Refocusing on the most important controls…it's about operations first…finance second

By Harry Gray and Chad Greenway

Often, we find that managers and business owners favor focusing their attention on financial controls. Unfortunately, financial controls tend to be indicators of prior events…controllable events.

In both high-growth and distressed environments, it is far more prudent to lock-down and institutionalize operating controls. Controlling enterprise-wide commitments that spawn future obligations of the firm is an essential activity that is embedded into the framework of leading corporations.

In high-growth environments, the activities of the management team are focused mostly on capturing the revenue upside. During this exciting and fast-paced time, it is exceedingly difficult to centralize decision making. Alternatively, as companies suffer in distressful times, managers tend to focus on cost-cutting and working capital management. This is akin to plugging holes in pipe leaks to thwart a flood. In both environments, it is more practical to lock down controlled commitments, which substantially mitigate surprises and the impact of rogue or poor decisions.

One simple technique that our team deploys is a comprehensive "authorities matrix" that governs the release authorities for all hierarchies and geographies across the firm. This is largely a cost-free, front-end control to restrict, in high-growth times, or prevent, in distressed times, the commitment of the enterprise to future obligations—the obligations that eventually get captured in A/P and evolve to monitoring as a financial control.

In our experience, the most commonly under-controlled operating/problem areas are: (i) product pricing at the salesperson level; (ii) engineering and development commitments; (iii) new customer acquisition costs; (iv) vendor proliferation; and (v) non-inventoried supplies, especially consumables.

The rollout of an "authorities matrix" is most effective when specifically structured by functional area and pay-grade level. At the same time, we strongly advocate that line managers and senior management acknowledge the matrix with signature. At larger, more complex organizations, it is worthwhile to scope a technology-enabled solution, such as a triangulated "requisition-to-purchase order-to-receipt" command and control system that is linked to the company's ERP application. However, these systems-based rollouts can often experience scope creep, and the reduced leakage may not justify the cost.

In any event, whether simple and cheap, or technologically complex and expensive, getting ahead of the commitment curve through this technique is a good practice for all businesses.