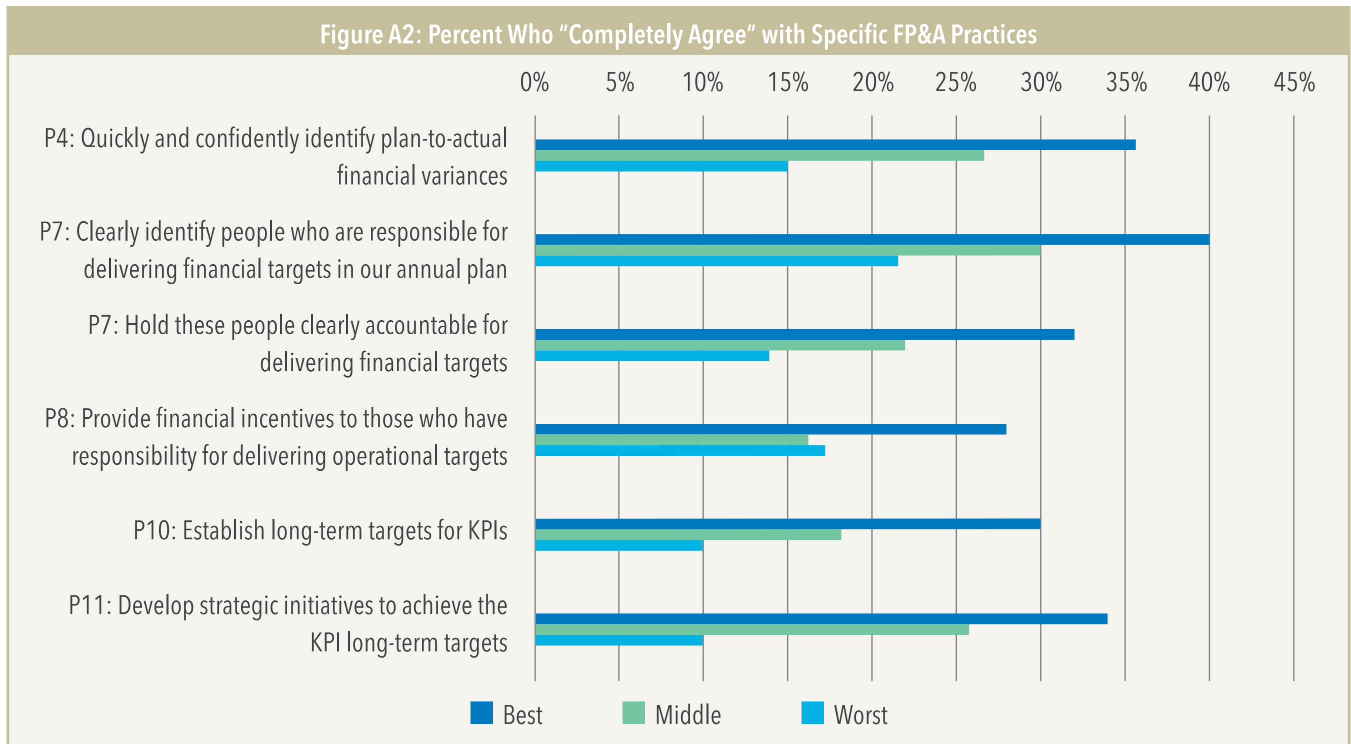
### Results of Survey Study on the 12 Principles of Effective FP&A

Figure A1 compares the percentage of those who "completely agree" from best, middle, and worst performers for each specific practice within each of the 12 principles. As shown, the best performers more often implement each principle. The principles that most distinguish the best performers from the rest are P2, P4, P7, P8, P9, P10, and P11. Based on Chi Square tests, all differences between the three performance groups are statistically significant at $p< 5\%$ except for P3.




*Note: Survey respondents were asked to what degree they agreed or disagreed with each statement: 1=completely disagree; 2=somewhat disagree; 3=somewhat agree; 4=completely agree. Each question for each principle can be found in Appendix 3.*

Figure A2 compares the percentage of those who "completely agree" from best, middle, and worst performers for specific practices within the 12 principles that most differentiate the best performers from the rest. The key differentiator practices were identified based on univariate Chi Square tests and multivariate binary logistical regression analysis comparing best performers against worst performers and best performers against middle performers for all practices. All differences between best- and worst-performing firms are statistically significant at $p < 5\%$ in the Chi Square tests.



