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CFOs Fulfilling Operations Roles ‘Admirably’

By Stephanie Forshee August 12, 2019

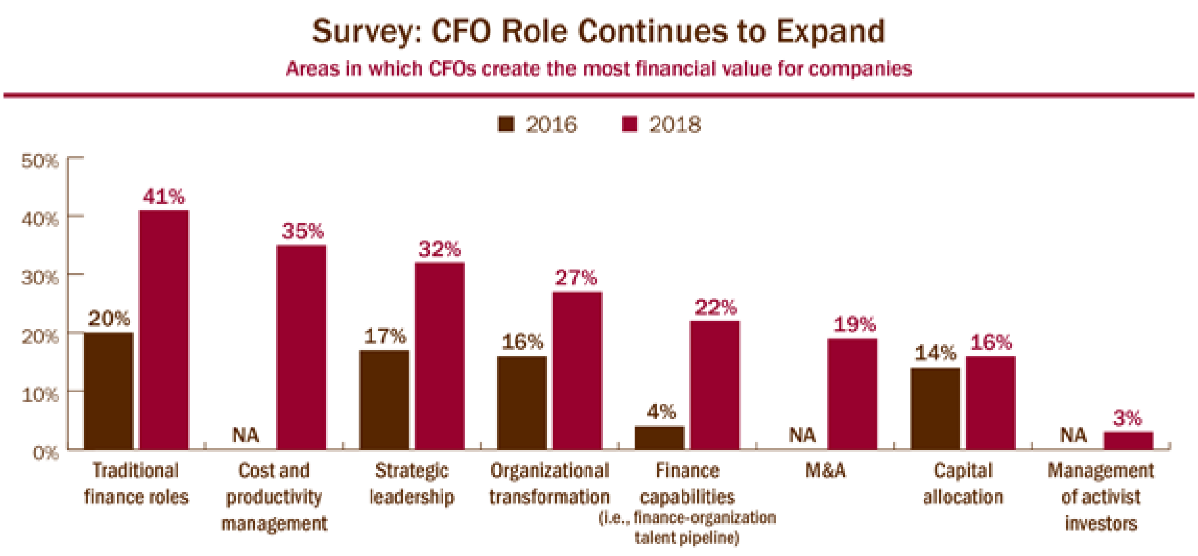
It’s no wonder board directors with an eye on succession planning may feel conflicted as to whether the finance and operations functions of their businesses belong together. Companies have faced scrutiny for the arrangement from investors and analysts.

In a report last month, for example, Michael Kors parent company **Capri Holdings** was criticized by research firm **Management CV** for its chief financial officer’s “overly broad job description, including COO.”

However, a new report by the **American Accounting Association** has found that when CFOs take on chief operating officer tasks, there is no negative impact on the company’s performance. The study’s authors believe this conclusion “informs boards of directors by providing evidence that CFOs who are given operational control can effectively perform both roles if the CFO/COO executive possesses the appropriate skill set.”

While the outcome of adopting such a hybrid role is dependent on the individual company or executive, boards should be asking whether it’s a smart idea to combine the two roles and what kinds of risks they could assume, experts say.

“It depends on the specific situation, but we see that a CFO in general is often a lead internal CEO succession candidate,” says **Matteo Tonello**, managing director at **The Conference Board**, who was not involved in the study. “The skill set and leadership experience can only be augmented by the direct responsibility that the person has assumed of operations.”



Note: Figures represent the percentage of 526 respondents in 2016 and 436 in 2018.
Source: McKinsey & Co.

What the Numbers Show

In the association's study, published in the **Journal of Management Accounting Research**, titled "Are CFOs Effective Operators? An Empirical Analysis of CFO/COO Duality," researchers from the **University of Alabama** and the **University of Oklahoma** analyzed 3,500 companies (438 with CFO/COO roles combined and 3,100 separate) over the span of a 16-year period and concluded from a select sample that "managers from a financial background can fulfill operational roles admirably."

