

# Enterprise Systems and Revenue Recognition: The Missing Link

**RevenueRecognition.com**  
*Revenue Management Resources for  
Today's Financial Executive*

FINANCIAL EXECUTIVE BENCHMARKING SURVEY

**Enterprise Systems Edition**

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## EXECUTIVE SUMMARY

RevenueRecognition.com in association with International Data Corporation (IDC) recently surveyed 685 business leaders about the need for improvements in their finance processes, with a focus on revenue recognition and related reporting processes. The survey was conducted in May 2006 by email and all responses were on an anonymous basis. More than 75% of respondents are CFOs, Controllers, senior finance executives, internal auditors, or compliance leaders. 120 responses were from companies with revenues of \$1 billion or more. References to the data and narrative in this report should be sourced:

**[www.RevenueRecognition.com](http://www.RevenueRecognition.com) and IDC, 2006.**

### Key Findings:

- The top 3 concerns for finance teams are the financial closing and reporting process, the use of spreadsheets, and revenue recognition.
- 92% of public companies rely on manual processes to perform key revenue recognition and reporting functionality (nearly the same percentage is true for private companies).
  - ▶ 68% of all companies stated their Financials/ERP systems DO NOT automate all their revenue recognition and reporting activities.
  - ▶ 84% of companies that initially stated Financials/ERP systems DO automate revenue accounting are actually using spreadsheets for these activities.
- Companies want to spend less time on data aggregation, manipulation, and validation and more time on business performance analysis.
- The finance processes that are most difficult to establish internal controls for are contract management and revenue recognition.

## THE IMPACT OF REVENUE RECOGNITION ON FINANCE RESULTS

There are several ways that revenue recognition can impact the validity of financial results, putting companies at risk for restatements or being cited for compliance control weaknesses, including:

- A lack of revenue recognition policies
- A lack of policy enforcement
- Manually-intensive revenue recognition practices that are prone to error and inconsistency
- Manual efforts that reduce time available for analysis and identification of critical issues

Compliance initiatives have highlighted control gaps within the organization, and revenue accounting is a key area that can benefit not only from documentation and testing, but automation across the process.

The results of this survey highlight the weaknesses that companies see within revenue recognition processes, identify the opportunities they see for improvement, and also reveal other finance processes ripe for improvement.

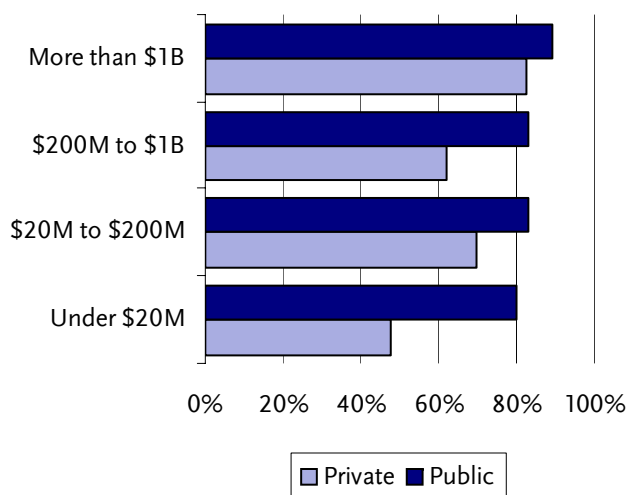
## REVENUE RECOGNITION POLICIES

Regardless of a company's size, ownership structure, or what systems it has in place, having a written revenue policy is fundamental to accurate revenue reporting. The revenue policy should govern how contracts are written, how orders are booked, define the revenue accounting workflow, as well as how journal entries are made as revenue is managed through the finance department.

Overall, approximately 60% of private companies and 85% of public companies have a written revenue policy. As Figure 1 shows, the number climbs to 90% for public companies with more than \$1 billion in revenue.

