Measuring the ROI on FP&A

Gavin Block, Market Vice President
Kforce Professional Staffing

Bill Sayer, FP&A Manager
Crump Life Insurance Services

Amber Bowden, CPA, CTP
Sr Analyst
Lockheed Martin
Investments made into the FP&A teams over past two years

- Added Staff: 48.7%
- Continuing Education: 51.3%
- Technology: 51.3%
- None: 23.1%
- Other: 7.7%
Organizations that have added headcount to their FP&A teams in 2013

- Yes: 56.4%
- No: 43.6%
Most Important Contributions of FP&A

- Forecasting: 41.0%
- Strategic Planning: 41.0%
- Budgeting: 10.3%
- Other: 7.7%
ROI of Your FP&A Department

- Why Evaluate ROI on FP&A?

- The Process

- Challenges
### Why Evaluate ROI on FP&A?

#### Direct Benefits of an ROI Study

<table>
<thead>
<tr>
<th>Improve project quality</th>
<th>Determine if objectives accomplished</th>
<th>Identify process strengths &amp; weaknesses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Enable a cost-benefit analysis</td>
<td>Determine appropriate solution</td>
<td>Establish priorities for future investment</td>
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</table>
Why Evaluate ROI on FP&A?

Indirect Benefits of an ROI Study

- Increase engagement within FP&A team
- Improve customer service
- Fewer complaints, reduced conflict
- Better understanding of FP&A function
- Better “seat at the table”
- Create developmental objectives
The Process

Make Your Decision

Define the Data

Calculate a Value

Measure Costs

Confidence Measure of ROI

Refinement & Ongoing Evaluation

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The Process: Decision

So you’ve decided to measure the ROI of your FP&A function…

How far do you want to go?
The Process: Decision

- Get a reaction to the idea/project and look for perceived value
- Do You Need Buy-In and From Who?
- What Will This Cost in Time & Money?
Challenges

- Lack of Support & Resources
- Time Constraints
- Valuing Soft Data
- Valuing Intangibles
- Defining Scope
The Process

Make Your Decision → Define the Data → Calculate a Value → Measure Costs → Confidence Measure of ROI → Refinement & Ongoing Evaluation
The Process: Define Data

- Job descriptions
- Department descriptions/flowcharts
- Task lists/calendars

Agree on what your FP&A function contributes based on your primary responsibilities.
The Process: Define Data

Assign a value to your primary responsibilities

- Assumptions/Estimates
- Historical trends
- Calculated time savings
- Calculations
- Sensitivity analysis
- Scenario analysis

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The Process: Define Data

Categories of Data to Consider:

- "Soft" data
- Quality (failure rates, waste etc.)
- Costs (variances, cost of sales)
- Output (units, accounts, clicks etc.)
- Time (cycle time, downtime, overtime)
The Process: Collect Data

Challenge: “Soft Data” – Attitude, Motivation, Morale, Satisfaction
  ➢ Communication breakdowns
  ➢ Employee satisfaction
  ➢ Employee engagement
  ➢ Employee development
  ➢ Customer satisfaction

Potential Sources of “Soft Data”
  ➢ Surveys & Interviews
  ➢ Focus groups
  ➢ Job descriptions or performance contracts
Define Data: What Are The Contributions Of Our FP&A Team?

- Assumptions
- Financial Services
- 10 person team
  - VP
  - Manager
  - 4 SFA’s
  - 4 FA’s
- Important – The method is the thing. Agree or disagree on our numbers.
Define Data: What Are The Contributions Of Our FP&A Team?

- **Primary goals for our team:**
  - **Accurate & Timely Financial Reporting**
    - Monthly executive business review meeting reporting
    - Internal and corporate parent close
    - Compensation support
  - **Business Support & Analysis**
    - Annual operating & strategic plan leadership
    - Variance analysis
    - Forecasting
    - Business Development
    - Improved Efficiencies

- **Secondary goals:**
  - Support of other finance teams as needed
  - Internal process improvement
  - Documentation
The Process

1. Make Your Decision
2. Define the Data
3. Calculate a Value
4. Measure Costs
5. Confidence Measure of ROI
6. Refinement & Ongoing Evaluation

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Calculate a Value: Things You Will Need

- Team goals and job descriptions
- Summary financial statements (P&L)
- FP&A team cost information (could be confidential)
- A few cooperative but credible internal sources to talk to
- A famous dead Italian physicist
Calculate The Value Of The Team Contributions

But How Do You Calculate?

Enrico Fermi, 1901-1954
• Physicist
• Nuclear energy pioneer
• Nobel Laureate
• Also…master estimator
Calculate The Value Of The Team Contributions

- The Fermi method of estimation:
  - Using clearly identified, reasonable assumptions, you can make a justifiable estimate about the quantity of something that seems impossible to know.

