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ENERGY / FORWARD

5 Keys to Unlocking CFO Approval

ENERGY STAR PARTNER

INTRODUCTION

Increasing energy costs and growing pressure on the bottom line are pushing more companies to look at efficiency improvements to lower operating costs. And, while many CFOs are aware that reducing energy usage can save money, efficiency project proposals are often buried in energy audits that are difficult for the CFO to comprehend. Why? These proposals aren't written for the CFO. They are focused on detailed energy analysis, and they often do not include the investment summary – including options to finance the project – that CFOs need to make informed investment decisions. As a result, more than three out of four projects do not get approved, according to a recent Noesis survey.

If you propose energy projects to CFOs, this is your guide to better understand how to make investment proposals that have a better chance to be approved. The guide will cover the five keys you should keep in mind when preparing your energy project's proposal. With these, you will be able to enhance your proposals, making them CFO-friendly by focusing on the issues that they care about most, which will increase your rate of project approval.

CONTROL THE ENERGY AND GREEN SPEAK

It's no surprise that energy professionals are comfortable talking about weather-adjusted baselines and energy conservation measures, but are often not trained to speak in the language of the CFO. They're trained to identify, evaluate and propose energy efficiency conservation measures to reduce the company's overall energy costs. The challenge for energy professionals is that they're also responsible for "selling" this project to the CFO, who (seriously) may not even know what a kWh is. So, energy professionals must speak in the financial terms that make it easy for the CFO to make an informed investment – not efficiency – decision. As everyone knows, CFOs are tasked with managing and maximizing the return on the company's investments, not saving energy. The more the energy speak is translated to financial speak, the better the chances the capital project gets approved.

Second, while you'd be hard-pressed to find a CFO that doesn't care about the environment, you'd be equally hard-pressed to find a CFO that will make a capital investment based purely on environmental impact. Efficiency projects should stand on their own financial merit, independent of any "green" benefits. To be sure, increasing efficiency reduces the impact on the environment, but it's a secondary benefit to the CFO, not a primary reason to make the investment. And, the unfortunate reality is that the more an energy project proposal focuses on the environmental benefits, the more suspicious the CFO becomes of the financial business case. So, does this mean that you shouldn't mention the environmental impact in your proposal? No, it means that you should keep the business case separate from the environmental benefits. Capital investments are made for business – not environmental – reasons. Industry insiders know that those reasons are highly correlated; however, many CFOs still think they're inversely related. As such, do your best to control the green speak when pitching your efficiency project.

DON'T SHOW UP UNPREPARED

With all of the other investment opportunities waiting on the CFO's desk, you often only have one opportunity to pitch your project. So, it is critical that you show up prepared to get your proposal approved. That is, you must know what the CFO uses to evaluate capital investment proposals and, second, what the process is for getting a "yes."

The first thing you must do is understand the company's financial decision-making criteria. Knowing the company's minimum requirements for investments will help you put together a tailored proposal with a better chance for approval. Most companies have an internal hurdle rate, which is the required minimum rate of return on a project. Know what this is beforehand. Once identified, you should make an assessment of the project using a risk-and-return perspective to determine if the project has a chance at being accepted. The project's internal rate of return (IRR) should be higher than the company's internal hurdle rate. If it's not don't waste the CFO's time. It's that simple.

Other financial measures, such as net present value (NPV), debt coverage ratios, payback period, and return on investment (ROI) should also be considered in the initial proposal to determine the project's viability. Know which ones your CFO likes, trusts and uses. To get this information, of course, communication with the CFO and finance department is important as you prepare your analysis.

Second, you must understand the process by which projects get approved and budgeted. Do they have to be vetted by procurement? Is there a bid or RFP process? What time of year do projects get budgeted? Who needs to buy off on the proposal before the CFO can approve it? If you're new to the organization, get this information from the facility team and others who have proposed equipment purchases in the past. They'll know the ins and outs, the pitfalls and internal best practices to getting projects approved.

Again, you often get one shot to propose your project. Know the criteria that the CFO uses and know the process for approving projects beforehand to maximize your chances for success.

EMPHASIZE BENEFITS TO CORE BUSINESS

CFOs focus on growing their core business, whether that's auto manufacturing or banking or whatever. As such, any use of their capital should impact the core business. This is where many efficiency project proposals fail. Do CFOs care about saving money? Of course they do, but they often need to think about the savings in terms of their core business to understand the impact and urgency of those proposals.