**Figure 1**

Companies that have a written revenue recognition policy.  
(By size and ownership, n=685)

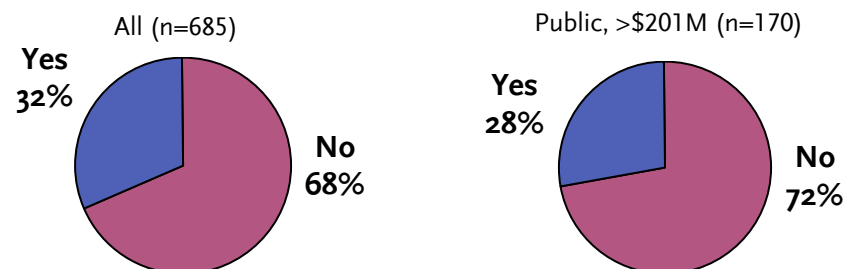


## ENFORCING REVENUE RECOGNITION POLICIES

How companies enforce revenue policies across their enterprises is of vital concern. The integrity of financial information is best maintained when it is systematically controlled from the moment an order is entered all the way through to the reporting process. Many companies depend on enterprise Financials/ERP systems to manage their financial processes. However, only 32% initially revealed that their Financials/ERP systems automate all their revenue recognition accounting and reporting requirements, highlighting a significant weakness that can represent a control risk that impacts financial results. In fact, the number was even lower (28%) for the largest public companies (more than \$200M in revenue).

**Figures 2a and 2b**

Does your current financial IT infrastructure (Financials/ERP system) automate all of your revenue recognition accounting and reporting needs?



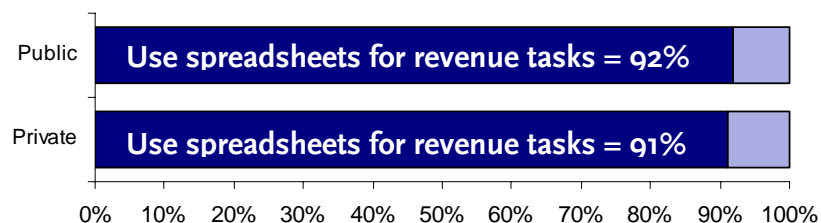
## ENTERPRISE SYSTEMS AND REVENUE RECOGNITION: *THE MISSING LINK*

In fact, there is a “missing link”: perception of the use of enterprise systems for revenue recognition is overstated. In Figure 3, 92% of companies said they are using spreadsheets for one or more of the following key revenue recognition and reporting tasks:

- Applying revenue allocation rules
- Redistributing revenue (e.g. based on SOP 97-2, EITF 00-21)
- Creating revenue recognition schedules for future periods
- Reviewing sales orders to identify deferred items
- Performing revenue contribution analysis
- Reporting on future revenue streams
- Creating accounting entries

**Figure 3**

Spreadsheet use for key revenue recognition and reporting tasks? (n=685)



### THE BOTTOM LINE

92%

Of public companies use spreadsheets for critical revenue recognition and reporting activities.

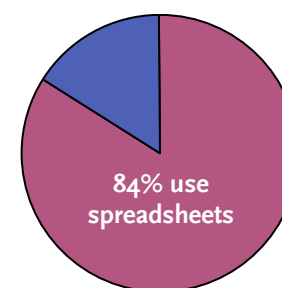
## ENTERPRISE SYSTEMS AND REVENUE RECOGNITION: *PERCEPTIONS VS. REALITY*

Why are 92% of all companies using spreadsheets when only 68% initially stated that their financial/ERP systems don't do the job? It seems there is a disconnect between the perceived capabilities of Financial/ERP systems and reality when it comes to revenue recognition and reporting tasks.

When looking at the subset of companies that had indicated their Financials/ERP systems do automate all their revenue recognition and reporting needs, 84% are also actually using spreadsheets for these activities, as shown in Figure 4. Clearly organizations have an opportunity to automate and improve the revenue recognition and reporting process.

**Figure 4**

Spreadsheet use by companies stating Financials/ERP systems automate ALL their revenue recognition and reporting needs. (n=217)