- The application of multiple nonbiased factors will likely be more accurate than an outright guess

- We’ve all been in this situation before

- Ask Fermi questions: Is it more than X? Less than Y?
Calculate The Value Of The Team Contributions

How can we use this?

– For your FP&A team’s contributions that cannot be directly measured or otherwise estimated, apply the Fermi method to arrive at a justifiable number.
Calculate The Value Of The Team Contributions

1. **Monthly executive business review meeting reporting**
   - ✔ 227 page package of reports
   - ✔ Estimated FP&A team time committed to process:
     - Creation of reports: estimate per page per month including production, quality review, process maintenance, analysis & summarization.
     - Total time = 151.5 hours (18.8 person-days)
   - ✔ FP&A review with executive team:
     - Monthly meeting w/business leaders
     - Key leaders have their own meetings
     - Total time = 28.5 hours
   - ✔ Total FP&A time = 180 hours.
Calculate The Value Of The Team Contributions

2. Expense & Revenue Impact
   ✓ Total non-compensation expenses reviewed during meetings: $10MM.
     • What are we worth? How much more would we spend if we did not report & analyze our expenses?
     • Fermi it: 5%? 3%?
     • Estimated impact of meetings on expense management: 4% ($400,000 monthly)
   ✓ Total revenue reviewed during meetings: $15M
     • Estimated impact of meetings on revenue creation: 2% ($300,000 monthly)
Calculate The Value Of The Team Contributions

3. **Business Support & Analysis**
   - Annual operating & strategic plan leadership
     - Annual value of expenses in plan: $175MM
     - Estimated value of FP&A impact on expense planning (no enterprise planning solution): 5% or $8.75MM
   - Variance analysis: included in monthly review estimate
   - Forecasting: included in monthly review estimate
   - Business Development
     - Total annual value of signed new business worked by FP&A team: $10MM
     - Importance of FP&A team on business development signing: pricing, pro forma planning, value prop development: 20% ($2MM)

- Improved Efficiencies
  - Waste, fraud & abuse identified: $100,000
  - Terminated contracts & expenses: $200,000
  - Improved metric reporting, better HC management: $150,000
Calculate The Value Of The Team Contributions

4. Compensation support
   ✓ $2MM in monthly variable compensation, inputs calculated & supplied by FP&A team.
   ✓ Estimated value of FP&A team through added accuracy and precision: 20% ($400,000 monthly)

5. Internal & corporate parent close
   ✓ Not included here: could be done elsewhere? Overlap?
   ✓ Excluding things is OK.
Calculate The Value Of The Team Contributions

6. **Secondary Goals: not included here.**
   - Support of other finance teams as needed: expected by any team part of a larger department.
   - Internal process improvement: no hard dollar savings if we have constant headcount.
   - Documentation: very hard to measure risk prevention for us. Could possibly still carry on without documentation due to experience from cross training and internal promotion/transfer of duties.
In Total the Value Of The Team’s Contributions

- **Monthly executive business review meeting reporting**
  - Total FP&A time = 180 hours

- **Monthly executive business review**
  - Estimated impact of meetings on expense management: 4% ($400,000 monthly)
  - Estimated impact of meetings on revenue creation: 2% ($300,000 monthly)

- **Business Support and Analysis**
  - Annual operating & strategic plan - Estimated value of FP&A impact 5% ($8.75MM)
  - Business Development - Total impact on signed new business - $12M
  - Improved Efficiencies - $450,000 annually

- **Compensation support**
  - Estimated value through added accuracy and precision: $400,000 monthly

- **Internal & corporate parent close**
Consider Any Hidden Value

Hidden value:

- FP&A as a source of internal business leader development (not included here)

- Human capital market value surplus:
  - Hiring an equivalent FP&A team off the street, at AFP’s compensation survey values at 50th percentile, would cost approximately $100,000 more.

- Cost of outsourcing
  - Assuming a 30% margin applied to internally-sourced cost of FP&A team, outsourcing would cost an additional $300,000
  - Hiring difficulty
The Process

- Make Your Decision
- Define the Data
- Calculate a Value
- Measure Costs
- Confidence Measure of ROI
- Refinement & Ongoing Evaluation
**Measure the Cost of the FP&A team**

<table>
<thead>
<tr>
<th>Category</th>
<th>Cost</th>
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<tbody>
<tr>
<td>All-In Compensation</td>
<td>$741,000</td>
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<tr>
<td>Travel</td>
<td>$35,000</td>
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<tr>
<td>Recruiting &amp; Training</td>
<td>$20,000</td>
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<tr>
<td>Systems &amp; Services</td>
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<tr>
<td>Other</td>
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<tr>
<td><strong>Subtotal</strong></td>
<td><strong>$826,000</strong></td>
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<tr>
<td><strong>SV&amp;A Overhead (20%)</strong></td>
<td><strong>$165,200</strong></td>
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<td><strong>Total</strong></td>
<td><strong>$991,200</strong></td>
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Hours 15,000

