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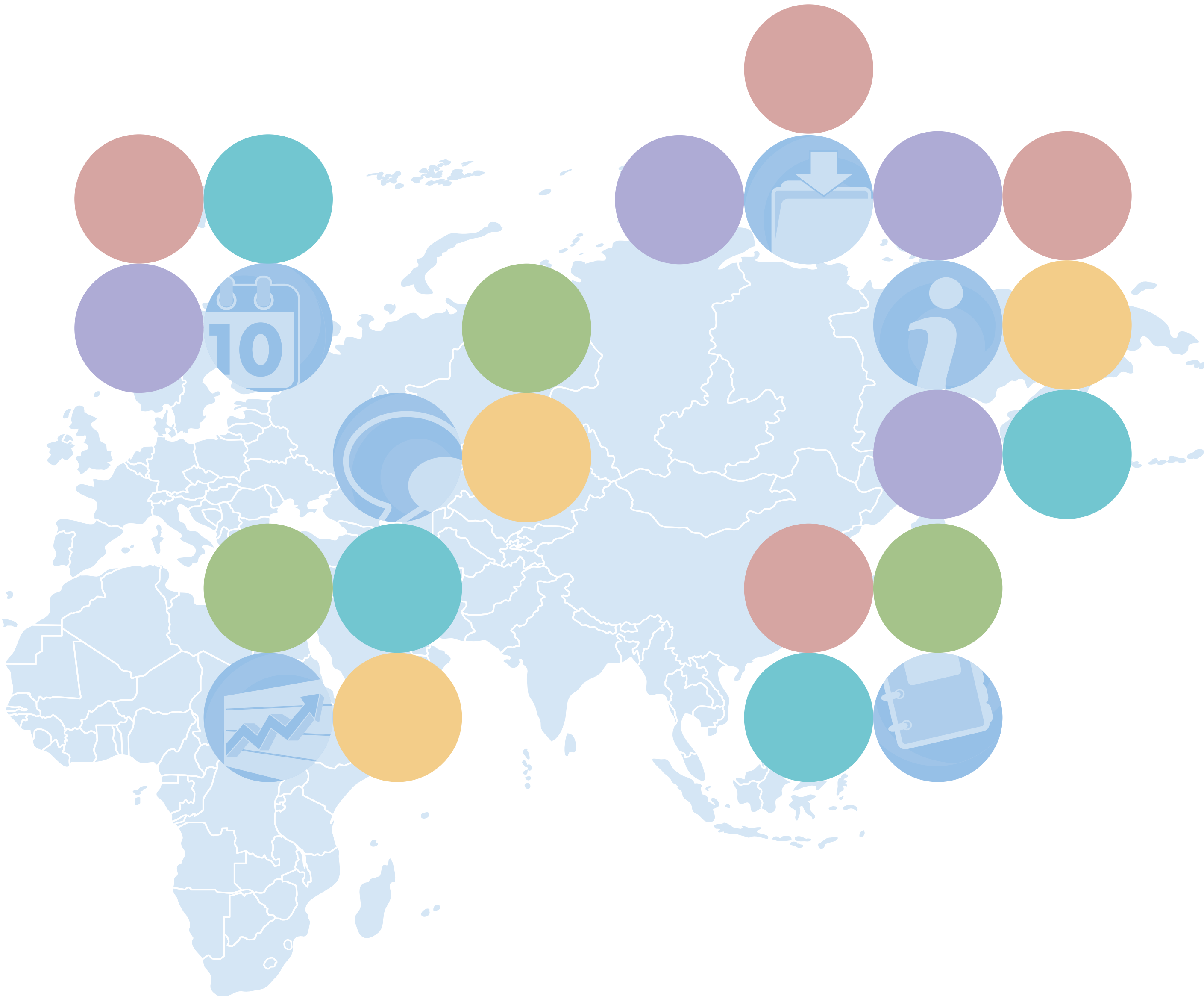

Making the numbers add up – how better financial accounting can support and promote growth

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Optimising finance processes and systems

Many of us have a tired boiler hidden away in our home – sometimes the house isn't quite warm enough and we're reminded that we really ought to get it serviced more regularly; we also have a niggling feeling that it's not very efficient or cost-effective, but we know that little short of catastrophic failure will lead to us actually doing anything about it. In the same way, many mid-sized businesses have a niggling feeling that their finance processes and systems could be improved, but with other priorities vying for their attention they let the old systems wheeze on for the time being and never quite get around to exploring the alternatives.

