Post Sarbanes-Oxley: Does XBRL Hold the Key?

What would you do if you were asked to reinvent accounting software given the changes to the accounting profession in the post-Sarbanes-Oxley (SOX) era? Significant new requirements have begun to take hold in corporations all around the globe. Companies now are asked to provide verifiable internal controls and executive-level sign-offs on SEC filings. There is increased pressure to improve financial reporting transparency and provide higher levels of audit scrutiny both from board-level audit committees and internal and external auditors. Few accounting solutions on the market can respond to these demands rapidly without substantial help.

The leading accounting systems of today were born and bred in an era of reflective bookkeeping. Before SOX, accountants provided management with business information about what occurred several weeks after an action took place. Auditors would appear after the close of a year and verify the financial condition of the company. This is like trying to drive a car while looking exclusively at your rear-view mirror. The method is great for telling management and business stakeholders where you have been, but it isn’t much for giving guidance on where you are going.

Rivet Software, a new company located in Denver, Colo., has fully embraced the post-SOX environment. They are starting with a clean slate and creating software that responds naturally to the new corporate governance, transparency, and compliance environments. Legacy accounting systems can’t react easily to requests for assurance about their internal controls, nor do they respond well to requests for more information from corporate audit committees or new demands from external auditors.

Rivet Software’s president, Michael Rohan, built the company around a simple concept: Build financial integrity management directly into the system. “We saw an opportunity to deliver applications for accounting and financial professionals that were fundamentally different from the products available on the market today. We made a conscious effort to build financial integrity into the fabric of our product line,” Rohan said.

Financial integrity management is a concept that’s very familiar to management accountants. Quality in financial reporting, both internally and externally, starts with reliable accounting information systems that provide quality information. The role of the management accountant is to build the quality into all aspects of business reporting. The foundations of financial integrity are:

◆ Low-level data tagging in industry standard XML format,
◆ Built-in internal control checklists,
◆ Drill-down capability for all business data,
◆ Reliance on XBRL-GL for internal data,
◆ External financial reporting fully integrated with internal data, and
◆ Low training required.

Wayne Harding, vice president of business development at Rivet Software, would like to see the day come soon where want-ads for accountants no longer specify an expertise in a particular software package and
instead focus on the accountant’s ability to deliver on improving business processes and strengthening internal controls.

Starting from a clean slate, Rivet Software is fundamentally different. They have set out to leverage the new financial environment by building in the ability of accountants not only to participate in the post-SOX arena but also to contribute strategically to the advancement of the business. Accountants will engage Rivet from a place of familiarity. Program interfaces are built in a Microsoft Office environment. If the financial professional can use Microsoft Word and Excel, he/she can use Rivet Software applications.

The approach of building XBRL into the foundations of an accounting software program is a major departure from what other software vendors are doing today. For example, Microsoft Business Systems Navision adds XBRL functionality as an addition to business reporting. In contrast, Rivet builds XBRL directly into the fabric of the program. This approach allows the accountant to create data streams of marked-up XBRL directly into internal business reporting systems such as digital dashboards or scorecard systems.

According to Harding, traditional accounting packages and business reporting systems fail to deliver. “Most Sarbanes-Oxley solutions are patchworks of existing technology and modules brought together to put a temporary solution on a long-term problem,” he explains. In the initial assessment of SOX requirements, large companies thought their existing systems of internal control were going to be sufficient to meet the new law’s requirements. They were wrong.

Asked why Rivet chose XBRL as a fundamental component of their software, Rob Blake, vice president of product management, said, “Building XBRL in at the lowest level of our software system allows us to achieve unprecedented native compliance with the internal control requirements of Sarbanes-Oxley, provide the needed visibility for the various audit teams, and provide integrity back into the financial reporting system. For us, XBRL was an obvious choice.”

Building Compliance In
Now that companies are facing real deadlines for complying with SOX Section 404, how are they doing? According to Robert Sepanloo from Fujitsu Software, the answer is “not well.”

“Many companies hit the panic button. They hired teams of expensive consultants, bought specialized auditing point solutions, and launched hasty projects to make sure they were on track to document their controls. This approach may help a company meet a deadline, but I believe it’s a fundamental misunderstanding of the post-Enron business environment.” (Source: Robert Sepanloo, “Sarbanes-Oxley: Stop Whining!” ComputerWorld, Fujitsu Software, November 2004.)

Companies looking for a better way of coping with the post-Enron era might want to try installing a new system that has built-in compliance to solve today’s problems as well as providing the foundation for using a new internal control system as a long-term strategic advantage. The audit firm Deloitte agrees: “We believe that an organization that views Sarbanes-Oxley as an opportunity to improve business performance, rather than as a mere exercise in compliance, will get a re-energized company, reassured investors, and an ultimate increase in enterprise value. To reap these benefits, however, a company must build the right controls and approaches into its compliance program from the beginning. Some key guiding principles for companies implementing Sarbanes-Oxley compliance programs include:

◆ An internal control program adopted and endorsed by the board, audit committee, CEO, and other C-suite executives;
◆ SOX compliance based on effective and efficient business processes, enabled by properly designed and implemented technology, and executed by competent people;
◆ An expectation that the accuracy,
timeliness, reliability, and transparency of a company's financial information will garner the recognition of stakeholders;
◆ Change is a necessary component for improving the organization;
◆ The critical need for sustainability (this is not a one-time issue);
◆ A financial commitment to strong governance; and
◆ A guarantee for open communication.  
(Source: http://www.deloitte.com/dtt/section_node/0%2C1042%2Csid%25253D61683%2C00.html)

Smart companies like Rivet Software know that building financial integrity management into their software will not only enable compliance with mandated regulations, but it will enable a new level of performance for the internal and external financial reporting process. With the help of XBRL touching all aspects of financial data, companies will be able to turn compliance into outstanding performance.

Rob Blake, VP of Product Management at Rivet Software, will be speaking at the IMA’s 2005 Annual Conference in Boston, June 18-22, 2005.

Neal Hannon is an accounting lecturer for the Barney School of Business at the University of Hartford. Author of two books and numerous articles, he is the IMA’s representative to the XBRL International consortium. Hannon is a former member of the XBRL-US steering committee and former chair of XBRL International’s education Committee.
Advice on how to reach a fair assessment that does not mislead investors regarding the condition of internal controls and the reliability of financial statements. We believe management’s formal assessment should reflect their belief as to whether the system of internal control provides reasonable assurance of the reliability of future financial statements. That reliability is based on the likelihood of an error that would be material to a reasonable investor. Key areas of focus in the Sarbanes-Oxley Act include corporate responsibilities, auditor independence and financial reporting. Under corporate responsibilities, in addition to new rules impacting insider trading and loans to corporate executives, is the requirement for CEO and CFO certification of financial reports. This is putting new pressures on corporations to tighten internal controls and drive for more internal transparency into the drivers behind the financial results. Concerning financial reporting, the Sarbanes-Oxley Act requires more timely and detailed disclosures of financial results, including more detail regarding off-balance sheet obligations, insider trades and other significant events.