"Learning that CFOs who take control of operations appear to do a reasonable job with operating decisions should be encouraging news for proponents of broad-based training among financial experts and to those accountants wishing to move beyond historic 'number counting' stereotypes," the study reads.

As for the quality of the financial reporting, the study found that discretionary accruals were more volatile for companies with a hybrid CFO and COO, but that accruals at those companies "are relatively more predictive of future cash flows "compared to accruals of firms where there was not a dual role. "We interpret this finding as an indicator that financial reporting quality improves in the presence of CFO/COO duality," the study found.

The study's authors are not oblivious to the fact that the hybrid role has its fair share of skeptics. The research accounts for three common concerns, including that "traditional COO operating responsibilities are incongruent with the stereotypical perception of CFOs as accounting/finance specialists."

Among the other concerns cited is the argument that "the added responsibilities and duties of a unified CFO/COO might overburden the executive relative to [the] traditional CFO role," and the study notes, "The combination of operational objectives (i.e., COO incentives) with financial reporting may create the incentive to opportunistically use accruals in an effort to meet operational targets."

TCB's Tonello agrees there are drawbacks to combining the CFO and COO function. "Senior executives have fiduciary responsibilities and, specifically, a duty of loyalty to the organization. As such, each of them acts as a check and balance of the actions and authority of other peer members of the C-suite. When two major functional roles are combined, there is always a risk of lowering those safeguards."

He suggests that boards carefully evaluate "the advantages resulting from the combination of roles against the vulnerabilities."

The University of Alabama's **Steve Buchheit**, one of the study's authors, tells *Agenda* that with regard to the hybrid role, he "wouldn't tell any board member it was always fine to do this, but it's probably pretty obvious they've demonstrated an ability beyond what your normal CFO has."

In addition to the study's showing that the hybrid role is not detrimental oftentimes executives with a dual CFO and COO title have landed in the CEO role. This was the case for **Occidental Petroleum**'s **Steve Chazen**, **PepsiCo** 's **Indra Nooyi**, **Cheesecake Factory**'s **Jerry Deitchle** and **Freeport-McMoran**'s **Richard Adkerson**, among others.

That could be an important consideration for boards focused on succession planning, particularly because anytime a company starts a CFO search, "it's almost certain the board wants a candidate that would be a strong CEO successor," says **Jason Waterman**, senior client partner at **Korn Ferry**.

It even occurred at his own company, Korn Ferry, when **Gary Burnison** assumed the CEO role in 2007; he joined the company in 2002 as CFO and the following year added on the COO title. Burnison, who also serves on the board, was unavailable for comment.

Waterman, who heads the firm's CFO practice, explains that taking on COO responsibilities can be a suitable path for CFOs with a desire to become the CEO, as they are "more involved in broader leadership responsibilities."

Meanwhile, boards should be mindful that even though it might make sense to "give operations to the CFO to help him or her prepare for the CEO role," Waterman says the "biggest drawback would be on succession issues. If you take operations and put it under finance, you've lost the path for other operations executives, such as chief supply chain officer, to move up."

In the case of Capri Holdings, parent to Michael Kors, Versace and Jimmy Choo, research firm Management CV criticized the luxury retail company for this very reason. Its July 8 report says, "Given the size and scope of the CEO's growth plans, we don't like that CFO **Tom Edwards** holds both the CFO and COO roles."

Management CV took issue with the fact that Edwards, a former finance exec with **Wyndham Hotel Group** and **Kraft Foods**, came from outside the retail or luxury sectors.

"We think that his SVP and Chief Operations and Transformation Officer **Cathy Marie Robinson** should simply be the firm's COO," Management CV states in its research report, citing Robinson's "good logistics and supply chain background" in previous roles at **Walmart**, **Toys R Us** and **Smart & Final**.

Neither Capri Holdings nor Edwards responded for comment for this article.

As for comparing CFOs with the dual COO title to those without, the study found the dual execs were more than twice as likely to be at least 62 years old, more than one third more likely to have been a CFO at a previous employer, and almost seven times more likely to be company board members.