In our recent survey of people in more than 100 mid-sized companies, we explored the frustrations of people responsible for processing financial data and also tried to understand the needs of those outside the finance department who rely on financial information. This survey was supported by interviews with consultants working for mid-sized companies, and the input of managers at mid-sized companies via a roundtable discussion.

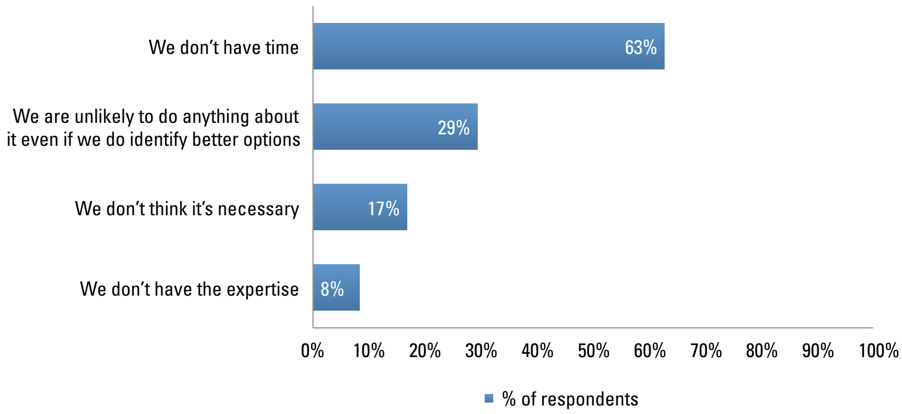
What became clear is that all is not as it should be. For example, more than 60% of people within finance functions recognise that they need to improve their financial processes and nearly 30% of end users believe that the data they receive is inaccurate, making it difficult to use financial information effectively in their roles. Yet, in many mid-sized companies, these issues remain unaddressed, either because of a perceived lack of time (63% of finance respondents) and/or a sense that the business is unlikely to act even if better options are identified (29%). That's set against the small minority (17%) of people within finance departments who believe that a more frequent review of finance processes and technology simply isn't necessary in the first place.

Our research suggests that the vast majority are right: things could be better. Much better, in fact. The potential benefits of better financial systems range from lower headcount within finance and the avoidance of revenue leakage and improved cash flow, through to better management of all aspects of an organisation.

Let's put it this way: if you discovered that your boiler wouldn't just heat your house, but could also make the kids' dinner, read them a bed-time story and pour you a glass of wine; just how much of the next five minutes would it take you to get someone round to fix it?

Figure 1:

Factors preventing more frequent review of finance processes and technology (finance perspective)