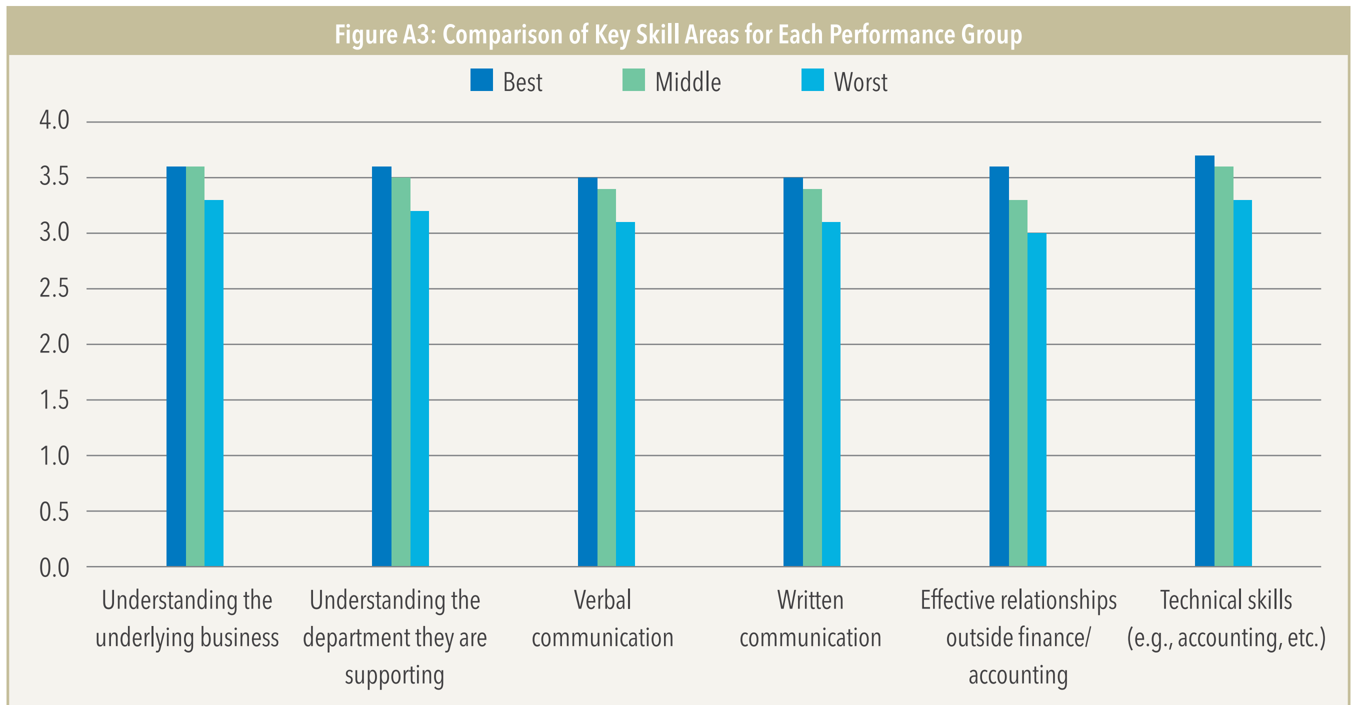

*Note: Survey respondents were asked to what degree they agreed or disagreed with each statement: 1=completely disagree; 2=somewhat disagree; 3=somewhat agree; 4=completely agree. Each question for each principle can be found in Appendix 3.*

Table A3 compares the number of practices that the respondents from best, middle, and worst performers answered "completely agree" to when asked if they followed each practice and suggests the more practices followed, the better the FP&A outcomes. The differences among the groups are statistically significant at $p < 5\%$ in ANOVA analysis.