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The Process

- Make Your Decision
- Define the Data
- Calculate a Value
- Measure Costs
- Confidence Measure of ROI
- Refinement & Ongoing Evaluation
## Arrive at a Confidence Measure of ROI

### Monthly Reporting:
- Production of Binder (hours) 114
- Analysis of Binder 38
- Review w/executive team 29

**Total Monthly Binder Hours** 180

**Weighted Avg Cost/Channel** $66.08

**Total Monthly Cost of Binder** $11,883

**Total Annual Cost of Binder** $142,601

### Monthly Review:
- Est Impact of expense mgmt $400,000
- Est Impact on revenue $300,000
- Compensation support $400,000

**Monthly expense impact** $1,100,000

**Annual Expense impact** $13,200,000

*Percent of total expenses* 8.8%

**Total Financial Review Value** $13,342,601

*Percent of total expenses* 8.9%

**5% Annual Expense Plan Impact** $8,750,000

**20% Business Development Revenue** $2,000,000

**Improved efficiencies** $450,000

**Total annual value** $24,542,601
Bill, that’s CRAZY…. $24 Million in value?
Let’s make some scenarios…

### Original Calculation

**Monthly Reporting:**
- Production of Binder (hours) 114
- Analysis of Binder 38
- Review w/executive team 29

<table>
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**ROI = 23.76**
**Bill, that’s CRAZY….$24 Million in value?**

Let’s make some scenarios…

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</table>

**Percent of total expenses** 8.8%

| **Total Financial Review Value** | $13,342,601 |
|**Percent of total expenses** | 8.9% |

| 5% Annual Expense Plan Impact | $8,750,000 |
| 20% Business Development Rev  | $2,000,000 |
| Improved efficiencies         | $450,000 |
| **Total annual value**        | $24,542,601 |

**ROI = 23.76**

### Alternative 1: A little conservative

<table>
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<td>Production of Binder (hours)</td>
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<td>$8,400,000</td>
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</table>

**Percent of total expenses** 5.6%

| **Total Financial Review Value** | $8,509,825 |
|**Percent of total expenses** | 5.7% |

| 3% Annual Expense Plan Impact | $5,250,000 |
| 10% Business Development Revenue | $1,000,000 |
| Improved efficiencies         | $300,000 |
| **Total annual value**        | $15,059,825 |

**ROI = 14.19**
Bill, that’s CRAZY….$24 Million in value?
Let’s make some scenarios…

<table>
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<tr>
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<th>Alternative 2: Very conservative</th>
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<td>ROI</td>
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5% Annual Expense Plan Impact $8,750,000
3% Annual Expense Plan Impact $5,250,000
1% Annual Expense Plan Impact $1,750,000
20% Business Development Rev $2,000,000
10% Business Development Revenue $1,000,000
5% Business Development Rev $500,000
Improved efficiencies $200,000
Improved efficiencies $200,000

Total annual value $6,147,931

ROI = 5.20

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Association for Financial Professionals®
Arrive At a Confidence Measure of ROI

\[
\text{ROI} = \frac{(\text{Gain from Investment} - \text{Cost of Investment})}{\text{Cost of Investment}}
\]

\[
\frac{($24,542,601 - $991,200)}{$991,200} = 23.76
\]

Plus: Hidden value

- Confidence: 50% on first pass: 11.5
- ROI could be as low as 5.2 at ~75% discount
Summary

- We excluded the following value:
  - Internal & corp parent close
  - Support of other finance teams
  - Internal process improvement
  - Risk management value through backup & documentation

- You can discount it down 75%

- WE STILL PROVIDE AT LEAST 5X RETURN
The Process

- Make Your Decision
- Define the Data
- Calculate a Value
- Measure Costs
- Confidence Measure of ROI

Refinement & Ongoing Evaluation
The Process: Refinement and Ongoing Evaluation

Clear Communication of Results is Essential to Project Success!
The Process: Ongoing Evaluation

- Periodic Review
- Satisfaction with Process
- Understanding & Application
Summary

- Even though this is challenging and can be inexact, it has many direct & indirect benefits

- Be unbiased and do it with an open mind, and be open to feedback

- Reevaluation and ongoing evaluation are critical, really makes the time worth it
Questions
Resources & Further Reading

- **Show Me the Money: How to Determine ROI in People, Projects, and Programs** *By: Jack J. Phillips & Patricia Pulliam Phillips*
- **The ROI of Human Capital** *By: Jac Fitz-Enz*
- **How To Measure Anything** *By: Douglas W. Hubbard*