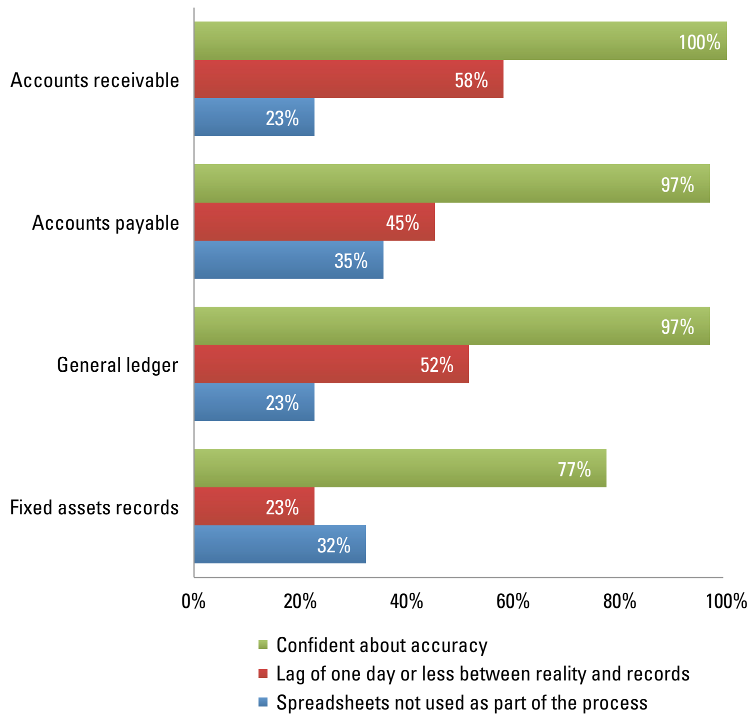


Core finance processes

Like the home-owner for whom hot water and warm radiators means the boiler doesn't need looking at, the automatic reaction of mid-sized companies is to be confident about the accuracy of key financial records: almost everyone we surveyed said that their accounts receivable, accounts payable and general ledger are accurate, and nearly 80% have confidence in their fixed assets records. However, further questioning suggests that this confidence is probably misplaced. The majority of respondents admit to a lag of more than one day between reality and their records, and the majority of companies (from 77% for general ledger to 65% for accounts payable) use spreadsheets as part of the process for producing each of these records. As Sally Scott at ABS says, "Wherever processes aren't automated and spreadsheets are used, the opportunity exists for human error. Often it is only when companies begin to challenge existing processes that they realise how many errors they have been inadvertently introducing." This view was backed up by a roundtable participant, "Reports have to be created from data in the system – our experience is that when people start manipulating data in Excel it becomes inaccurate."

Figure 2:

Views on key finance processes (finance perspective)

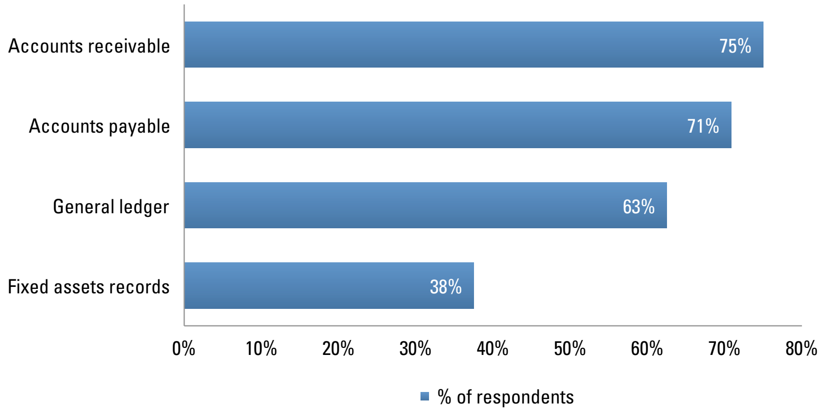


It's not just in the accuracy and timeliness of records that these manual processes cause problems. However well developed the process, a manual solution will require a higher headcount than an effectively automated process. Often more significant, but not as visible, is the revenue leakage that can be associated with processes that have developed over time. For example operators or engineers may not be logging time correctly against individual clients which in turn means clients are under-billed. According to Andrew Brayson at ABS, "Simply by stemming revenue leakage by tracking work performed against contractual terms and the invoicing process , the typical mid-sized company can increase turnover, recoup costs and improve profitability. Similar benefits are often seen in chasing debtors where an automated work flow can ensure that the correct process is followed for every invoice."

Manual processes also inevitably lead to organisations being dependent on key individuals, and when these individuals take holiday or, even worse, leave the company, the processes suffer. And for those companies looking to grow, more business means more headcount – an issue recognised by our survey respondents (Figure 3) – but one that can be avoided through leveraging technology.

