

CONSOLIDATION

LAYING THE GROUNDWORK FOR
SUSTAINABLE COMPLIANCE



COGNOS®

THE NEXT LEVEL OF PERFORMANCE™

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INTRODUCTION

“We haven’t had time to think about much else. Strategic planning and new-product research have had to take a back seat to these requirements.”¹

Louis P. Valente, Chairman,
Palomar Medical Technologies

The *Sarbanes-Oxley Act*, signed into law in 2002, represents the most comprehensive reform of US securities law since the *Securities Exchange Act* was passed in 1934.

The legislation places a heavy burden on publicly held companies. This became all too apparent in the first year of implementation, as organizations deployed substantial resources, time, and effort to comply with Section 404 reporting and control requirements. The cost? An estimated US\$5.5 billion.²

With increasingly accelerated filing requirements and more expansive corporate governance mandates anticipated in the coming years, accounting and financial reporting practices must become steadily faster, more visible, and more accurate. Corporations will need to direct significant time and resources to the cause. In effect, complying with Sarbanes-Oxley has become and will continue to be a cost of doing business in the United States.

Other mandates are also gaining influence. The impact of International Financial Reporting Standards (IFRS), the challenges of US and other GAAPs, and the potential merging of related standards on a global basis will affect accounting and financial reporting practices in the coming years.

“Many businesses that thought of this as a “year 2000-like” remediation effort are being shaken to the roots of their corporate cultures by the realization that Sarbanes-Oxley compliance is an ongoing, high-cost event requiring previously unnecessary tracking and documentation of changes in business processes.”³

Gartner Research

¹ From “Is that a Ticking Clock or a Time Bomb?” *Corporate Board Member Magazine*: What Directors Think: Special Issue. November/December 2004.

² John Hagerty. “Compliance Costs Expected to Rise in 2005.” AMR Research. May 28, 2004.

³ Richard J. De Lotto. “Compliance is Essential to Running a Successful Business.” Gartner. November 14, 2004.

CONSOLIDATION: THE FIRST STEP IN SUSTAINING COMPLIANCE

“As US public corporations adapt to the more stringent regulatory climate, they must look for ways to enhance their control and reduce the cost of compliance. For many, the consolidation and closing process has the potential to do both.”⁴

Ventana Research

Compliance is a business reality for publicly traded companies in the US. But as the regulatory climate shifts from immediate response to long-term sustainability, many finance executives are hard pressed to know what the next step is. Where does the organization proceed from here? What are the priorities in terms of changing internal processes and technologies so they're repeatable and effective?

The first priority is to focus on improving the core systems that directly support financial reporting and accuracy. This means looking at the processes for gathering, consolidating, and reporting financial information results, and finding improvements to deliver the information in a more transparent, accurate, secure, and timely manner.

The goal is to have a consolidation and financial reporting system that helps businesses effectively manage their financials; reduce the risk factors for errors, fraud, and manipulation; lower the cost of compliance audits; and accelerate the closing and reporting process.

Reliable financial data is the backbone of compliance, and a robust consolidation system provides the foundation for accountability. And this is the jumping off point for delivering greater transparency and management of company performance—the broader, sustainable objectives going forward.

⁴ Robert Kugel, “Consolidation, Closing and Sarbanes-Oxley.” Ventana Research. February 2005.

KEY SECTIONS OF THE ACT AT A GLANCE

Section 302—

Corporate Responsibility for Financial Reports

- Certify truth and accuracy of annual report and other financial statements.
- Establish and maintain internal controls.
- Evaluate effectiveness and accuracy of internal controls; disclose significant deficiencies.

Requires that consistent information be accessible to all authorized users; linkages between operational and financial data to enable deeper accountability; and consistent, automated, and auditable closing and financial reporting processes to minimize errors and misstatements.

Section 404—

Management Assessment of Internal Controls

- Establish and maintain an adequate internal control structure and procedures for financial reporting.

Requires airtight and auditable transaction and compliance policies, guidelines, and related controls governing transaction systems.

Section 409—Real Time Disclosure

- Disclosure to the public, on a rapid and current basis, any information concerning material changes in the financial condition or operations of the company.

