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Align Financial Processes And Systems For Better Business Value And Compliance

by Paul D. Hamerman
for Business Process Professionals

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by Paul D. Hamerman
with Rob Karel and Emily Fowler-Cornfeld

EXECUTIVE SUMMARY

The three key activities of corporate financial management take place on a continuum of the past (reporting and compliance), present (analysis and measurement), and future (planning and forecasting). Financial business process (BP) professionals must coordinate the activities that are part of this financial process life cycle (FPLC) to enhance the value of information within the business and drive better execution of compliance imperatives — but automation and integration gaps discourage their efforts. By treating the full array of financial activities as a cycle or continuum, financial BP pros can more effectively integrate and automate these activities, creating a valuable resource of historical, performance, and predictive information. This information will give financial BP pros a better understanding of past results, current business performance, and expected future results and improve their ability to make strategic and tactical decisions.

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NOTES & RESOURCES

This research is based on approximately 75 Forrester client inquiries over the past year, as well as discussions with 12 financial management software vendors: Adaptive Planning, Concur Technologies, Host Analytics, IBM, Infor, NetSuite, Oracle, Prophix Software, SAP, Tagetik, Trintech, and Unit4.

Related Research Documents

"Trends 2011: Financial Processes And Applications"
February 18, 2011

"TechRadar™ For BP&A Professionals: Financial Management Applications, Q2 2009"
June 30, 2009

"Accounting Systems: The Nucleus Of Your Recession And Recovery Command Center"
March 24, 2009

FINANCIAL PROCESSES REQUIRE ACCURACY, INSIGHT, AND INTEGRATION

Enterprises struggle to coordinate financial processes using various piecemeal and disparate systems. Many financial processes are periodic and are thus tied to a set of batch processes and interfaces. This process wiring inhibits companies from driving higher levels of business performance because organizations don't design core financial systems to deliver timely or predictive insights.

Financial BP pros are looking to address a variety of information and process challenges caused by the disconnected nature of their financial systems and processes. Discussions with Forrester clients about financial systems and processes reveal that:

- **For many companies, the core accounting system is a transaction hub.** Most companies maintain dozens of systems that feed the core accounting applications such as procurement, inventory, fixed assets, and accounts receivable. In addition, most enterprise-class companies manage not one central accounting system but several disparate systems supporting various business units and subsidiaries.

- **Batch processing persists in the accounting realm.** Accounting system interfaces tend to be orchestrated via batch processes to reflect accounting's periodic nature. Typically, systems are updated daily or monthly as required to support the monthly close process. This close process often takes several days due to latency in information and the complexity of procedural accounting requirements such as accruals and adjustments.

- **Financial performance measurement requires more timely information.** Core accounting systems can't provide real-time information to support business decisions due to their historical, batch orientation. Yet the pace of finance processes in areas such as treasury and cash management, revenue management, and electronic payments is much quicker. Adoption of standards-based, real-time integration lags behind business needs for real-time business performance information.

- **Planning processes lack coordination.** Budgeting is a classic planning process that drives discipline and control over spending but seldom provides the flexibility businesses need as conditions change. Finance organizations often support numerous additional disconnected planning and forecasting processes that provide visibility into sales, production, capacity use, cash flow, human resources turnover, and hiring.

Financial Management Processes Must Evolve With Changing Business Conditions

Forrester survey data shows that financial management systems represent a top application investment priority in 2011.[1] Core accounting systems are mission-critical to the extent that companies of all sizes must have them. These systems must supplement various other solutions that automate the financial reporting cycle end-to-end, from closing the books to meeting regulatory compliance obligations and generating insight into business performance.

The following trends in financial systems and processes are playing out currently:

- **Regulatory compliance is a fundamental driver for financial systems.** International Financial Reporting Standards (IFRS) and mandatory filings using XBRL technology continue to drive investment in financial accounting and reporting systems. Financial consolidation software and disclosure management applications are high priority for larger companies facing increased compliance requirements. The Sarbanes-Oxley Act of 2002 (SOX) introduced stringent internal control requirements that remain a priority as well, promoting technology use for automation and substantiation of effective controls.

