

A Director's Guide to Compliance Software

BY DAVID SHAW

AN EXECUTIVE of our acquaintance — a longtime member of multiple public company boards — looked at us during a recent meeting with the DIRECTORS & BOARDS team.

“Enterprise compliance software,” he said. “What is it? Why do I need to know about it? And what do I need to know about it?”

That’s not an uncommon set of questions among corporate board members this year.

If the company you serve as a board member is like most, it’s probably grinding away toward meeting the first Sarbanes-Oxley Section 404 filing deadlines (Nov. 15, 2004, for most companies with market caps of more than \$75 million, and July 15, 2005, for others). But, also like most others, your company may be setting itself up for continual compliance grief and cost, because there’s something missing: a strategic enterprise-wide compliance software solution to help the company manage both getting to compliance and, more important, staying there.

The decision to invest in enterprise compliance software has become yet another item for the board member’s agenda. Board members probably won’t be — and shouldn’t be — reviewing individual vendors, but they should know enough about

possible compliance solutions to ask the right questions of their company’s executive, financial, audit, and IT teams. What can and should a company expect from a compliance software solution? And can the company measure and achieve a return on the not-insubstantial investment such a solution entails?

This “Director’s Guide to Compliance Software” provides a non-technical overview of the critical issues a board should be addressing and a punchlist of questions that should be asked by the board. In compiling this Director’s Guide, we spoke with representatives from seven compliance vendors to seek their insights into non-technical issues regarding the decision to implement a compliance software solution. There are many more such vendors out there, as

well as a number of analysts and consultants. Each can bring a unique perspective to the question.

Background Noise

Vendors of compliance solutions are looking for business from your company, and many bring solutions from a different perspective — document management, business process management, contract management, enterprise resource management, e-commerce, audit tools or programs built solely around compliance.

“Vendors are coming at compliance from a variety of angles,” notes Dan Ryan, executive vice president of marketing and business development for Stellent.

The right angle for your company will depend on a number of factors, but as a board member, you should be asking questions to ensure that your financial, audit, and IT teams are considering not only the near-term goal of reaching attestation, but the more long-term goals of continuing compliance and, ultimately, generating a return on investment from the cost of compliance.

“There are too many controls, which makes it impossible for a manual system to do the job unless you want to double or triple the size of your finance organization,” says Eric Keller,

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CEO of Movaris. “And there’s a lot of choice. I encourage directors to ask questions. You don’t have to settle for something that just does a piece of the job.”

Compliance software vendors are beginning to reach out to boards to communicate the benefits of enterprise compliance software. “Virtually every board is talking about SOX 404



Dan Ryan of Stellent: ‘Compliance software is different from a typical IT initiative.’

requirements and the ongoing management of risk and the cost of compliance,” says Renee Lorton, senior vice president and general manager of PeopleSoft Financial Management Solutions.

After attestation, then what?

At a recent PeopleSoft leadership conference, Lorton polled approximately 350 companies in attendance. Some 65-75% have gone through what she terms the “first wave” of compliance — documenting internal controls, understanding those

controls, deciding standards, and getting it all on paper.

“Now these companies are realizing that SOX doesn’t go away after the first audit, with all of the manual effort that went into getting there,” Lorton says. “Now it’s going to take some automation to lower risks, keep costs down, and meet the demands of the quarterly audit. SOX will be a quarterly exercise until the end of time, or a change in the law.”

If you’re like most directors, you have a right to be suspicious of enterprise compliance software. As with many IT investments you’ve reviewed, it can be expensive, and ROI is hard to measure directly.

The bad news, according to Vani Kola, president and CEO of Nth Orbit, is that “at least 80% of companies will have to redo their SOX effort, because the first time they did it, they didn’t do it in a leveraged, sustainable manner. Only a few boards looked at it as a long-term challenge, and not a one-time thing.

“How did boards get this wrong?” muses Kola. “Did they ask about software tools? I think many boards let this happen because they didn’t get involved in thinking about software. We made an emotional decision to focus on the Big Four for tools. Now, the second time around, let’s make sure we’re asking the right questions.”

Tim Welu, CEO of Paisley Consulting, agrees: “There was a lot of poor guidance from outside auditors and consultants. Companies took the software tool their auditors were offering, and this caused as much grief as help. The Big Four have now realized they’re not in the software business, and that they don’t want to be.”

“SOX 404 requirements have been met with tools like Excel,

Word, 13-column paper or mom and pop software solutions,” adds Phil Strand, global strategist and program director for financial intelligence and corporate governance for SAS. “Now you need something sustainable and scalable across the enterprise.”