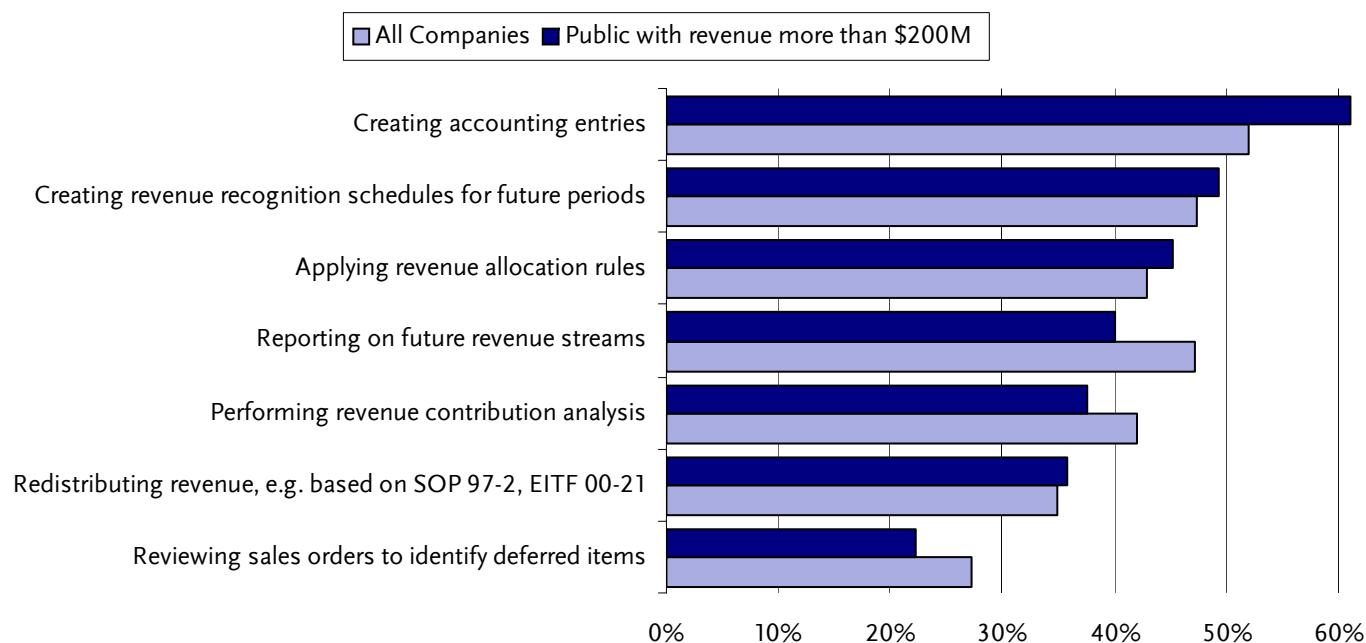
- Use spreadsheets for one or more of the revenue tasks above
- Do not use spreadsheets for any of the revenue tasks above

## THE FUNCTIONALITY GAP

The question remains then, which activities are falling through the cracks in the enterprise financial infrastructure? We asked respondents to identify what tasks they are performing with spreadsheets in order to assess where the problems lie. The results, depicted in Figure 5, show heavy reliance on spreadsheets for all the key revenue related processes listed. Creating accounting entries was number one, but there is not much difference between the top 5 tasks for which companies are using spreadsheets.

Despite the fact that larger, more complex organizations have significant IT investments, public companies with more than \$200 million in revenue are substantially more reliant than the overall sample (61% vs. 52%) on spreadsheets for basic accounting entries.

