

From Crisis To Control:

Full Command of Financial Close Processes and Performance

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Executive Summary:

Automation can transform your financial close process from chaos to control, from a tactical obligation to a foundation for strategic financial decisions and leadership. Significant quantitative and qualitative benefits can be realized through an automated system that can serve as a unified platform for the efficient production of your financial information.

Key Findings:

- Despite a predictable monthly, quarterly and annual schedule, the financial close process is often remarkably chaotic
- Nearly every company has defined goals for improvement in financial close speed, efficiency, and costs, yet few are achieving them
- Systematic automation is often lacking in today's financial close processes

Recommendations:

- Companies need automated process control, performance control and measurement, and self-documentation to improve their financial close process
- Seek “control”—strategic command of your finance processes and information—not simply tactical compliance to “controls”

Introduction

Most financial departments have broad strategic goals for improvement of recurring financial close processes. But your staff can only do so much: automation of the financial close process is crucial to achieving faster close times, higher efficiency, and increased strategic value. Automation enables financial teams to take command of the entire financial process instead of simply managing to controls.

With automation, your company can gain full command over financial close cycles, streamlining the entire workflow and capturing important metrics to monitor, measure and improve performance.

Financial Close: Processes and Goals

In spite of the predictability of its monthly, quarterly and annual occurrences, the financial close process is often remarkably chaotic. In most companies, it's generally a recurring managed crisis, dependent largely on the controller or close manager, who acts as the centralized “traffic coordinator” and attempts to contain and direct the chaos within a tight deadline.

Typically, during the close period, the close manager and the rest of the accounting team have little advance warning of bottlenecks or issues, and it's difficult to get a detailed view of the status of completed and outstanding tasks. In spite of all these limitations, the financial team rises to the challenge and powers through the process largely through brute force, allocating as many staff members and as much overtime as it takes to hit the targets for handoff to the reporting process.

It's an exhausting process, and nearly every company has defined goals for improvement. Speed and efficiency are high on the list: faster close times become increasingly important as reporting requirements increase and deadlines decrease; and companies must reduce

errors, risk and costs. Further, these companies seek to gain more strategic involvement from the finance team on company initiatives, including leadership in higher-level and higher-value financial governance roles.

Financial Close: Challenges and Issues

Unfortunately, many companies are not achieving their goals for improvement in financial close. Is yours? If not, it may be time to change the way you view financial close. Your financial close processes are as important as the processes that result in the products and services you deliver to your customers.

Financial close is a recurring process, with known input sources and pre-defined outputs, as much a production environment as a manufacturing line, retail storefront, or freight provider. Nearly every department and industry with similar recurring, systematic processes has deployed technology to ensure that they can achieve high efficiency, high quality, high repeatability, and can capture the performance metrics to manage the process.

Yet that same systematic automation is often lacking in today's financial close process. In many companies, the close period is still highly-reliant on manual—and menial—work to perform the necessary tasks and manage the process. Is your financial close process more like an automated assembly line or a workshop? No matter how skilled the craftspeople, the workshop will reach a performance threshold.

Also missing from most financial close processes are the means to capture performance metrics. As previously mentioned, this results in limited visibility to detailed status and performance during the close. Worse, measurements that could be used after the close to evaluate workflow, eliminate bottlenecks, consolidate tasks and otherwise improve the process are rarely available. Without this information, attempts at process improvement can only be guesswork.

In addition to these internal issues, companies like yours are also facing external challenges. An uncertain economy has increased the importance of all financial areas—from cash flow and revenue recognition to capital investment, credit and liability. More analysis and a strategic approach is needed from the finance team to best react to downswings without restricting the ability to profit during upswings.

Regulations and requirements for financial reporting are also increasing, leading to increased scrutiny on the financial close processes that serve as the source of that information.

Financial Close Processes in Today's Regulatory Landscape

Regulatory compliance has become an increasingly costly burden. For example, SIFMA has estimated that the U.S. securities industry in 2004 spent \$23.2 billion on compliance-related activities¹. In addition, regulatory mandates have become more intrusive in their application to how business is conducted. In response to corporate scandals such as Enron, the mandates have shifted from regulating the final **work product** to be produced for regulatory review, such as the enterprise's financial statements, to also regulating the **process** by which the final work product is produced. This principle is clearly evident in Section 404 of the Sarbanes-Oxley Act ("SOX")². Section 404 requires corporate management to prepare a report on their internal controls and disclosure and their analysis

¹ See <http://www.sifma.org/research/surveys/pdf/CostofComplianceSurveyReport.pdf>.

