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The Financial Close: A Key Financial Control Process

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IDC research shows that the financial close is a key area that is marked by a lack of automation as well as cited by auditors as having control weaknesses. Organizations can improve this process and decrease risk through the use of software.

The following question was posed by IBM Cognos to Kathleen Wilhide, research director of IDC's Compliance and Business Performance Management Solutions practice, on behalf of IBM Cognos customers as part of the company's analyst series *Controllers' Corner: Two-Minute Essays on Financial Management and Control*.

Q. How can organizations increase financial accountability by integrating the financial close process with internal control compliance requirements?

A. Pressures are weighing on finance teams, despite their best efforts; Sarbanes-Oxley has taken the financial close process one step further, forcing organizations to review and document all of the internal controls surrounding operational processes that impact financial results. A recent review of material weakness disclosures reported to the U.S. Securities and Exchange Commission (SEC) revealed that operational finance issues and the application of accounting policies during the closing process represent more than 30% of reported disclosures. It is important that organizations conduct the closing process with controls that ensure accountability and risk mitigation along with the reporting of financial results, and do so in an auditable system of record. Currently, the handoff of information during the closing process results in a transfer of accountability that directly conflicts with the mandates of corporate governance such as Sarbanes-Oxley. Internal control reviews, testing, and sign-offs are treated as disconnected processes, out of context with key financial assessments and reviews on a regular basis. This increases the likelihood of weaknesses that impact financial results.

Clearly, the attestation, certification, and reporting/disclosure processes are loosely connected to the financial close on a quarterly basis and an annual basis. However, there are many opportunities to integrate control activities on a more regular basis by linking relevant activities to monthly closing tasks. This accelerates visibility of issues and reduces the burden during quarterly reviews and year-end audits. More importantly, more regular integration of control activities increases reliance on operational processes versus the burden of compliance being treated as a fire drill.

IDC research shows that many organizations have experienced a 60% increase in audit fees driven by compliance legislation and a 150% increase in fees when material weakness is found. For large enterprises, these costs run into the millions of dollars, despite efforts to control costs via client-prepared work papers. The potential to save audit fees by implementing a system of record that incorporates financial results, controls, analysis, documentation, and approvals is realistic. Organizations can embark on an initiative to integrate and coordinate the financial close process and internal control reviews through the use of technology. When the features of compliance management applications are integrated with financial consolidation and reporting, the close process can become a system of record that is more complete and auditable.

Finance organizations need a visionary model for finance transformation to make clear and valuable contributions to the success of the business while meeting compliance requirements. Finance can leverage IT to achieve operational efficiencies while also freeing up time for more strategic, value-added analysis. When companies integrate internal control reviews and financial statement preparation into a cohesive, unified, and automated process, they are one step closer to making compliance operational, increasing visibility, and allowing timely remediation of risk. Automating and integrating the financial close and control review process eliminates control gaps, reduces reporting timelines, and increases efficiency and accuracy.

Automating processes and controls will be an increasingly important part of compliance programs. As software solutions evolve to address compliance requirements, auditors will rely on these systems of record. Just as important are the core improvements that these solutions contribute to excellence in finance. For many enterprises, the value proposition for investing in solutions increases significantly as they consider sustainable compliance objectives within the context of broader finance optimization. Integrating the internal control review and financial closing process is the logical next step to achieving what will be defined in the longer term as an office of finance best practice.

ABOUT THIS ANALYST

Kathleen Wilhide is a CPA and is the research director for the Compliance and Business Performance Management (BPM) solutions practice at IDC, a worldwide research firm with headquarters in Framingham, Massachusetts. Ms. Wilhide directs IDC's research efforts on software solutions supporting compliance and risk management and related business assurance processes. Ms. Wilhide also directs the research for BPM applications and participates on teams related to general enterprise applications research, with a focus on enabling finance and corporate governance through technology.

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