**Table A3: Number of Practices for Each Performance Group**

| Performance Group | Mean | Standard Deviation | Median | Range |
|---|---|---|---|---|
| Best performers | 9.1 | 9.83 | 7 | 0-29 |
| Middle performers | 7.4 | 8.31 | 4 | 0-28 |
| Worst performers | 5.1 | 6.87 | 7 | 0-26 |
| All companies | 7.8 | 9.02 | 4 | 0-29 |

*Note: Survey respondents were asked to what degree they agreed or disagreed with each statement: 1=completely disagree; 2=somewhat disagree; 3=somewhat agree; 4=completely agree. Each question for each principle can be found in Appendix 3.*




*Survey Question: In most organizations, a "business partner" from FP&A (or finance/accounting or other area) will work with the rest of the organization to develop their plans and forecasts. On a scale of 1 to 5 (with 5 being the highest or best score), how would you rate their ability in the following areas? Differences among the groups are all statistically significant ($p<.005$).*

# Appendix 2: Developing an ROI for an FP&A Improvement Initiative

Let's assume an FP&A improvement initiative calls for providing financial incentives for the operations team tied to increasing output accompanied by implementing Lean production practices. It is estimated that nonproductive time will be reduced and productive time increased by at least 6% and as much as 20% leading to more output. The analysis calculates values using different levels of increased production time (low 6%, medium 12%, and high 20%). An estimated value and ROI for this initiative might be computed as follows:

| | | | |
|---|---|---|---|
| **EXPECTED BENEFITS:** | | | |
| **Operational incentives and Lean practices:** | | | |
| A. Increased production time % | **6%** | **12%** | **20%** |
| B. Current productive time per employee (month) | 150 | 150 | 150 |
| C. Number of employees | 125 | 125 | 125 |
| D. Total current productive hours per month (B x C) | 18,750 | 18,750 | 18,750 |
| E. Additional productive hours (A x D) | 1,125 | 2,250 | 3,750 |
| F. Contribution margin per unit of additional output | $24 | $24 | $24 |
| G. Average production hours per unit | 12 | 12 | 12 |
| H. CM per hour (F ÷ G) | $2.00 | $2.00 | $2.00 |
| I. Expected value per month (E x H) | $2,250 | $4,500 | $7,500 |
| **J. Expected value per year (I x 12)** | **$27,000** | **$54,000** | **$90,000** |
| **EXPECTED COSTS:** | | | |
| **Cost of Incentives:** | | | |
| K. Total number of eligible employees | 20 | 20 | 20 |
| L. Average annual salary/wages per employee | $60,000 | $60,000 | $60,000 |
| M. Average % incentive pay per employee | 2% | 4% | 6% |
| **N. Expected incentive payout (K x L x M)** | **$24,000** | **$48,000** | **$72,000** |
| **Initial cost of implementing Lean practices:** | | | |
| O. Training and consultants | $10,000 | $10,000 | $10,000 |
| P. Increased maintenance costs | $3,000 | $3,000 | $3,000 |
| Q. New layout of operations area | $12,000 | $12,000 | $12,000 |
| **R. Total initial cost of implementing Lean (O + P + Q)** | **$25,000** | **$25,000** | **$25,000** |
| **S. Total Expected costs (N + R)** | **$49,000** | **$73,000** | **$97,000** |
| **Expected ROI for operational incentives and Lean practices:** | | | |
| Expected value per year (J) | $27,000 | $54,000 | $90,000 |
| Total expected costs (S) | $49,000 | $73,000 | $97,000 |
| ROI-Initial Year (J - S) ÷ S | -45% | -26% | -7% |
| ROI-Second Year (J - N) ÷ N | 13% | 13% | 25% |

# Appendix 3: Assessment of FP&A Practices

**Overall Questions:**

1. What is the potential value of financial planning and analysis (FP&A)? (Check all that apply)
    a. Effective FP&A can drive shareholder value (or business value if privately held).
    b. Effective FP&A can drive execution of the strategy.
    c. Effective FP&A can provide the mechanisms to ensure the financial and operational goals of the organization are achieved.
    d. Effective FP&A can build organizational awareness of the strategy and each department's role in achieving it.
    e. Effective FP&A can ensure the optimal allocation of resources.
    f. Effective FP&A can ensure coordination of initiatives, projects, and programs.