Setting the tone

The most important role that boards can play in the enterprise compliance software decision, software executives agree, is setting the corporate philosophy on compliance. “Is compliance about meeting a mandate, a minimum requirement, or do you believe that governance and compliance can be an asset for how you do business?” asks Nth Orbit’s Kola. “What is the culture of the company toward governance and compliance? The board plays a key role in shaping this perspective.”

Software tools, she notes, play a role — but only as effectively as the end goal the company is trying to achieve. “I think boards have to set the operational aspects of compliance from the perspective of the corporate philosophy on compliance.”



Phil Strand of SAS: ‘Now you need something scalable across the enterprise.’

What you should expect

Board members should expect a “solution which can give assurance that controls remain in place, and that people who are responsible for those controls can be held accountable,” says PeopleSoft’s Lorton. “This will allow directors to be sure that the company’s financial reports are accurate to the best of their knowledge.”

Says SAS’s Strand: “Directors should have some level of transparency shown in the financial organization. They should actually be able to read a report and not have someone translate it for them.”

Regardless of the compliance software your company ultimately chooses, there are elements that a complete solution should contain, according to Nth Orbit’s Kola. These include:

1) *Documentation.* Does the solution provide a structural business topography, in the context of the general ledger, balance sheet, fiscal year end, monthly closings, 10Ks, and so on? Does the solution track changes — when something changes, why did it change?

2) *Operational Effectiveness.* Does the solution manage workflow — monthly, quarterly, annually? Can a company look at transactions, and allow multiple people to do testing and assessments? Can a company store these transactions for auditing and evaluation in future?

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A DIRECTOR'S PUNCHLIST

Directors should be asking the following key questions about enterprise compliance software.

INTERNAL QUESTIONS

Does your company have a compliance vision and mission statement?

"Software is not the be-all and end-all of compliance," says SAS's Phil Strand. "You can't add software if the culture isn't in place. Integrity is either in your corporate DNA or it isn't. It starts at the top with strategy."

What is your company's plan to maximize its chances of meeting SOX requirements this year?

- What is the time frame for the project?
- What resources are required?
- How much time will be required of company personnel?
- How much consulting time will you use?
- Who's in charge of the project?

What compliance solutions do you already have in-house?

"There's a lot of hype and panic around SOX, and a lot of vendors are selling on that fear," says Click Commerce's Nancy Koenig. "But a lot of other solutions that you already have in-house might be helping you toward your compliance goals."

How can the company derive additional benefits from SOX and other compliance solutions?

"Compliance solutions should offer longer-term business value (e.g. more productivity, intelligent analytics, stronger efficiency, etc.) to garner more bang for your buck," says PeopleSoft's Renee Lorton.

SOFTWARE SOLUTION QUESTIONS

Is it a complete solution?

"Depending on the compliance solution, the software may address only one section of the Sarbanes-Oxley Act, which limits its value to your overall business," says Lorton.

What, if any, other software solutions will be needed to ensure compliance?

"There's a lot of noise and a lot of pretenders out there," says Paisley Consulting's Tim Welu. "Some companies might provide a component of compliance. The standards need to be there, and there needs to be flexibility, too."

Does the compliance solution enforce compliance with SOX 404?

"Many compliance solutions only offer monitoring and

documentation functionality but still require people continually to review the countless internal control points for failures," says Lorton. "There are new solutions on the market that offer diagnostic tools, which proactively alert appropriate managers of internal control failures, for immediate reaction."

Does the software address a company's indirect channels?

"When you look at the opportunities to miss your audit, look to places where you're selling products through indirect channels, where you're not engaged in a simple buy-sell transaction," says Click Commerce's Koenig. "Things like warranties, service agreements, and cooperative marketing — all are transactions where money changes hands, and are subject to SOX 404."

How compatible will the software be with existing software applications, and what will be the process for installation?

"Most compliance solutions claim to have integration with your existing financial management solutions; however, it requires lengthy customization," says PeopleSoft's Lorton. "Some compliance solutions offer pre-packaged integration that can speed up software installation."

What kind of training will be available to ensure that the software is understood and used?

"Even the best software in the world offers no benefit if users resist using it or are unsure how to maximize the various product benefits within the software," says Lorton.

VENDOR VIABILITY

What product support does the vendor offer?

"Does the software vendor provide software upgrades and how often?" asks Lorton. "It is important to know the vendor's long-term plans and commitment to the compliance solution you are purchasing, including frequency/time required for software updates that meet ongoing regulatory changes."

What are the vendor's expansion plans and R&D plans?