Requires proactive monitoring of material events that meet SEC disclosure criteria; enhanced report preparation and distribution capabilities that support accelerated disclosure; and real time disclosure of changes in the financial condition of the business.

“Spending will continue to increase in 2005 as companies move from a tactical attack to an ongoing process. As more companies—small cap firms and foreign registrants—enter the SOX fray in 2005, it’s apparent that this issue will be with us for some time to come.”⁵

AMR Research

Addressing the Consolidation Challenge

Meeting the consolidation challenge is difficult because organizations use manual, inadequate, or multiple consolidation systems for their financials. The result: they are unable to structure, control, and automate the process for internal and external reporting, and are unable to gain a single, accurate view of financial results.

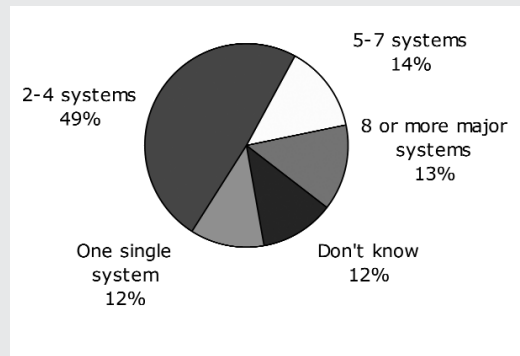
THE IMPACT OF IFRS

As of 2005, listed companies in all European Union countries are required to prepare their financial statements in accordance with International Financial Reporting Standards (IFRS), developed by the International Accounting Standards (IAS) Board. These standards are also being adopted in other nations around the world. The United States is considering convergence of US GAAP standards with IAS/IFRS requirements to stay in step with the trend toward international regulation.

Under the IFRS, companies are required to provide financial statements that fairly disclose their financial position, performance, and cash flows. The goal is to increase financial transparency by setting more comprehensive reporting requirements. This will make it easier to analyze and compare financial performance around the world. IFRS will necessitate changes to existing accounting policies, including segment reporting and financial instruments.

⁵ John Hagerty, Fenella Scott. “Final SOX 2005 Spending Forecast: \$6.1B.” AMR Research. December 16, 2004.

Number of Major Systems Used to Pull Financial Information⁶



ERP Systems

Enterprise resource planning (ERP) and ledger systems are excellent for storing data and managing the transactions that support the business. Companies typically have an array of ERP and other financial data systems, ranging from state-of-the-art solutions to legacy and proprietary data systems.

Unfortunately, ERP and general ledger systems are not designed to easily integrate or consolidate data from other sources. To produce appropriate financial statements, a single aggregated view across all transactional systems is required. As well, these systems do not provide all the necessary consolidation functionality. To ensure the closing process is timely and accurate, the system must handle all the complexities of consolidation—such as currency conversion and inter-company eliminations. What’s more, it is not flexible enough to manage the accounting of business changes—such as mergers and acquisitions—in a timely manner.

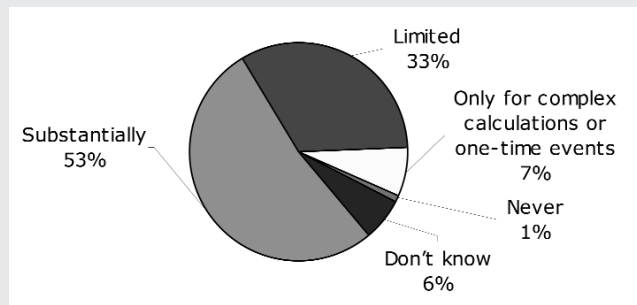
Spreadsheets

Spreadsheet systems are widely used for accounting and financial reporting. But multiple spreadsheets make each person or department an island of report information. This can lead to duplicated effort and opens the door to inconsistent data interpretation. Who has the right numbers?

In the Sarbanes-Oxley era, internal control risk is directly linked to the degree of spreadsheet use within an organization. Spreadsheets drive unacceptable rates of input errors—from data entry, re-keying, and cut-and-paste activities. Security of spreadsheets is inherently problematic, since communication of information is via emails or shared drives. As well, auditing of spreadsheet content is virtually non-existent, since there is no systemic ability to track who received what information or who made which changes to the data.

As with ERP systems, spreadsheets also lack sophisticated consolidation capability. They don’t have the necessary level of sophistication needed to calculate and track important functions such as inter-company adjustments, business changes, and other journal entry changes.