² See <http://www.sec.gov/about/laws/soa2002.pdf>.

as to the effectiveness of the internal controls in producing reliable financial statements for the corporation. As part of the Section 404 requirement, management must identify the internal controls framework on which the internal controls are based (e.g., the Committee of Sponsoring Organizations of the Treadway Commission (COSO) framework). Management also must obtain an attestation from an independent auditor as to the sufficiency of their internal controls

Increasing the regulatory pressure, the frequency with which important mandates are being issued has grown over the past few years. Further, reporting deadlines also have been shortened. For example, under Section 409 of SOX, issuers must publicly disclose "on a rapid and current basis" any "additional information concerning material changes in the financial condition or operations" of the company. In order to implement this SOX provision, the U.S. Securities and Exchange Commission shortened the period within which a Form 8-K "Current Report" must be filed to four business days. Four day reporting periods can pose a serious problem for companies with data contained in a multitude of repositories subject to different policies, where an inadequate self-document regime is in place and where the financial close process is heavily manual. This environment can result in the time-consuming need to conform data before consolidation into one master data set before further time-consuming manual financial close processes can begin.

One consulting study estimated that a likely allocation of industry compliance budgets is as follows: (a) 55% for staffing, (b) 15% for IT, (c) 12% for training, (d) 10% for external counsel, and (e) 8% for auditing and monitoring³. The study's formula makes it clear that the majority of compliance cost (67%) results from training and staffing, rather than from IT and other costs. This suggests that automation of financial close business processes based on an enterprise-wide self-documentation and controls approach will reduce staffing and training costs. This in turn should reduce total compliance costs and help companies shortened reporting deadlines.

The Difference Between "Controls" and "Control"

In order to achieve your *strategic* goals of increased speed and efficiency from financial close, and take a higher-level role in planning and governance, you need a strong *tactical* foundation of control.

This tactical "control" is different from "controls." Finance is typically focused on managing, enforcing, and complying with internal and external controls. Such controls include internal rules, formulas, policies and procedures and external regulatory requirements for transparency and risk management. The emphasis is on "what"—providing the right output—with secondary consideration of "how," mostly to ensure consistency of the output.

"Control" goes beyond these "controls." Control means that you are in command of your finance operations. You are able to define proactive plans, schedules and tasks that set expectations for performance prior to the start of the financial close period. During and after the close process, information is captured so you have the necessary situational awareness to inform your decision-making instead of reacting based solely on intuition.

Control gives you the ability to effectively shift roles and focus within the finance team based on market conditions—up or down—and company initiatives and cycles, such as annual budgeting or an acquisition.

³ See Virginia Garcia, "Seven Points You Should Know About IT Compliance Spending" (TowerGroup September 2003).

Control addresses both “what” and “how” equally, enabling you to ask not just “did we do it right?” but “how can we do better?” To get this control, to reach your performance goals, the financial process needs automation.

Automating Financial Close Processes

Automating the financial close process brings all components of the close, from start to finish, into a single, unified system. This automated system becomes the new “hub” of the close process, managing all data, policies, processes, tasks, collaboration and communication. This automated system becomes the production platform for the entire financial close process, and delivers three key attributes needed for improved performance: process control, performance control and management, and self-documentation.

Process Control: Automation of Workflow

The first step toward gaining control of financial close is automating the process itself—automating the actual financial close workflow to follow to your company’s standardized processes and procedures.

All financial close tasks are managed within the automated system, with associated due dates, dependencies and descriptions. These tasks can be assigned across the finance team, regardless of physical location.

With the automated system, the close manager is freed from the role of hands-on “traffic coordinator,” and gains detailed visibility to the status of the close process. All communication and collaboration is managed through the system, enabling staff to work with each other, directly sharing tasks and information. Issues that will lead to delays can be flagged early, and clearly show the potential impact on other tasks. Overdue tasks are automatically escalated, eliminating the need to chase missing information.