Figure 3:

Processes requiring larger headcount if revenue increased by 50%



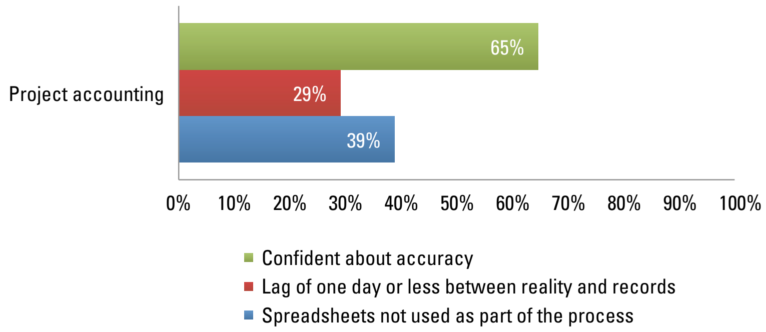
Whilst the focus so far has been on the impact of 'making do' on the finance department, the real impact spreads much further. Inaccuracies and lack of timeliness in official information tends to drive people outside of finance to create their own records (a cost that is very rarely recognised) or simply to get by without using financial information – something that's a real issue for any company in today's fast-changing environment.

Project accounting

In terms of financial processes, mid-sized companies are less confident about their project accounting than anything else. About two-thirds of people express confidence in their accuracy but, as with other financial processes, even this level of confidence is probably misplaced. Indeed more than 70% admit to a lag of more than one day between reality and records and over 60% confess to using spreadsheets.

Figure 4:

Views on project accounting processes (finance perspective)



Whilst on the surface project accounting may not seem as important as, say, accounts receivable or the general ledger, the reality is that cumbersome, potentially inaccurate, processes, can cause a number of problems for mid-sized companies. According to Dennis Horner at consulting firm PKF, "It's very difficult for someone to manage a project if they don't have access to accurate and up-to-date information. Giving someone responsibility without the tools they need to manage that responsibility makes a successful outcome much less likely. I also see this issue manifest itself when mid-sized companies are dealing with much larger clients – clients who expect to be given up-to-date and accurate cost or expenditure information without too much delay."

Making better use of financial data

Whilst we can't be sure that there's any difference between the attitudes of people in accounting departments and anyone else, our research suggests that there is an element of truth in the idea that a large amount of time is spent creating financial reports that aren't necessarily valued or used.

In fact nearly half of respondents within finance believe that they're producing reports which are never used; something that goes a long way to explaining – and even forgiving – a loss of humour on the part of finance departments. And feedback from senior managers in other parts of the business suggests that they're not wrong – about half (52%) of managers and directors look at a report produced by someone else more than once a week. The other half don't seem to make much use of financial reports at all.

"People who work in accounting departments often work 12 hour days creating reports that nobody cares about. This gives them a very bad attitude. Do not attempt to humour them."

Dilbert (Scott Adams)

Combine this apparent lack of interest from senior managers in the reports that are being produced with systems that make processing and analysing financial information very time intensive, and even bad attitude becomes quite understandable.

From the perspective of the finance team, the key issue here, alongside inefficient systems and processes, is that senior managers aren't using financial information enough (Figure 5). And anyone who has worked in or with companies would no doubt attest that there is an issue – many senior managers have built their career through a functional route; they are experts in their field but, unless they've taken time out to study, have seldom trained in finance. Even large companies struggle to find the time and resources to devote to their senior managers' financial education. Indeed the non-finance people in our survey agreed with this assessment: more than a third agreed that other people don't appreciate data and analysis and just 7% strongly disagreed. Combine this lack of knowledge with a culture that doesn't demand a strong focus on numbers, and it is not surprising that finance departments are left frustrated that more isn't being made of the information they provide.

But let's not be too quick to point the finger at senior management. Of the directors and managers working in non-finance functions, 31% believe that the data they receive is out of date and 27% feel it is inaccurate. Most people wouldn't accept this from outside parties (imagine trying to purchase something at John Lewis and them telling you their data was out-of-date and inaccurate) so why should they accept this in their own business? Added to which, people struggle to know what to focus on because they receive too many reports (23%). As one of the managers at our roundtable discussion highlighted, "We get monotonous reports every month and they aren't being used to drive any kind of action; people don't bother looking at them until the final months of the year."

It's tempting to conclude that managers should just create reports for themselves whenever they need them. But more than a third of respondents said that doing so was just too time consuming. Nor does a 'made to order' system always work: put in a request to the finance department and, 26% of people tell us, you'll experience too long a gap between your request and the response. So it's no more of a surprise that finance managers aren't making use of financial data than it is that finance people have a sense of humour failure.