Use of Spreadsheets in the Closing Process⁷



⁶ “Financial Reporting and Consolidation: Taking Performance to the Next Level.” Sponsor Report. Ventana Research 2005.

⁷ Ibid.

First-generation Consolidation Systems

First-generation consolidation systems are a major improvement over spreadsheets. These systems integrate financial and operational data, consolidate financials at each level, and allow closing of the books quickly and effectively. Many provide allocations, eliminations, and currency conversion to further accelerate the process.

While these systems have addressed many of the fundamentals and core tasks, they don't address some of the more leading-edge issues: how to address company restructurings and other material business changes in real time, how to provide the required set of accountability and audit controls demanded in the current climate, and how to seamlessly adapt to evolving accounting standards and global business requirements.

Other limitations of first-generation systems:

- Not multidimensional—the inability to link dimensions (such as product, customer, or region) limits views into the business and curtails reporting and tracking performance.
- No auditability or data submission certification capability. Regulatory mandates demand a greater degree of security for certification and collection of submissions from other parts of the organization. This capability is not supported in current systems.
- Each deployment is optimized for one country or accounting regulatory environment, making it difficult to achieve integrated, multi-jurisdictional reporting.
- These systems are often supplemented by spreadsheets and manual intervention, approaches that are no longer viable in this era of compliance.

COMPLIANCE CALLS FOR A BETTER SOLUTION

“Companies should examine the magnitude of savings (measured in internal headcount and external audit fees) they would be able to achieve by automating more of the consolidation and closing processes.”⁸

Ventana Research

Using manual and inadequate consolidation systems creates inefficiencies, exposes the process to errors, and increases compliance costs. Such systems negatively impact the bottom line, as businesses sacrifice performance initiatives to instead direct time and resources toward fixing errors and re-working the numbers. This can lead to further inspections, audits, and restating of financial statements, which drive expenses even higher.

In the current regulatory environment, companies need a consolidation system that streamlines processes, ensures accuracy, and helps control costs. It is essential that the system deliver in these areas:

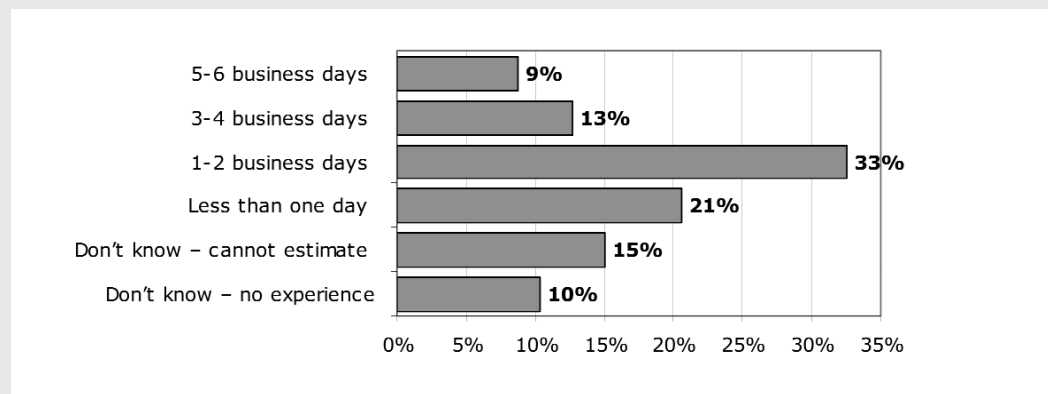
- A single, centralized platform for all processing and calculations. It is no longer appropriate to provide supplementary processing with multiple systems, spreadsheets, and people.

- Financial reporting from a single version of the truth. Reporting must also support delivery of many styles and types of reports – for example, producing reports across multiple GAAPs – and providing a line of sight from management reports to financial statements.
- Future-proofing of consolidations. As requirements such as IFRS enter the fold, systems need to be able to handle the different consolidation and reporting complexities driven by common accounting standards and reporting.

“A sustainable and affordable compliance framework must be underpinned by appropriate IT systems.”¹⁰

Gartner Research

Impact of Errors in Prolonging Close⁹



⁸ Robert Kugel. “Consolidation, Closing and Sarbanes-Oxley.” Ventana Research. February 2005.