Will your software vendor be around five to 10 years from now?

"Currently, there is a lot of consolidation happening within the enterprise software market, and many of the smaller niche players may go out of business or be acquired," asserts PeopleSoft's Lorton.

What is the depth of the vendor's management team and board?

What do the vendor's customers say?

"Due diligence is easy to do, and a must," says Nth Orbit's Kola.

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3) *Monitoring and Reporting.* Does the solution have the reporting capability to look at information in multiple ways? Is the reporting flexible enough to make the data useful in the business context of your company?

4) *Project Management.* Does the solution allow the company to track what needs to be done to get the project finished on time?

5) *Transparency.* Is there external access to the data for auditors, the audit committee and customers? SOX requires that you must certify third parties if you outsource significant transactions.

6) *Storage and Retrieval.* Can a solution archive to meet statutory regulations?

Enterprise compliance solutions can help organize data and processes and track them successfully for SOX 404 compliance. “Software can have a dramatic impact on ensuring discipline,” notes Keller of Movaris. But it can’t do everything. “A compliance software solution cannot prevent fraud if you have high-level people in the organization involved in fraudulent activity,” acknowledges PeopleSoft’s Lorton. “But if you have a trusted executive team, a compliance software solution should be able to reassure board members.”

“Software isn’t the answer to compliance — it’s just a tool. Software can’t make you successful, fix your process problems or lack of resources in your finance organization,” says Nth Orbit’s Kola. “And while people expect software to reduce the human effort involved in compliance, it won’t take away from the dollars you should spend in effectively training and educating your organization on compliance issues.”

Return on investment

A year ago, ROI from compliance software seemed hard to measure. As an article on compliance software in *Baseline Magazine* in 2003 noted: “The return on investment? The exhaustive analysis of processes may generate some incremental returns, but few companies are expecting a windfall. For now, it’s simply a cost of doing business — one you’ll be sure to document and certify in your brand-new compliance system.”

But that’s changing. With AMR Research’s John Hagerty estimating that the costs of SOX compliance will grow to \$5.4 billion this year — double last year’s cost — and with the technology component of that cost increasing tenfold over the 2003 level, companies are now looking to squeeze measurable ROI from their compliance technology investment.

“SOX-related or not, a board should expect an ROI from any IT investment. Period,” says Nancy Koenig, vice president, product operations and marketing for Click Commerce. “And some of the IT investments you’re already making today might give you the means to achieve section 404 compliance at a greater ROI.”

PeopleSoft’s Lorton agrees: “In general, we look to measure ROI in terms of costs and savings. We focus on expense reduction, and dramatically reducing the time it takes to survey and monitor compliance.”

But as Dan Ryan of Stellent points out, “Compliance software is different from a typical IT initiative, because compliance itself is mandated. So part of the question is what’s the best way to reduce risk, not build ROI.”

“It’s tricky to measure ROI with computer solutions,” says Paisley Consulting’s Welu. “But you can measure the following: better visibility, better reporting, better understanding of the business, reduced manual effort, reduced testing and evaluation. If we do a good job with the tool, can we reduce the amount of time the external auditors have to spend internally? If you can cut that time, you’ll have a measurable ROI in reduced auditor billable hours.”



Vani Kola of Nth Orbit: ‘How did boards get this wrong?’

There are some different returns on investment that a company can measure, however. According to SAS’s Strand, the first can be reflected in the stock price: “Do investors feel comfortable with the information they’re receiving?”

And the second is whether SOX compliance is helping the company run more efficiently. “People are finding that the way they define processes isn’t the way they do business, so they’re changing the way they do business,” says Strand. “So how much more effectively can you run your company in the long term? It can be business process reengineering under another name.”

Agrees Dean Berg, director of business development for Stellent: “Directors are now looking at what they’ve learned from SOX 404 year one, to see how they can structure that project into a process, so it’s more a part of daily life. How can we take these processes we’re documenting and reengineer them for the most effectiveness and cost efficiency?”

After SOX 404 compliance

“Our general belief is that compliance is broader than SOX,” says Stellent’s Ryan. “Companies are going from only looking for SOX solutions to a framework for all of their compliance needs.”

Many vendors of compliance software solutions recommend that companies look forward to other areas of compliance when evaluating a solution. Will your company be able to track, manage and audit SOX Sections 103, 301, 302 and 403? Can the company also manage other compliance mandates, including HIPAA, OSHA, ISO 9000, The Patriot Act and the many others it may encounter in the course of doing business?

“In the end, you’ll have no choice but to automate,” says PeopleSoft’s Lorton. ■