- **Budgeting and forecasting enable companies to manage through uncertainty.** For many companies, budgeting remains ingrained as a planning discipline and cost control vehicle, despite its high level of effort and relative inflexibility. Forecasting is a more nimble process, since updates occur more frequently, and is becoming more and more relevant as financial BP pros try to anticipate the timing of the economic recovery. Planning software that supports budgeting and forecasting processes also represents a robust area of investment. Predictive algorithms, real-time collaboration, and external data feeds will enhance the capabilities of these solutions going forward.

- **Closing the books starts the financial reporting cycle.** Companies will increasingly look to automate the entire financial close-to-disclosure cycle. Several leading vendors now aggregate solutions, historically sold separately, that enable financial close, reconciliation, statutory consolidations, regulatory filings preparation, XBRL tagging, tax planning, and internal management reporting. Increased automation of this entire cycle will improve the efficiency and timeliness of financial reporting.

- **SaaS financial solution adoption will strengthen as solutions mature.** SaaS adoption is already mainstream in several application areas, such as HRM and CRM, but relatively light in financial management. Adoption of SaaS solutions in finance will increase as more competitive and scalable options materialize, including core SaaS accounting systems. In addition, a variety of other financial process solutions are migrating to a SaaS deployment model, including expense management, planning, financial disclosure management, treasury systems, account reconciliation, and other point solutions.

- **Financial application footprints evolve via rationalization and standardization.** Enterprises continue to reduce the number of moving parts in their financial applications portfolios by consolidating accounting systems to a single centralized, global instance. Smaller subsidiaries, however, tend to remain outliers in this portfolio. Companies now make moves to standardize these subsidiary systems on lighter-weight accounting packages. Fewer systems will reduce IT costs while providing for a faster and more efficient closing cycle.

THE FINANCIAL PROCESS LIFE CYCLE INTEGRATES INFORMATION ACROSS TIME DIMENSIONS

Financial processes can be categorized by the three dimensions of time — past, present, and future (see Figure 1). These time dimensions are a convenient way of categorizing financial process activities based on the information content:

- **The past dimension is the essence of the accounting discipline.** Accounting professionals record the historical financial performance of the business, from transactions to summarized reporting. The range of their activities includes booking transactions and subsidiary ledger balances to the general ledger accounting system, closing the books periodically, producing internal and external financial reports, and meeting compliance obligations.

- **The present dimension analyzes the current situation.** In the present dimension, we measure how the business is performing today, and in some cases, *right now* (i.e., real time). Accounting systems are not designed to support this dimension, so measuring and monitoring the business requires analytic applications as well as monitoring systems to look at financial performance metrics, trends, cash flow, investments, and controls.

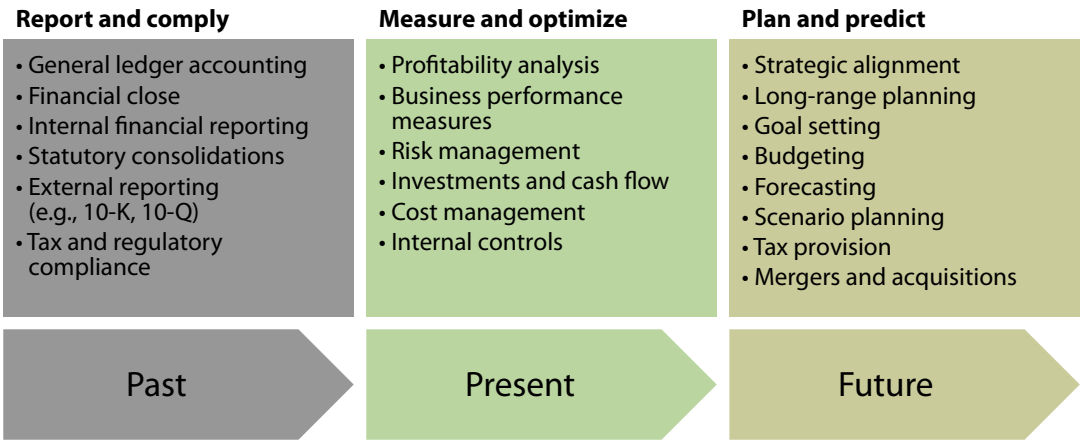
- **The future dimension looks into the crystal ball via planning, budgeting, and forecasting.** The future dimension deals with planning processes of different types and frequencies, from long-range strategic plans and annual budgets, to short-term forecasts and event-driven scenarios. Building useful plans and forecasts relies on data produced from the other two dimensions.