2. To what degree does your organization realize the full potential of FP&A? Please enter a number between 0 and 100 (with 0 representing none at all and 100 fully realizing the potential).

3. If FP&A is done poorly or not effectively, what are the negative consequences?
    a. Waste of the organization's resources (time and money).
    b. Reduced chance that financial and operational goals will be achieved.
    c. Increased likelihood that departments will act at cross purposes.
    d. Reduced chance that the strategy will be properly executed.

4. How often do you see evidence of these negative consequences occurring in your company/institution?

5. While every department is somehow involved in the FP&A process, what department in your company/institution would you say really manages the FP&A process (for example, which is most responsible for facilitating/orchestrating the process)?

6. 6a. Does your company or institution primarily use Excel for most FP&A activities or a dedicated FP&A application?
    6b. If you use an FP&A application, please name it here:

**Principles Questions**

Would you agree or disagree with the following statements?

**Principle 1:** ***Develop a strategic long-range plan and identify specific initiatives and projects/plans to execute it.***

1.1 We have a strategic/long-range plan.
1.2 We identify specific initiatives to achieve the strategy/long-range plan.
1.3 We translate those strategic initiatives into shorter-term operational projects/plans.

**Principle 2:** ***Identify resources needed to implement projects/plans and put them in the budget.***

2.1 We identify the resources (money and people) necessary to execute the operational projects/plans.
2.2 We incorporate those resource requirements into our financial plan/budget.

**Principle 3:** ***Understand how operational plans will drive financial results and monitor progress of those plans.***

3.1 We have a clear understanding of how our operational projects/plans will impact our financial results.
3.2 We monitor the progress of our operational projects/plans as we progress through the year.
3.3 We have a clear understanding of how progress, or lack of progress, of our operating projects/plans impact our actual financial results.

**Principle 4:** ***Quickly identify the business reasons behind plan-to-actual financial variances.***

4.1 We quickly and confidently identify plan-to-actual financial variances.
4.2 We can quickly and confidently identify the business reasons for plan-to-actual variances.

**Principle 5:** ***Make course adjustments when falling behind on financial or operational goals.***

5.1 We monitor the progress of our financial goals as we progress through the year.
5.2 When we fall behind on our financial goals, we make course adjustments to get back on track.
5.3 When we fall behind on our operational goals, we make course adjustments to get back on track.

**Principle 6:** ***Cascade both financial and nonfinancial operational targets down the organization to more specific targets.***

6.1 Financial targets clearly cascade down the organization (from higher-level targets to more specific area/departmental/individual targets).
6.2 Nonfinancial operational targets clearly cascade down the organization (from higher-level targets to more specific area/departmental/individual targets).

**Principle 7:** ***Hold people accountable for delivering*** **financial** ***results and link to financial incentives.***

7.1 We clearly identify people who are responsible for delivering financial targets in our annual plan.

7.2 We hold these people clearly accountable for delivering the financial targets.

7.3 Those same people have financial incentives tied to achieving their financial targets.

**Principle 8:** ***Hold people accountable for delivering*** **operational** ***results and link to financial incentives.***

8.1 We clearly identify people who are responsible for delivering specific operational targets.

8.2 We hold these people clearly accountable for delivering the operational targets.

8.3 Those people have financial incentives tied to achieving their operational targets.

**Principle 9:** ***Identify what drives business success and develop key performance indicators (KPIs) for those drivers.***

9.1 We have a clear sense of what drives success in our business (for example, "Innovation is a key driver of success in our business").

9.2 We have clear measures for those drivers (for example, "We measure innovation as the percentage of sales coming from products introduced in the past two years").