⁹ “Financial Reporting and Consolidation: Taking Performance to the Next Level.” Sponsor Report. Ventana Research 2005.

¹⁰ C. Rozwell, J. Bace, L. Leskela. “Compliance Management Solutions Can Create Improved Business Performance.” Gartner Research. January 17, 2005.

- Adaptable to business change. The current pace of business requires a new degree of agility and nimbleness in finance. Companies need to quickly incorporate the latest information for analysis or to identify scenarios for mergers and acquisitions. As organizations add and divest new entities, financial results must reflect these changes in a timely manner.

“Technology will play an increasingly strong role in making compliance activities repeatable, sustainable, and cost effective in the mid- to long term.”¹¹

AMR Research

¹¹ John Hagerty. “Compliance Has Many Faces.” AMR Research. November 5, 2004.

INTRODUCING COGNOS CONTROLLER

Cognos Controller provides built-in financial intelligence and advanced analysis capabilities to deliver on today's consolidation requirements. The Web-based platform provides centralized, synchronous financial consolidation. It compresses the time to close, ensures accuracy, and ensures that the business controls directly impacting your corporate reporting process are effective.

“Our use of the Controller product has allowed us to consistently produce consolidated reports at the speed our business demands.”

Ross McEwan, Head of Finance & Actuarial Systems,
AEGON UK

You gain true and reliable consolidated financial data, based on a clear link between statutory and management consolidation, which provides a solid foundation for your operational and strategic decisions.

Cognos Controller gives you a many-fold advantage in addressing compliance needs:

- Automates the consolidation process.
- Compresses closing times.
- Accelerates reporting times.
- Significantly reduces the risk of financial reporting errors.
- Minimizes compliance costs.

“The multi-dimensionality of Controller offers enormous potential. It provides us with excellent support for our extensive management reporting. All necessary eliminations and adjustments can be performed at an operative level as well as at an organizational level to reflect the current structure.”

Sweden Post

KEY FEATURES

- **Application approach** – Directly managed by finance, not by IT, for rapid implementation. Eliminates extensive development and programming that adds complexity. Simplifies and automates the definition, structure, and rules of the consolidation process.
- **Single, accurate, corporate view of key information** – Consolidates multiple, diverse ledgers with thousands of operating units and accounts into a single, common, chart-of-accounts structure.
- **Sophisticated, global consolidation functionality** – Provides inter-company elimination and reconciliation, multi-currency translation, complex ownership calculations, and financial consolidation rules to handle multiple reporting and consolidation standards.
- **Leverages existing assets** – Integrates data from existing ERP, transactional, and desktop systems.
- **Provides reporting and analysis on controls and transparency into information** – Mitigates risk and delivers accurate information to support compliance requirements.
- **Built-in finance consolidation intelligence** – Includes pre-defined consolidation functionality and reports that incorporate best practices for managing the consolidation of financial information and delivering external management and corporate reporting.
- **Adaptable to unique requirements** – In addition to statutory dimensions, Cognos Controller provides user-defined dimensionality to support collection and reporting at all levels including cost center, product, and customer.
- **Real-time adjustment to meet new business, environment, or legislation changes** – Easily and rapidly accommodates changes such as mergers and acquisitions as well as reorganizations.

PERFORMANCE MANAGEMENT: THE NEXT STEP

“The basic architecture and infrastructure for gathering compliance-related information can be easily extended to provide better business management. Extending the information gathered and analyzing it will help manage key risks. To mitigate the cost of compliance, companies must look for and execute the leverage points that improve business performance.”¹²

Gartner Research

Consolidation provides the foundation for accurate, validated, and auditable financial information. To achieve greater transparency and improve business performance, Cognos Controller can be linked with Cognos enterprise planning, business intelligence, and scorecarding through a single corporate performance management (CPM) platform.

Enterprise Planning

The visionary CFO strategically thinks about the financial data environment across all time horizons. Financial consolidation delivers the validated, historic results. This creates the starting point for business planning and rolling forecasts—the forward-looking view of the business. Effective planning drives higher levels of predictable financial and operational performance. In terms of compliance, predictability results in fewer regulatory and investor surprises.