To optimize business processes across these three time dimensions, financial BP pros must consider the value of information over time (see Figure 2). Information delivers the most value when it's fresh, but that value erodes over time, no matter which dimension we're talking about. The pace of value erosion varies by process.

Performance measures, for example, offer near-term value, but the value falls off a cliff in a few weeks. This is similar for business forecasts. Longer-term plans and budgets boast a greater shelf life, at least until internal and external business conditions affect the validity of the assumptions upon which those plans are based.

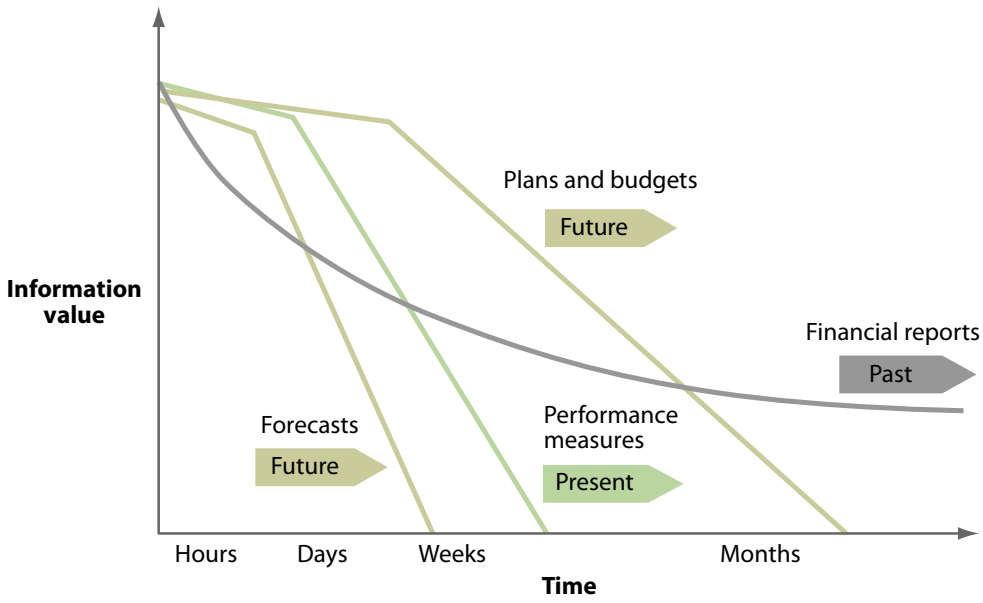
Accounting and financial reporting offer longer-term value because it creates a historical record of financial performance. Even so, financial BP pros should look to accelerate these processes to produce information more quickly, because fresher information translates into more actionable and value-added decisions. If you can accelerate the financial close-to-reporting cycle, financial results will provide increased relevance and value to help the business run more effectively.

