

Beyond Compliance

Regulatory mandates can yield a performance dividend.

Regulatory compliance can be like a bad dream. As any CFO will testify, aligning an organization to satisfy the mandates of Sarbanes-Oxley has proven to be a huge challenge.

But the dream can end happily. While the costs of compliance violations are daunting, choosing the right way to respond to the demands for transparency, timely reporting and accuracy will deliver more than a good night's sleep. New research shows that leading-edge CFOs are moving their organizations to use compliance as a lever to dramatically improve corporate performance.

The process involves understanding and documenting existing processes, improving those processes and investing in technology to support business process change. By doing so, an organization's compliance efforts can yield a substantial dividend: A lens into the business that supports sustainable compliance as well as an enhanced capability to manage business performance. This, in turn, translates into a sustainable competitive advantage.

Short Term vs. Long Term

Top-of-mind these days for almost every corporate officer is the Sarbanes-Oxley Act of 2002, especially what is universally known as "404." This section requires management to assess the effectiveness of its internal controls over financial reporting and then report on that assessment at the close of its fiscal year. It also requires validation from an external auditor.

The law requires that CEOs and CFOs personally vouch for the integrity of financial statements. Although both are subject to criminal penalties for knowingly and willfully certifying incomplete or inaccurate reports, the CFO is considered the key compliance manager. And the CFO's financial consolidation and reporting systems are the foundation of Sarbox compliance.

Unfortunately, existing financial reporting systems, typically supported by spreadsheets and manual intervention, have not proven equal to the consolidation task. "Most CFOs and their teams feel pressure to deliver financial information on a timely basis," notes a recent report by International Data Corp. (IDC), a Framingham, Mass.-based research firm. "Yet they are tied to



period-end financial closing processes that take too long to complete, followed by cumbersome, manually intensive report preparation processes that precede actual performance reporting and analysis.”

As a result, many companies have fallen into the trap of allocating resources to speed the response time of existing systems and tying them together with ad hoc connections.

In a competitive market environment and with stakeholders watching, this costly manual approach is not sustainable in the long run. “We can’t just keep throwing people at the problem,” says David Axson, President of The Sonax Group, a business consultancy in Bath, Ohio.

Robert Kugel, Vice President and Research Director at Ventana Research in San Mateo, Calif., says this short-term focus on automating legacy processes is about “paving the cow paths” rather than designing more direct routes. He argues that companies should consider replacing their traditional bottom-up, sequential consolidation process with a synchronous approach wherever possible. Kugel suggests this can be faster, more accurate and less expensive.

Redefining Processes

CEOs and CFOs are looking to technology to make financial consolidation and reporting more efficient and cost-effective. “Some companies recognize that a number of compliance issues can be addressed by redefining processes within the organization to eliminate manual steps, for example, or eliminate spreadsheets or just simply automate functions that no one had thought of before,” Kugel explains.

Indeed, a recent poll of CFOs and other senior financial managers by CFO Research Services found that implementing technology is the most frequently taken step when launching a new process initiative.

In addition, new regulations were the most frequently cited catalyst for finance and IT department change, just ahead of customer or partner requirements (see chart, Regulations Drive Finance and IT Change).

Information on Compliance and Performance

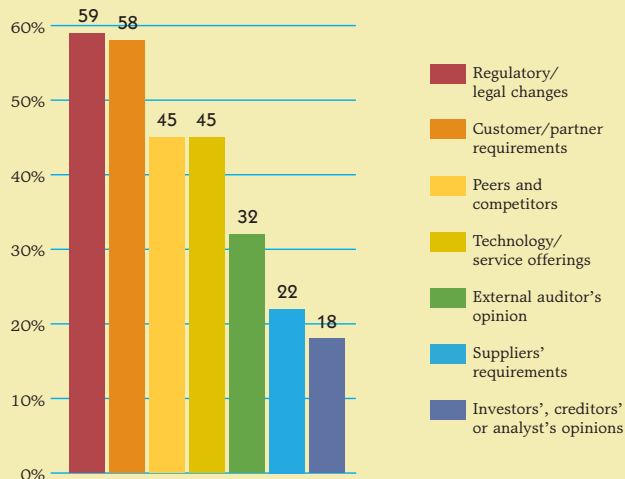
You can address regulatory compliance while delivering the competitive edge of performance management. Visit the Cognos Compliance Resource Center for comprehensive analyst reports from Gartner and Ventana, our whitepaper “Compliance and Performance-Neither is Optional” and other valuable information.

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In the pre-Sarbanes-Oxley environment, spending to upgrade consolidation and closing processes that were adequate to the required tasks wasn’t high on the priority list. Now, in the face of the requirements of Sarbox, the International Financial Reporting Standards, Basel II, HIPAA and their siblings as well as the increased costs for headcount resources and audit fees, that

Regulations Drive Finance and IT Change

(percentage of respondents rating the biggest catalysts for change by choosing 4 or 5 on a 1-to-5 never-to-often scale)



Source: CFO Research Services, *Compliance: Finance's Bridge to the Enterprise*, November 2004

cost-benefit equation has shifted. Today, the migration to financial consolidation and reporting tools is a low-threshold process. Solutions to replace existing manual systems are easy to set up and flexible enough to adapt as organizational priorities or legal mandates change.