First, you should discuss the project's benefits, keeping in mind the company's functions, to show exactly how the project will reduce costs. For example, if the project is retrofitting an office building, how much cash savings can the CEO expect to see per square foot? Or, for a manufacturing plant, how will the project affect the cost per production output? Cost/benefit analysis, the ratio of the project's total capital cost to the direct savings, helps prove the project's worth. Financial analysis should incorporate variables unique to the company, such as operation hours or production outputs, so that the investment appears aligned with the company's core strategies and savings estimates are more accurate.

In the end, the CFO should be able to read directly – not infer – how the savings from the project can help drive the core business, whether that's more cars produced, increase in retail store margins, and so on.

In addition to growing the core business, the second benefit that CFOs focus on is growing the value of the assets of that core business, such as increasing the value of the company's building stock. Building values are a function of cash flows generated. If the building generates more cash, the building's value increases. While this is not news to most people, what energy professionals often overlook is the power of illustrating incremental cash flow at the building and portfolio level. The CFO knows their real estate capitalization rate and can quickly calculate the increase in value that the efficiency project delivers to their real estate. This also helps the CFO make a sound business decision, not an energy efficiency decision, which also improves the proposals odds of getting approved.

BRING FINANCING OPTIONS TO THE TABLE

One of the biggest mistakes energy efficiency professionals make when putting together project proposals is not including 3rd party financing options. While some CFOs prefer to self-fund capital investments, many CFOs do not have the budget set aside to invest in unanticipated – and often large - efficiency projects. Many would like to look to outside lenders for investment, but don't have the time to. As such, many projects that are not budgeted simply do not get approved. In fact, many projects – because their returns are so compelling – don't get rejected, they just get shelved for the next budget cycle and are often never seen again.

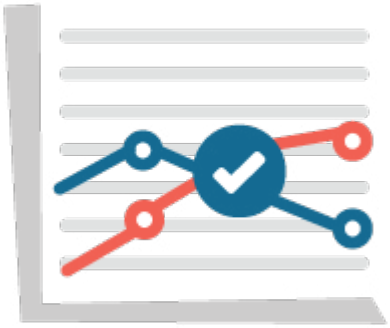
Presenting a range of financing options is often effective at getting a project approved, but finding the right financing vehicle and lender can be time consuming and confusing. It is your responsibility to understand the types of options available and discuss them with a project finance expert before presenting them to the CFO. Even though CFOs are fluent in financing, the financing vehicles for efficiency projects are various and sophisticated, each type having its tradeoffs. Whether it's a capital lease or an operating lease, guaranteed savings or not, variable payments or fixed, on-balance sheet or off, there are many factors to consider when determining the right vehicles to include in your proposal. Upfront homework on financing preferences and working with an expert in efficiency finance is the best way to make sure that you present relevant and viable financing options to the CFO.

ADDRESS THE COST OF DOING NOTHING

Efficiency upgrades are one of many investment opportunities the CFO is considering across their organization. Efficiency upgrades represent untapped savings potential that if shelved or passed over will continue to cost the company incrementally over time. The cost incurred from inefficient equipment when projects don't get implemented is one of the most compelling arguments in helping make the efficiency business case.

When projects don't get installed companies continue to pay for the utility costs to run inefficient equipment up and until the equipment reaches the end of its useful life. When equipment fails it is typically unplanned and must be replaced quickly. This process can be just as costly as the efficiency upgrades that were passed over and the equipment is never as energy efficient as what was initially proposed. When efficiency upgrades are not addressed the company ends up paying more for less efficient equipment than they would have for the high efficiency equivalent.

Aside from avoiding the operational costs of inefficient equipment and emergency installations for failing equipment, efficiency upgrades free up cash flow. This cash flow can be used to fund other efficiency investments or simply moved to another part of the business. Whether financed internally or by a 3rd party, efficiency projects can free up significant funds for use within the company. It's critical that your proposal shows that the project will begin paying for itself upon installation and consequentially identifies how much money will be freed up from the project. When considering an efficiency project in place of other investment opportunities the ability of the project to free up cash flow day one gives the CFO flexibility in managing the several investment opportunities where they are considering at once.



CONCLUSION:

Efficiency investments are an unfamiliar territory for most CFOs and often get turned away due to lacking or incomplete project proposals. To get more energy projects approved and implemented, you must know what CFOs look for in proposals and how to present them in a language that the CFO understands. Taking on energy projects should be viewed as an ongoing business strategy to lower the company's operational costs.

Keep the keys above in mind when preparing your energy project proposals and they will help unlock the necessary CFO approval to get your projects done.