**Principle 10:** ***Establish long-term and short-term targets for the KPIs.***

10.1 We establish long-term targets for those measures.

10.2 We establish shorter-term or annual targets for those measures.

**Principle 11:** ***Develop initiatives and operational projects to achieve KPI targets.***

11.1 We develop strategic initiatives to achieve the long-term targets.

11.2 We establish operational projects and plans to achieve the nearer-term targets.

**Principle 12:** ***Monitor results of KPIs and link to financial incentives.***

12.1 We monitor actual results of those measures.

12.2 We tie achievement of targets to incentive compensation.

**Skills Questions**

Q16. In most organizations, a "business partner" from FP&A (or finance/accounting or other area) will work with the rest of the organization to develop their plans and forecasts. On a scale of 1 to 5 (with 5 being the highest or best score) how would you rate their ability in the following areas:

a. Understanding the underlying business. ________

b. Understanding the specific area/department they are supporting. ________

c. Verbal communication. ________

d. Written communication. ________

e. Building effective working relationships outside of finance/accounting. ________

f. Technical skills (such as accounting and working with spreadsheets). ________

## Further Reading

Rand Heer, "How agile is your planning? Find out by measuring the ROI of your planning software," *Strategic Finance*, April 2012, pp. 45-50, bit.ly/2VGuA2F.

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*HBR's 10 Must Reads on Strategy*, Harvard Business Review Press, Boston, Mass., 2011.

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IMA Management Accounting Competencies, www.imanet.org/career-resources/management-accounting-competencies.

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Mary Driscoll, "Why is Financial Planning and Analysis Falling Flat?" CFO.com, March 19, 2015, ww2.cfo.com/accounting-tax/2015/03/financial-planning-analysis-falling-flat.

David McCann, "Why you should take the 'F' out of FP&A," CFO.com, September 28, 2017, ww2.cfo.com/business-planning/2017/09/take-f-fpa.

Kasthuri V. Henry, "The FP&A Squad: Financial Agents for Change," *Strategic Finance*, April 2012, pp. 37-43, bit.ly/2VYpymY.

Lawrence Serven, "Is Forecasting Destroying Your Planning Process?" *Strategic Finance*, July 2017, pp. 34-39, bit.ly/2X7TFFi.

Lawrence B. MacGregor Serven, *Value Planning: The New Approach to Building Value Every Day*, Wiley, Hoboken, N.J., 2001.

| GLOSSARY OF TERMS | |
|---|---|
| Activity-based budgeting | An approach to budgeting in which a company uses an understanding of its activities and driver relationships to quantitatively estimate workload and resource requirements as part of an ongoing business plan. Budgets show the types, number of, and cost of resources that activities are expected to consume based on forecasted workloads. The budget is part of an organization's activity-based planning process and can be used in evaluating its success in setting and pursuing strategic goals. |
| Annual operating plan (AOP) | Defines what will be achieved in the upcoming fiscal year and how. |
| Budget | The expense side of the annual operating plan. A statement of planned or expected revenues, expenses, assets, and liabilities. A budget provides guidelines for future operations and appraisal of performance. Also called profit plan. |
| Business planning | Understanding where the business is today, where you want it to go, determining how to get there, monitoring progress along the way, and making course adjustments as necessary. |
| Continuous forecasting | Forecasting on an as-needed basis. |
| Driver-based forecasting | Applying statistical measures (such as occupancy rate) in financial models to produce a projection of future results. |
| Forecasting | A prediction of future events or conditions, usually based on a financial model. |
| Initiative | Usually a longer-term program that is undertaken to meet established goals and to improve the business. |
| Key performance indicator (KPI) | Measurable value that demonstrates how effectively a company is achieving its most important strategic objectives. |
| Project | Planned set of interrelated tasks to be executed over a fixed period and within certain cost and other limitations. |
| Project charter | Defines the goals and objectives, team structure, roles and responsibilities, timetable, scope, and resource requirements. |

| GLOSSARY OF TERMS | |
|---|---|
| Project plan | Defines the activities and tasks that will be executed over a specific time period. |
| Rolling forecast | Updating a forecast on a set schedule and looking out the same number of periods each time (such as a rolling 18-month forecast). |
| Variance analysis | Investigation of the causes of the variances between actual costs and standard or budgeted cost (or actual to forecast results) with explanations for key differences. |
| Zero-based budgeting | A budget that is developed by analyzing the amount of each element of cost that should be incurred under a variety of assumptions for the budget period and then selecting what appears to be the optimum "decision packages" from these alternatives. The first package is the amount developed "from scratch," that is, the amount required for the lowest possible level of activity. Conceptually, zero-based budgeting resets all budgets to $0 at the start of the budget process, with managers providing a business case for every dollar they plan on spending in the upcoming year. |