So what's the solution? Well, one set of trusted numbers would be a good start. "I see lots of companies where people don't trust the data and many incidents where there are multiple and contradictory sources, often because people have started to create their own parallel records," says Dennis Horner. "This leads to duplication of effort but, even more importantly, a lack of trust in financial data. When it comes to making critical decisions, the debate centres on which numbers to trust if financial data is brought into the equation at all."

But creating a business which makes effective use of financial information requires more than just accurate, and timely, data. It relies on financial education and cultural changes that emphasise the need to make decisions based on good information and analysis. For businesses that do this well, the role of finance is fundamentally changed. Its focus is no longer on marshalling data (because the systems are there to do that) but on working with the rest of the business to agree key financial measures, to streamline regular reports and to support users so that they can get the information they need as and when they need it. Once the manual processes and multiple spreadsheets are eliminated, finance can focus on adding real value to the business rather than bringing cost.

Figure 5:

Producing financial information for other parts of the business (finance perspective)

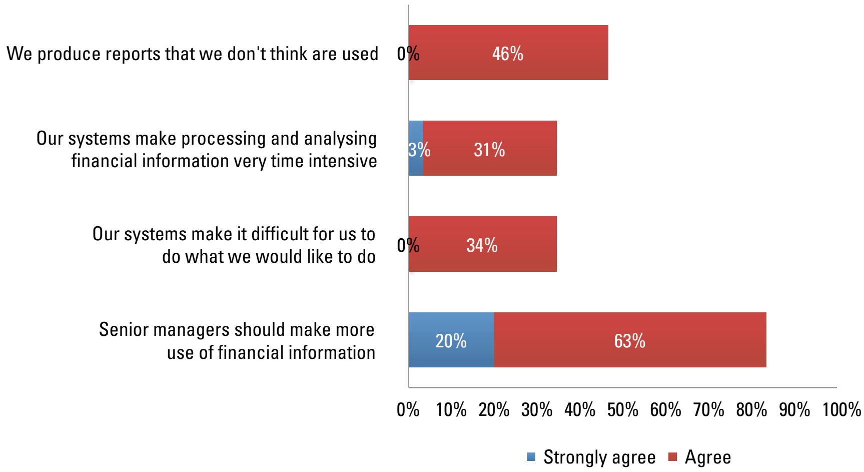


Figure 6:

Use of reports (Directors and managers outside finance)

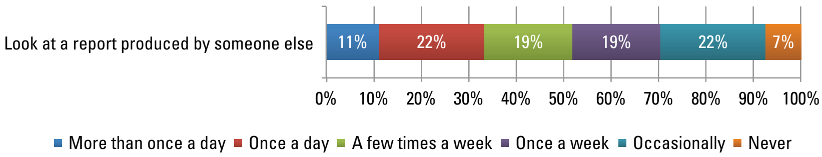
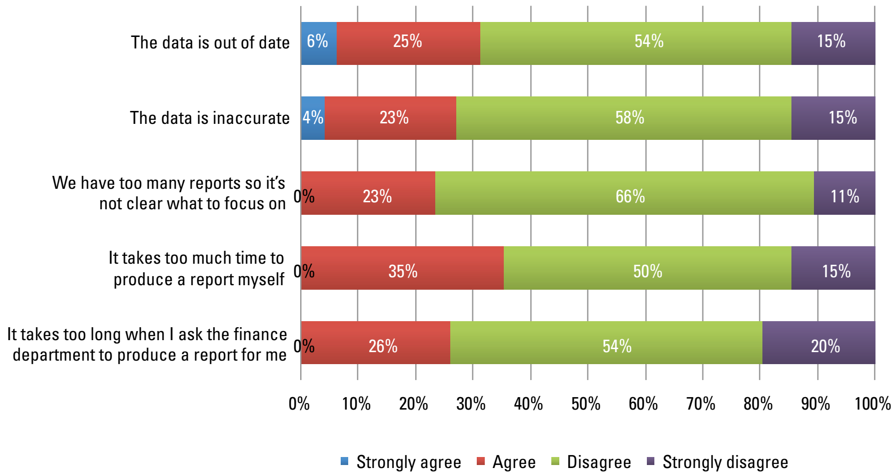