**Figure 5**  
Spreadsheet based revenue recognition and reporting tasks.  
(Multiple responses accepted, n=685, 170)



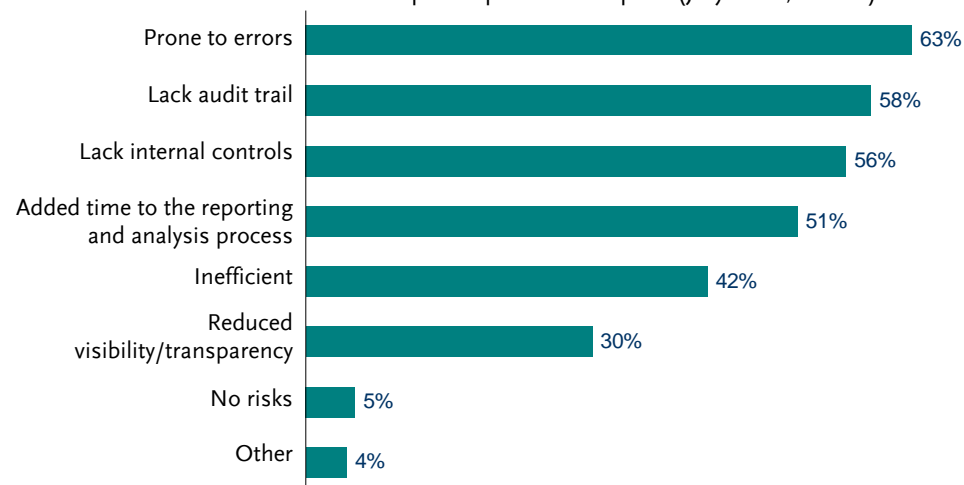
## REVENUE ACCOUNTING SPREADSHEETS: *THE COMPLIANCE KILLERS*

These results should be alarming for corporate finance departments, executives and investors alike. The risks introduced by spreadsheets have been well documented in numerous studies, including a previous RevenueRecognition.com survey. 95% of respondents to our July 2004 survey indicated that spreadsheets are on the wrong side of key compliance issues. As Figure 6 shows, nearly two-thirds said that the most significant risk of using spreadsheets is that they are prone to errors.

The complicated mechanics of revenue accounting make the use of spreadsheets in this process especially troublesome. IDC research confirms that auditors find spreadsheet errors difficult to detect because they lack audit trails and internal controls, and the use of spreadsheets for key processes such as revenue accounting tasks is a concern.

**Figure 6**

In your opinion, what are the major risks associated with using spreadsheets?  
Multiple responses accepted (July 2004, n=118)

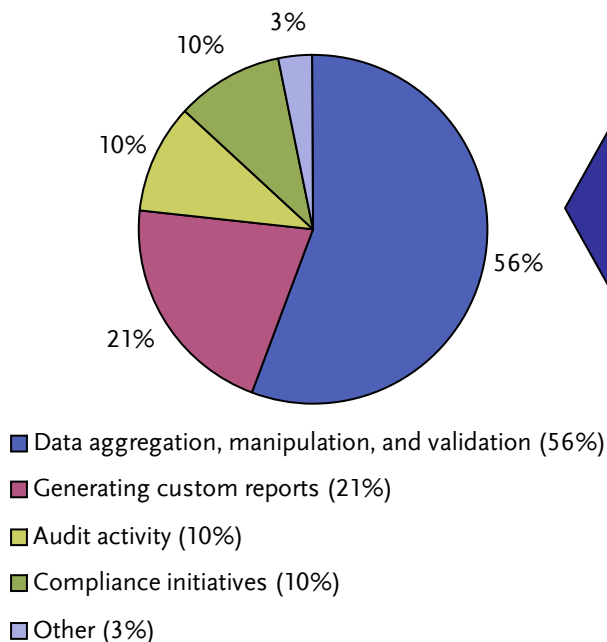


**It is apparent that spreadsheets are filling a serious functionality gap, but they violate basic compliance principles.**

## WHAT DO YOU NEED TO SPEND LESS TIME ON?

Manual, spreadsheet-based processes are productivity time drains. They involve data aggregation, manipulation and validation, which considerably reduce the time available for high-value tasks such as analysis. As Figure 7 shows, more than half (56%) of all respondents want to reduce the time and effort spent on these activities, followed by a reduction in time spent generating custom reports, at a distant 21%. The results are even more pronounced in companies with more than \$1 billion in revenue where data aggregation was rated number one by 59% of respondents.

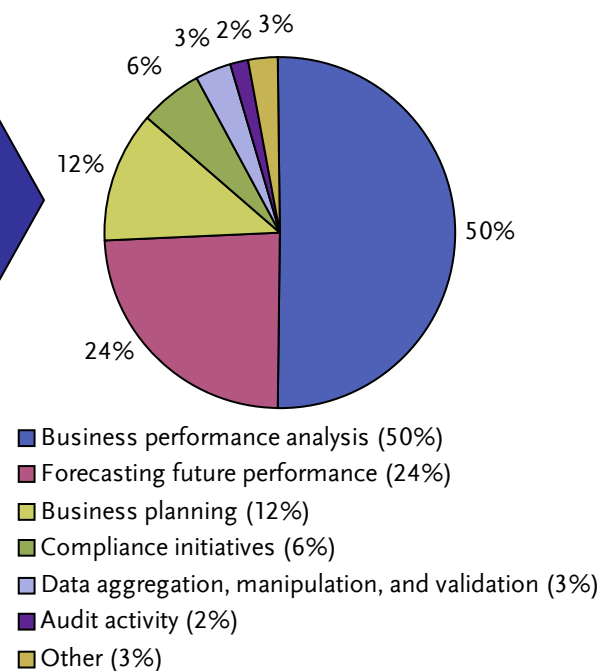
**Figure 7**  
What do you need your revenue management team to spend LESS time on? (n=685)