Figure 1 Financial Process Strategies Must Integrate Across Time Dimensions



59381 Source: Forrester Research, Inc.

Figure 2 Financial Information Value Erodes At Varying Speeds



59381 Source: Forrester Research, Inc.

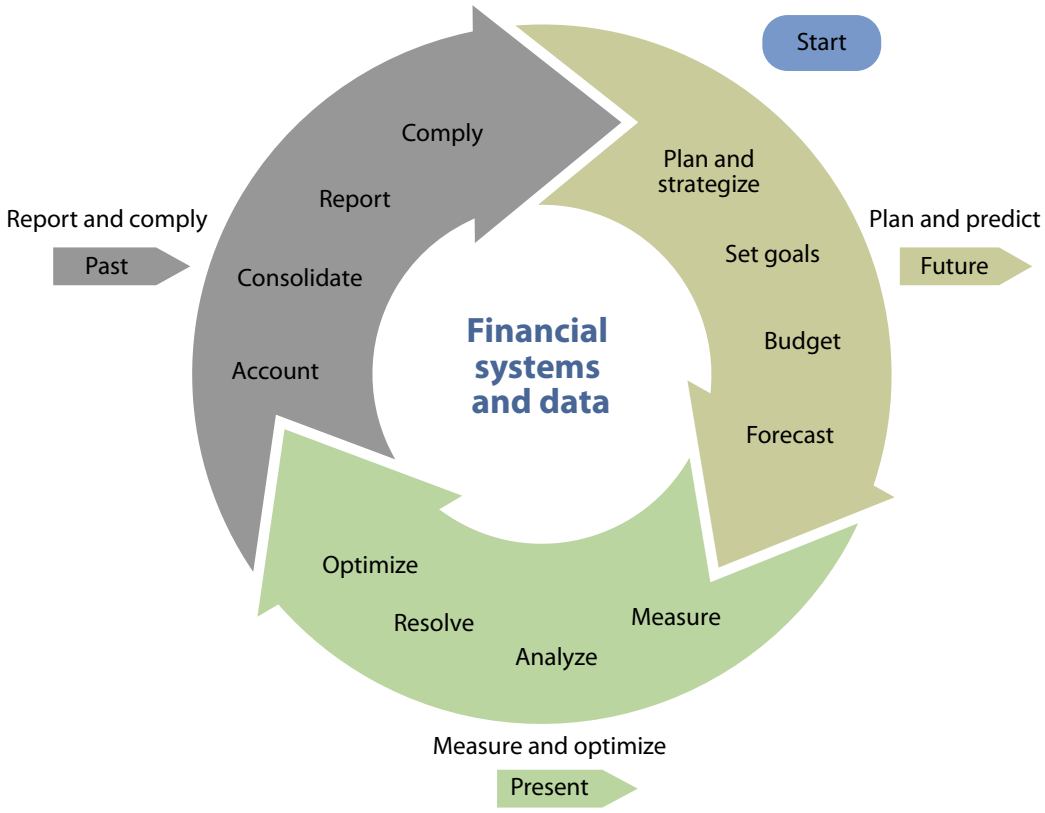
The Financial Process Life Cycle Is A Continuum Of Processes Across Time Dimensions

The financial process life cycle is a recurring set of activities that includes planning, measurement, forecasting, analysis, and reporting (see Figure 3). Optimizing the integration and coordination of this universe of processes into a coherent systems architecture enables better business decisions.

Companies that fully integrate this set of related activities will achieve significant benefits in efficiency, business insight, internal control, and predictive accuracy, leading to improved business performance. Doing this in an integrated fashion allows process and information alignment across the three dimensions of time and better coordination between accounting, reporting, performance measurement, and planning activities.

The frequency of these underlying processes varies; some are daily, monthly, annual, etc., and you don't actually iterate these processes in sequence. Nevertheless, these processes often leverage a considerable amount of common underlying data. For example, financial BP pros base plans and budgets on understanding historical financial results; performance analysis draws insights from transactional patterns; financial reporting summarizes and distributes actual results from historical transaction streams. Successfully executing the processes around the FPLC, therefore, depends on a set of common data elements and efficient and timely data integration. Without this integration, BP pros in finance, accounting, and operational lines of business will create spreadsheets and other manual workarounds to drive business process outcomes.

Figure 3 The Financial Process Life Cycle (FPLC)



59381 Source: Forrester Research, Inc.

HISTORICAL PROCESSES ENCOMPASS ACCOUNTING, REPORTING, AND COMPLIANCE

In the realm of accounting, a complex set of requirements exist that emanate from accounting standards and procedures such as US GAAP and IFRS as well as from regulatory requirements related to controls, integrity, financial reporting, and disclosures. Key business process requirements in this past dimension include:

- **Closing the books quickly and accurately.** The more quickly the books can be closed each period, the better the opportunity for management at all levels to access and react to timely information about business results. Accuracy and consistency of the closing process can't be sacrificed, however, based on the strict accounting rules discipline.