Figure 7:

Factors preventing greater use of financial data (Directors and managers outside finance)



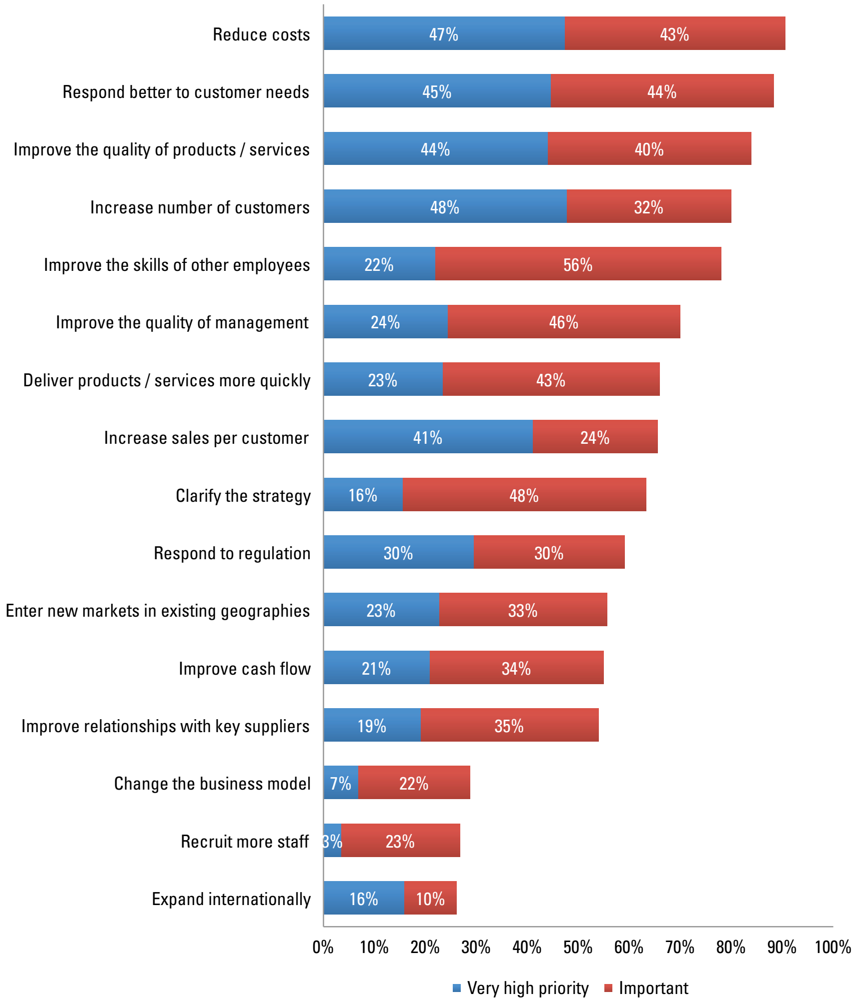
Does the boiler have to explode before you address the issue?

Given the concerns of people both within and outside the finance department, and the benefits of change, why isn't finance a higher priority for mid-sized companies?

In our survey we asked companies about their broader priorities. Given the economic turmoil, it's not surprising that reducing costs came top of the list, with over 90% saying this is important or a very high priority. Given this, finance might be expected to receive attention – slicker, automated systems can quickly reduce the number of people required for basic processes, as well as being instrumental in eliminating revenue leakage. Mid-sized companies are also aware of the need to improve the quality of management (70% of respondents) and again finance can be instrumental in ensuring decisions are made based on good data and analysis. Yet still, as our 2011 report highlighted, financial accounting is often bottom of the list.