Built-in data validation rules help reduce errors and eleventh-hour troubleshooting. The system streamlines the entire financial close process to help achieve the goals of faster close and higher efficiency, while reducing the amount of manual and menial effort. In an ideal environment, the financial close automation is integrated both upstream—with transaction and account reconciliation—and downstream—with financial reporting.

Performance Control and Measurement: Metrics and Financial Performance Management

The benefits of process control described above improve an active financial close process. To achieve true control over performance, to reach beyond “faster close time” to higher-value improvements, you need information on the performance of the financial close process itself. Automated financial close helps you plan and analyze “how we can do better” before, during, and after every close.

Performance metrics are critical to achieving ongoing improvements in performance, and modifying your financial close process for optimum results as your organization evolves. Changes to accounts, cost centers, policies, organization structure and regulations significantly impact the close process. You need to have information that leads to insight for strategic planning. Where are you experiencing bottlenecks? Can steps be eliminated from the process? What anticipated changes require adjustments to the timeline or workflow for the next close?

Automation of financial close provides the performance control and measurement metrics *and* the increased efficiency to enable this level of strategic review and planning.

A wide variety of performance metrics are necessary for thorough analysis and reporting. Results should be grouped or filtered by category, task, user, and other criteria for both wide-angle and narrow-focus views. Performance should then be analyzed as benchmarks or KPIs in tabular or graphic formats.

Benchmarks report absolute performance measurements for evaluation against internal targets or industry standards.

Example Benchmarks:

Costs	<ul style="list-style-type: none"> • Cost of noncompliance/control failure • FTEs for close • Finance as % of revenue • Audit fees as % of revenue
Quality	<ul style="list-style-type: none"> • Number of control remediations • Auditor adjustments • Post-close adjustments • Draft reports
Timeliness	<ul style="list-style-type: none"> • Days to close • % tasks late

KPIs are “indicators” along the process stream that give alerts to process issues which, if not addressed, can impact business outcomes.

Example KPIs:

Costs	<ul style="list-style-type: none"> • Increase in number of non-recurring transactions • New account requests • Task Re-work; supporting schedules • Journal Entries containing errors or requiring re-adjustment
Quality	<ul style="list-style-type: none"> • Changes in policies/procedures • Increase in issue escalations • Increase/decrease in expected results (returns, receivables, etc.)

Timeliness	<ul style="list-style-type: none"> • Increase in expected volumes (POs, invoices, paychecks, etc.) • Post cut-off transaction postings • Current days to close vs. previous days to close
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Real Time-Documentation

Real time-documentation is the third attribute of automated financial close and a key support for both process control and performance control.

For process control, real-time documentation embeds and synchronizes your policies with your process. This self-documentation ensures that your tasks match your policies—changes to policy are immediately reflected in the action plan—so financial staff has a single authoritative source for every task.

Throughout the process, your detailed instructions, supporting attachments, notes, communication chains, and review procedures accompany every active and completed task in the financial close process. While process control automation ensures that tasks are completed according to your plan, real-time documentation automatically captures the supporting information to document that compliance for review and audits.

Further, real-time documentation is the enabler of performance control. Measurements are captured automatically, as part of the financial close process. No effort is added to the tactical steps of the financial close process to yield a wealth of strategic insight.

Benefits of Financial Close Automation

Automation can transform your financial close process from chaos to control, from a tactical obligation to a foundation for strategic financial decisions and leadership. Significant quantitative and qualitative benefits can be realized through an automated system that can serve as a unified platform for the efficient production of your financial information.

Benefits of Financial Close Automation

Quantitative Benefits

- Shorter cycle times
- Increased productivity
- Reduced overtime and costs
- Reduced write-offs
- Reduced audit fees through automatic supporting documentation
- Lower operational and training costs

Qualitative Benefits

- Increased accuracy
- Increased compliance through technology-supported and -enforced controls
- Increased visibility
- Increased focus on strategic projects
- Better decisions
- Reduced risk
- Improved staff satisfaction, utilization and retention through reduced menial work
- Improves recruiting through lower requirements and shorter learning curve
- Better adaptability to up/down economic conditions