- **Delivering management reports to the business.** Business unit managers and executives rely on accounting information to understand the health of the business in terms of profitability, growth, cost controls, and other financial and operational measures.

- **Meeting regulatory reporting requirements.** Quarterly and annual results are key milestones for disclosing annual results to the investor community for companies whose securities trade on public exchanges. In addition to the financial statements themselves, detailed disclosures are required as part of regulatory filings (e.g., US 10-K and 10-Q SEC filings).

- **Managing internal controls.** SOX requirements for internal controls within US public companies (i.e., those whose shares are traded on public securities exchanges) call for monitoring of financial processes to minimize errors and reduce the likelihood of fraud. Similar requirements exist in other geographies as well as among many public sector organizations.

Best Practices In Accounting Focus On Consolidation, Automation, And Integration

Financial accounting, reporting, and disclosure management requirements focus on best practices for achieving better business result by consolidating disparate systems, automating labor-intensive processes, and modernizing systems integration using real-time technology. These best practices are accomplished by:

- **Consolidating disparate and redundant systems to a single global instance.** As companies grow via acquisition, acquired accounting and ERP systems often remain in place for many years. By consolidating these systems to a single global instance, financial information will flow more quickly and higher levels of standardization can be achieved in processes and transactional classification (i.e., the Chart of Accounts).

- **Automating manual and spreadsheet-based processes.** Manual and spreadsheet-driven financial processes still exist to a significant degree in a number of areas, including account reconciliations, preparation of regulatory filings, expense reporting, and internal controls management. BP pros should leverage highly functional packaged applications — often available through a SaaS deployment model — to manage and automate such labor-intensive processes.

- **Modernizing systems integration.** Since the accounting system is a mission-critical transactional hub, industrial-strength integration technology should be used to drive the close-to-report process. Using web services technology, BP pros can orchestrate system interfaces so that data flows virtually real-time, replacing existing batch interfaces. State-of-the-art data and process integration will enable the accounting system to support daily performance measures, for example, rather than optimizing process frequency for end-of-month reporting.[2]

THE PRESENT DIMENSION MEASURES THE HEALTH OF THE BUSINESS

Business performance management consists of a set of processes, frameworks, and systems for planning, measuring, communicating, and monitoring business results. These activities are typically closely linked to corporate strategies and objectives and might be driven down to many individuals within an organization to encourage accountability and control.

The challenges and requirements for business performance management also include:

- **Determining the right measures to put in place.** "How's business?" is a loaded question that needs to be put in its proper context of relative performance. Measuring performance includes how the company is performing relative to its peers, prior periods, the strategic goals set forth by the overall strategy, and leading indicators that help predict how the company will perform in the future.

- **Overcoming resistance to change and measuring its effect on individual performance.** Any initiative to drive change in an organization, even if mandated from the top, faces natural resistance. The phrase "you are what you measure" highlights the importance of measuring individual performance and its behavioral implications. Actually putting results measurements into play is the best way to gauge how the change affects employee behavior, so trial-and-error tweaking may be necessary.

- **Making performance information accessible and transparent.** Transparency of measures allows workers and managers to understand how their performance compares with that of peers in addition to how they track against their own goals. Such openness and accessibility of performance measures also encourages working toward common team-based and company goals and reinforces the connections between individuals and their contribution to company success.

- **Plumbing integration among internal systems.** Effective systems integration is of paramount importance to delivering useful performance information. Timely measurements of how the company is performing *right now* enable early warnings and corrective actions for results that are below expectations and for recognizing business opportunities for situations where measures exceed expectations.

Best Practices In Performance Measurement Focus On Strategy And Culture

The economic crisis of the past few years continues to linger and highlights the need for companies and government organizations to improve focus on monitoring business results and taking appropriate action to keep the business on track. Despite a large body of knowledge and best practices concerning business performance management, many companies still struggle to put appropriate processes and technology solutions in place. Business performance strategies require executive leadership, a clear and structured business strategy, organizational commitment, process maturity, and technology to deliver results.[3] To accomplish this, BP pros must:

- **Define strategic performance measures aligned with business execution.** Business leaders must articulate the corporation's vision and strategy and create a framework for translating the strategy into executable initiatives. Top-level sponsorship and involvement helps create a sense of urgency and importance that can help energize the notion of business performance management.