Figure 8:

Organisational priorities



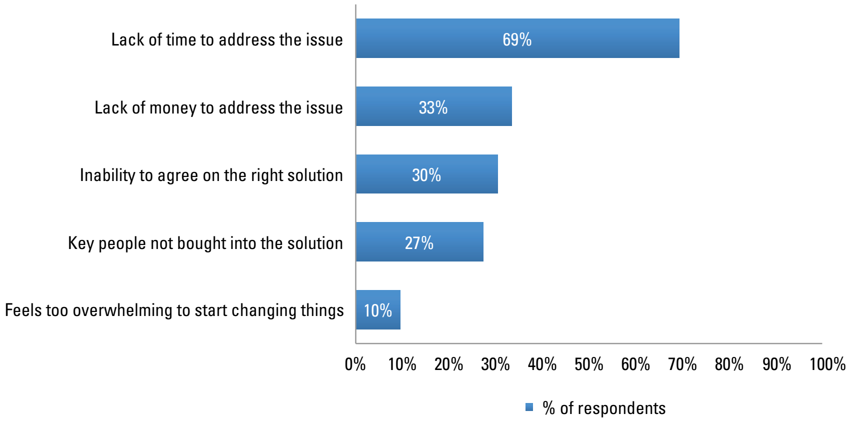
As with those old, inefficient, boilers in our own homes, one of the key barriers appears to be an 'if it ain't broke, don't fix it mentality' and very rarely does some big event happen to demonstrate that financial processes and systems are definitely broken. The reality is that most mid-sized companies can get by day-to-day. It's not obvious that finance processes could be run with fewer people or that the business is suffering because managers don't trust the data.

A second barrier is the role and power of the finance director. After years of being asked to cut costs, and being berated when things go wrong, many finance directors feel unwilling to suggest that their organisation ought to spend money on finance in order to reap rewards going forward. And for the finance director operating in an environment where financial analysis is not prioritised, the challenge is even tougher.

A third barrier, according to Andrew Brayson, is a fear of losing control. "Even in organisations where financial data is valued, some finance managers have a perception that they're in control when elements are being handled manually. To automate processes can be frightening – yet the reality is that automated processes seldom fail, while there are numerous opportunities for manual processes to do so. The key thing is to ensure that the new process is easier than the old because people are people and will often revert to what makes most sense to them personally."

Figure 9:

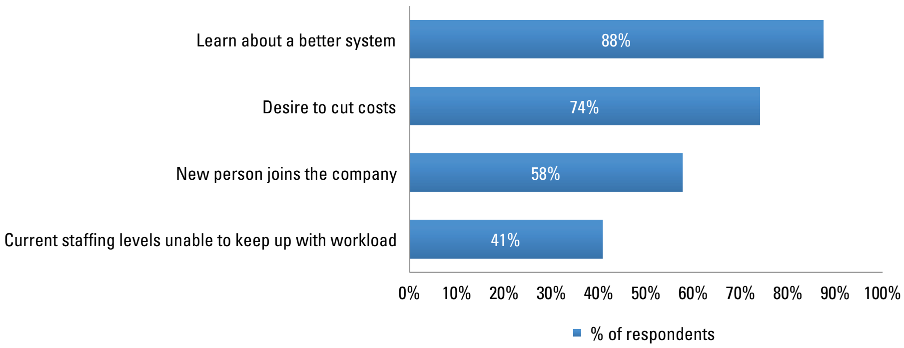
Factors preventing organisations from addressing an opportunity (finance perspective)



Finally, some organisations are reluctant to even think about a new system because they believe it will be extremely time intensive to manage the change, and too expensive (Figure 9). According to Andrew Brayson however, "When people actually get some facts about the costs and disruption associated with this type of project, they're always surprised by how much cheaper and easier this is than say, ten or even five years ago. Technology has moved on massively."

Figure 10:

Factors causing companies to review their finance processes and/or systems



So what does drive companies to reconsider their existing finance processes and systems? According to our survey (Figure 10), a desire to cut costs is often the trigger, as is current staff being overwhelmed by their workload. However, for many companies, it's realising – either through a new person joining the company or because they learn about a better system – that more could be possible, which pushes them to address that niggling concern.

Boiler health check

Instead of waiting for a major failure, or for someone new to join the department, here are five questions that should help quickly identify whether you've got an efficient and effective finance department, or whether there's a lot of room for improvement.