Cognos enterprise planning translates corporate objectives into concrete financial and strategic plans. It links operational plans to financial plans, allowing users to see in real time the effects of operational changes on the financial bottom line. Cognos planning is optimized for high participation, high frequency, driver-based planning and forecasting, and it leverages data from the historic perspective to enhance the forward view of the organization.

Business Intelligence

Companies amass large amounts of operational and business data, but it is locked away in disparate systems. As a result, critical information is inaccessible and underutilized. Cognos business intelligence lever-

ages the information assets within your organization, giving you insight into the Why behind financial, operational, and business performance.

This visibility provides greater transparency, allowing you to drill-down to the root cause of errors and events, and address them systematically. Addressing cause and effect ensures accountability and improves business performance.

Cognos scorecarding lets you define and monitor critical success factors and measure progress against plans and strategic targets. With this capability, you can identify shifts in trends, model alternative plans, and where necessary, take appropriate action in time to improve performance.

“We drive our corporate performance through global sales forecasting with support from Cognos Enterprise Planning. Key figures in our planning processes need to be integrated with other important data, such as financial and non-financial data that has been reported and processed using the Cognos consolidation solution. The link between these two solutions ensures that we have an overall picture for performance management purposes, as well as the ability to examine a detailed breakdown of key figures.”

Ola Salmén, Chief Financial Officer
of the V&S Group

¹² C. Rozwell, J. Bace, L. Leskela. “Compliance Management Solutions Can Create Improved Business Performance.” Gartner Research. January 17, 2005.

COMPLIANCE AND GOOD BUSINESS PRACTICE

The *Securities Exchange Act* of 1934 was enacted with two basic purposes: to improve disclosure to investors and to prohibit fraud in connection with the sale of securities.¹³ The Sarbanes-Oxley Act shares the aims of the 1930s legislation. It reinforces what many have been pursuing as good business practice for years.

The Act's various sections reinforce investors' need for appropriate levels of transparency into the operations and financials of companies where they invest their money. This transparency enables true accountability, and in turn, leads to better decisions and management of company performance.

"Today, as business fundamentals and credible accounting become the new touchstones by which investors judge corporate quality, many companies would benefit if their CFOs gave renewed attention to helping chief executive officers understand the performance of their businesses and to evaluating critical strategic decisions," write Timothy Koller and Jonathan Peacock in the *McKinsey Quarterly*.¹⁴

Compliance is a critical driver for publicly traded companies. But improving business practices is just as relevant for private companies. With corporate performance management, you can gain greater visibility into your business, achieve greater accountability, and drive greater predictability and performance.

These objectives are key to business success, whether you are a private or public organization. And ultimately, an investment in performance management will also give your company a true competitive advantage.

For more information on Cognos corporate performance management, visit: www.cognos.com/products/corporate_performance_management

¹³ "Significant Historical Dates (1792-1969)." NYSEData, http://www.nyse.com/factbook/viewer_edition.asp?mode=table&ckey=104&category=4

¹⁴ Koller, Timothy, & Peacock, Jonathon, "Time for CFOs to Step Up." *McKinsey Quarterly*, Number 2, 2002. http://www.mckinseyquarterly.com/article_page.asp?ar=1188&L2=5&L3=5

MEASURING UP AND STAYING AHEAD

Sarbanes-Oxley and global standards such as IFRS are pressuring companies to improve accounting practices and financial reporting, increase transparency, and achieve greater corporate governance.

Cognos Controller provides advanced consolidation capabilities to address the accountability issues your organization faces. And by integrating consolidation with CPM—planning, analysis, and metrics—you can achieve greater control and management of your company's performance.

Compliance is the new business reality. With state-of-the-art consolidation technology and performance management capability, you can keep on top of the rules, achieve good governance, and stay ahead of the competition.

ABOUT COGNOS

Cognos is the world leader in business intelligence and enterprise planning software. Our solutions for corporate performance management let organizations drive performance with planning and budgeting, monitor it with scorecarding, and understand it with business intelligence reporting and analysis. Cognos is the only vendor to support all of these key management activities in a complete, integrated solution.

Cognos serves more than 23,000 customers in over 135 countries. Cognos enterprise business intelligence solutions and services are also available from more than 3,000 worldwide partners and resellers.

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