- **Create a performance-driven culture around people.** In a performance-driven environment, everyone focuses on business performance measures and can see how their contributions support individual, team, business unit, and company objectives. The people aspects of business performance focus on encouraging positive behaviors, including collaboration, and are supported by appropriate rewards and incentives.

- **Formalize business processes for analysis and action.** Key business processes for performance management include establishing goals and objectives, measuring achievements, and analyzing business fundamentals, including costs and profitability. "Days sales outstanding" (DSO), for example, is a common and useful measure to assess the time required to convert receivables to cash. Predictive measures such as lead-to-close times and sales conversion rates are useful for predicting revenues.

- **Put technology in place to deliver actionable results.** Financial BP pros must engineer the delivery of performance information visually, using dashboards and other graphical means. These dashboards should allow a user to explore the data to understand the details that are causing red flags and how to respond to business problems. Anomalies in production backlogs, for example, may reveal unforeseen capacity constraints.

FUTURE-ORIENTED PROCESSES PROVIDE PREDICTIVE VISIBILITY AND FISCAL DISCIPLINE

In the future dimension, companies have several important process requirements to effectively plan, guide, and predict future business results. In our research on business performance solutions (BPS), we find that leading planning solutions are versatile modeling tools that support multiple types of financial planning processes.[4] Spreadsheets are too often used for these planning processes, but these fall short in their ability to aggregate and manage large amounts of data and scale to multiple users. The key types of planning process requirements include:

- **A budgeting process that documents business expectations and controls spending.** Budgeting is a time-consuming process that consumes months of preparation time and numerous planning meetings. While alternative processes and philosophies have emerged, budgeting remains a common corporate practice (and mission-critical practice in government) to institute rigorous constraints on spending and cost control.

- **Forecasting processes that range from collaborative to predictive.** Forecasts are a more nimble process than budgeting, and financial BP pros use them widely to predict business outcomes more than guide and control. The methods vary not only across industries but company departments. A collaborative process may be used to predict sales pipelines, for example, and more elaborate predictive models using advanced analytical tools are common where extensive data is available.

- **A framework for evaluating business scenarios and initiatives.** Scenario-based planning is another process that is used by finance professionals to assess a range of "what if" scenarios, as well as to model the impact of strategic moves such as acquisitions and divestitures. Complex and detailed models are typically created to examine the financial implications on resources, cash, and equity.

- **Creating long-range strategic plans to guide the company.** Long-range planning typically falls into the executive domain, where strategies are analyzed to model the long-range evolution of the business. These plans are typically much less detailed than budgets but span multiple years and assess the effects of strategic initiatives shaping the business.

Best Practices In The Future Dimension Include Collaboration And Predictive Tools

Our discussions with vendors and buyers, and our analysis of software market trends, indicate that investment in planning solutions is strong, significantly outpacing investment in core enterprise applications such as ERP. A significant part of this growth is driven by economic uncertainty, where the ability to plan and forecast is even more critical to running a business. Best practices in planning include the following:

- **Engineer planning processes that are continuous and collaborative.** Collaborative forecasting is an emerging trend that involves larger numbers of users with frontline visibility into revenue and expenditure patterns, including specific sales deals and opportunities that should be reflected in revenue forecasts. Once a forecasting process is moved to a collaborative, real-time environment, it can become continuous rather than periodic.

- **Increase the agility of the budgeting process.** Budgets are too often cut in stone and inflexible, but business conditions and planning assumptions change frequently. Many companies adopt a process of monthly rolling budgets, with resource reallocations to reflect changes in business. Some companies embrace even more agile processes based on forecasts and performance measures in lieu of the traditional budgeting approach, a movement known as "Beyond Budgeting."[5]

- **Improve systems integration that enables the comparison of actual and plan data.** Integration of financial systems and processes across the scope of the FPLC is essential to gain insights into business performance results and to validate plans. Actual results and performance measurements are compared with plans to analyze variations from plans (a long-standing management accounting practice) and to address these variations via corrective actions. Effective system integration automates variance analysis and allows for the use of effective graphical visualizations and data exploration.