- **Are spreadsheets ever used in finance?**

  A. Never.

  B. Some of the time.

  C. Regularly.

- **If 20% of your finance staff were away tomorrow, what impact would this have on core processes?**

  A. They would carry on as normal – they require very little manual input.

  B. We would have to decide which ones to delay – some processes would suffer.

  C. It would be chaotic.

- **How confident are you that clients are being invoiced correctly and that late payers are being chased?**

  A. 100% confident – our workflow systems mean everything is recorded correctly and actions are followed appropriately.

  B. There are probably occasional issues.

  C. These processes depend on the individuals concerned.

- **Are senior managers outside of finance keeping their own records?**

  A. No – all our data comes from the same source.

  B. Some are.

  C. Yes, this happens a lot.

- **When making important decisions, how is financial data and analysis used?**

  A. It's key to our decisions and people are confident in the underlying data.

  B. We try to include it but the discussion often centres on where the data has come from or the quality of the analysis.

  C. Financial data takes a back seat.

All A:

Great – sounds like you're in good shape.

Mainly A's & B's:

Whilst you're doing better than many mid-sized companies, we recommend spending some time understanding the benefits and costs of better processes and systems.

Mainly B's & C's:

You can expect to see significant benefits from improved finance processes and systems.

A note from our sponsor

In a difficult market, mid-sized companies face plenty of challenges as they try to grow their businesses. Volatile demand, the escalating cost of raw materials and the continuing economic turmoil associated with the sovereign debt crisis in Europe, will all be preying on the minds of business leaders.

And yet this report reminds us that the enemy may be within, as well as without; that companies may be holding themselves back by failing to address the need to improve their financial systems and processes. Worrying though that may be, the good news is that – unlike many of the challenges they face – this is something that is entirely within the control of mid-sized companies to fix.

Doing so needn't be difficult either – technology has come a long way and made solutions far more readily available. And the benefits, many of which are discussed in this report, can be huge. Indeed at a time when the search for low-hanging-fruit on the tree of business improvement has generally been called off, this looks like one opportunity that most companies have missed.

Finding it, and putting it right, is what we do. We have a huge amount of experience helping mid-sized companies to realise the untapped potential of better financial systems and processes and we'd love to hear about your situation to see how we can help.

Simon Fowler

Managing Director, Advanced Business Solutions

Methodology

In March 2012, we surveyed 104 decision makers in mid-sized companies to understand their experience of creating and using financial information. Approximately one third of respondents work within finance.

This was supplemented with a conversation with a group of managers, also from mid-sized companies, as well as interviews with management consultants.

For further information about Source's research, please contact julie.ahadi@sourceforconsulting.com or telephone +44 (0)20 3178 6445.

About Source

Source (www.sourceforconsulting.com) is a leading provider of information about the market for management consulting. Set up in 2007 and based in London, Source serves both consulting firms and their clients with expert analysis, research and reporting. It draws not only on its extensive in-house experience, but also on the breadth of its relationships with both suppliers and buyers. Source is owned by Source Information Services Ltd, an independent company, which was founded by Fiona Czerniawska and Joy Burnford. Fiona is one of the world's leading experts on the consulting industry. She has written numerous books on the industry including: *The Intelligent Client* and The Economist books, *Business Consulting – A Guide to How it Works and How to Make it Work* and *Buying Professional Services*. Joy Burnford was Marketing and Operations Director at the UK Management Consultancies Association between 2003 and 2010, and prior to that worked for PA Consulting Group and has extensive experience of marketing consulting services.

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Advanced's software systems comprise core accounting/financial management, procurement, human resource and payroll systems, integrated with a range of collaborative, document management and business intelligence solutions to extend the value and effectiveness of the finance, human resource and payroll departments. These can be delivered as a managed or bureau service. Customers are from both the public and private sectors and include Companies House, Newcastle City Council, WH Smith, Royal Bank of Scotland, Aer Lingus, National Express Group, DFS, RSPB and Great Ormond Street Hospital for Children NHS Trust.

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