The Next Step

In addition to deploying an automated financial consolidation system with the requisite controls, an organization must ensure visibility into those controls and the business activities they monitor. The reporting and analysis tools that provide this visibility also can improve business performance.

“A key to improving business controls is structuring and automating those important, repetitive financial processes like consolidation, planning and reporting,” says Delbert Krause, Director, Global Marketing, Office of Finance, at Cognos. “This same investment often collapses cycle time, creating a more continuous and dynamic assessment of performance. Not only does the comparison of actual to expected performance provide confidence that there has been a full and fair accounting of results, but it also creates important lead time for companies to respond with precise, coordinated action to improve performance.”

Improving consolidation tools and adding planning, analysis and reporting capability creates an opportunity, says The Sonax Group’s Axson. “The opportunity is to take the discipline the regulations demand and apply it to broader sets of information. By using the tools in corporate performance management technologies, you can take the visibility and transparency that you’re being forced to deliver for a sliver of your information related to finance and apply that to the broader operation.”

Axson and other consultants have identified 10 “hidden treasures” of automated systems installed to meet regulatory requirements. The right system provides CFOs with a better

understanding of the underlying business processes, how their companies use resources and where there are opportunities to improve. Ultimately, a finely tuned system can deliver sustained competitive advantage relative to other organizations (see box, The Hidden Treasures of Compliance).

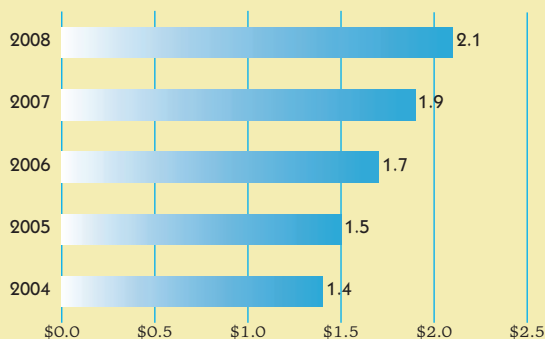
A recent market forecast by IDC predicts that sales of business performance management applications, which include financial consolidation, planning/budgeting and scorecarding solutions, will increase at an 11 percent compound growth rate through 2008 (see chart, Growing Interest in Business Performance Management Applications).

And compliance is one driver of that increase. "As companies come out of year one of Sarbanes-Oxley 404, the attitude is, 'I'm not doing this again,' and there are clear plans to invest in solutions to better manage the process in the future," explains Kathleen Willhide, the Research Director, Compliance and Business Performance Management Solutions, at IDC. "Budgets are freeing up for compliance management systems, performance management solutions to support financial and management reporting, and a business intelligence infrastructure so that companies can better meet compliance and other reporting and performance management challenges."

Adds Sam Silvers, Principal and National Practice Leader, CFO Services, at New York-based Deloitte Consulting LLP, "we're see-

Growing Interest in Business Performance Management Applications

(worldwide software revenue, \$ billions)



Source: IDC, July 2004

ing a definite uptick in organizations willing to make investments." The era of Sarbanes-Oxley, he says, has added both the reduction of compliance costs and the ability to mitigate risk as positive ROI factors. "Neither of those really mattered a few years ago."

The Right Tools

CFOs are buying toolsets that let them function as both the corporate strategist and the compliance monitor. They want and need an unobstructed view of financial and operational data as

The Hidden Treasures of Compliance

Complying with regulatory mandates about finance through automated consolidations can lead to tremendous business performance benefits.

- Reduced finance costs
- Fewer errors
- Faster and more efficient quarterly and annual closings
- Investor and director satisfaction
- Financial transparency
- Improved business decision-making
- Return on compliance investment
- Opportunity for finance to play more strategic role in operations
- Better understanding of underlying business processes
- Opportunity to identify inefficient business processes

Sources: IDC and Ventana Research analyst firms and The Sonax Group

well as the analytic tools to determine patterns, uncover key relationships and forecast future performance. Once CFOs have these abilities, they can advise other C-level executives and line-of-business managers about opportunities to reduce costs and re-allocate resources to higher yielding activities.

The ROI of mitigating risk and other benefits may be difficult to quantify because the potential effects are so broad and also deep. But the combination of regulatory mandate and performance management fine-tuning should make the value obvious. "There are investments that CFOs know inherently to be good decisions, even if they can't quantify the return," says Doug Barton, Vice President, Global Marketing, Office of Finance, at Cognos.

"It is hard to test the ROI of some strategic systems because you never know what the cost of not investing in better performance management systems is," Barton adds. "It's the cost of a bad decision or a situation avoided or a risk mitigated. Most CFOs will tell you about their frustration as they reach the end of a quarter or a fiscal year, not knowing what they can do about the gap between their goals and forecasted performance. The demands of regulatory compliance may introduce hurdles for finance executives to overcome, but they know that greater performance is really the race they're running." ■

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For More Information

Information about financial planning and consolidation, corporate performance management and other finance tasks is available at <http://www.cognos.com>