- **Leverage advanced forecasting tools incorporating predictive analytics and industry data.** Predictive analytical and forecasting tools are useful for creating sophisticated models based on statistical algorithms and quantitative methods. More recently, the ability to consume and process massive amounts of data via in-memory computing architectures allows the increased use of external data that may impact business operations, such as climate conditions, traffic patterns, and retail sales.

RECOMMENDATIONS

USE TECHNOLOGY TO DRIVE THE BENEFITS OF AN INTEGRATED FPLC

Address financial performance life cycle activities from a technology standpoint as a continuum of related processes. Even in the best-run businesses there are opportunities to improve the accuracy, timeliness, and flow of information. Financial processes must support efficient internal business processes, enable lines of business to gain insight into financial performance, and provide performance and planning support to top management. In addition, BP pros should:

- **Assess the health of your financial systems and processes.** This means take inventory of all the accounting, reporting, planning, and performance measurements systems and assess the gaps in integration and process automation. From this assessment, develop a long-range vision for your financial systems that span the three dimensions of time — past, present, and future. Finally, develop an actionable road map to meet critical business needs; also factor compliance imperatives into the timing of your road map.
- **Consolidate your accounting and reporting systems.** The objective of having a single instance for the entire enterprise is to optimize the flow and summarization of financial results at lower costs. If you get there, you will speed summarization, simplify integration, reduce compliance risk, and avoid the costs associated with maintaining multiple applications and interfaces. Companies with many smaller units may want to consider a two-tier strategy, where cost to deploy enterprise systems in these units is prohibitive.
- **Integrate processes to improve information value.** The value of the information increases as timeliness of delivery is optimized to the process requirements. Analyze the effectiveness of financial systems integration across the entire FPLC and replace legacy batch integration with web services-based (SOA) integration. Additionally, develop a financial systems data hub as an integration exchange and repository for reporting and analysis.
- **Put a framework in place for performance measurement and results accountability.** Instill a discipline for business performance measurement and a measurement framework that combines strategic alignment of performance measures, accountability and ownership of results, rewards for achievement of goal, processes to react to results, and technology to make the performance consumable across a variety of business stakeholders.

WHAT IT MEANS

AGILE FINANCIAL PROCESSES ENABLE COMPANIES TO PERFORM BETTER

Companies that transform to agile and integrated financial performance systems and processes will achieve improved business results and potentially realize competitive advantage over their peers. This transformation has already begun, and approximately half of the Global 2000 companies will adopt this integrated life-cycle approach to financial management during the next three years. Packaged software, which is critical to achieving this transformation, is evolving toward a complete end-to-end financial life-cycle solution, but gaps remain in these solutions. Integrated software solutions from leading enterprise applications and business intelligence (BI)) vendors will evolve to support financial performance life-cycle processes within the next two years, and they will continue to evolve beyond this time frame with increasing levels of industry-oriented support.

ENDNOTES

[1] Forrester's survey data from 913 IT decision-makers related to 2011 investment plans for finance and accounting software with shows that 6% are planning to implement within the year and 22% are planning to upgrade or expand their finance and accounting implementations. See the February 18, 2011, "Trends 2011: Financial Processes And Applications" report.

[2] Integration trends and technologies are examined in more detail. See the April 8, 2011, "Seven Top Integration Trends For 2011 To 2012" report.

[3] A best practices framework assessing business performance readiness is available in this report. See the April 2, 2008, "Measuring And Aligning Business Performance" report.

[4] Planning solutions, along with financial reporting and consolidations, cost and profitability management and performance measurement solutions are evaluated. See the November 19, 2009, "The Forrester Wave™: Business Performance Solutions, Q4 2009" report.

[5] Source: Jeremy Hope and Robin Fraser, *Beyond Budgeting: How Managers Can Break Free from the Annual Performance Trap*, Harvard Business School Press, 2003. The Beyond Budgeting Roundtable is a member organization that was established prior to the publication of the book and continues to promote its concepts via events, publications, and its website (http://www.bbrt.org/).

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