## WHAT DO YOU NEED TO SPEND MORE TIME ON?

When asked what activities require more time and attention, respondents were equally decisive—"business performance analysis" far outranked all other activities, as illustrated in Figure 8. Forecasting future business performance followed with 24%.

**Figure 8**  
What do you need your revenue management team to spend MORE time on? (n=685)



**Productivity vs. Performance**  
Companies want to spend less time on manual data activities and more time analyzing performance.



## INTERNAL CONTROLS AND COMPLIANCE

With regard to revenue recognition, the previously reported survey results do not highlight compliance directly as an issue – recognizing that improvement is needed in the business process itself, which, when managed optimally, meets compliance goals. However, as Figure 9 shows, two key internal controls challenges still exist in this area:

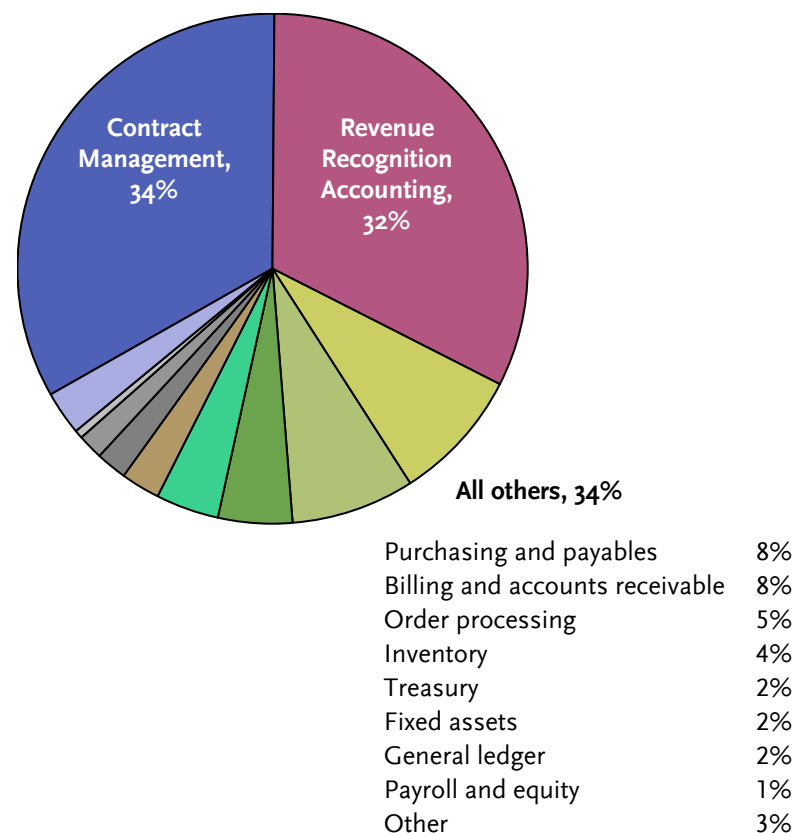
- Contract Administration and Management
- Revenue Recognition Accounting

Contract management is a critical pre-process for revenue recognition and both are complicated. Contract terms such as pricing, discounts, delivery schedules, performance incentives, etc. are needed to set up revenue recognition schedules and amounts.

One of the key challenges in establishing internal controls for these processes is coordinating the handoff of information across the sales cycle, order entry process, and recording of financial transactions. Even basic information such as the definition of a customer may vary between systems. Other key challenges are the inherent complexity of the revenue accounting process itself and pervasive use of spreadsheets to manage it. To be effective, the internal controls must be applied as information is transformed across the process, resulting in consistent definitions for information.

**Figure 9**

In your opinion, for which area is it most difficult to establish internal controls? (\$20M+, n=492)



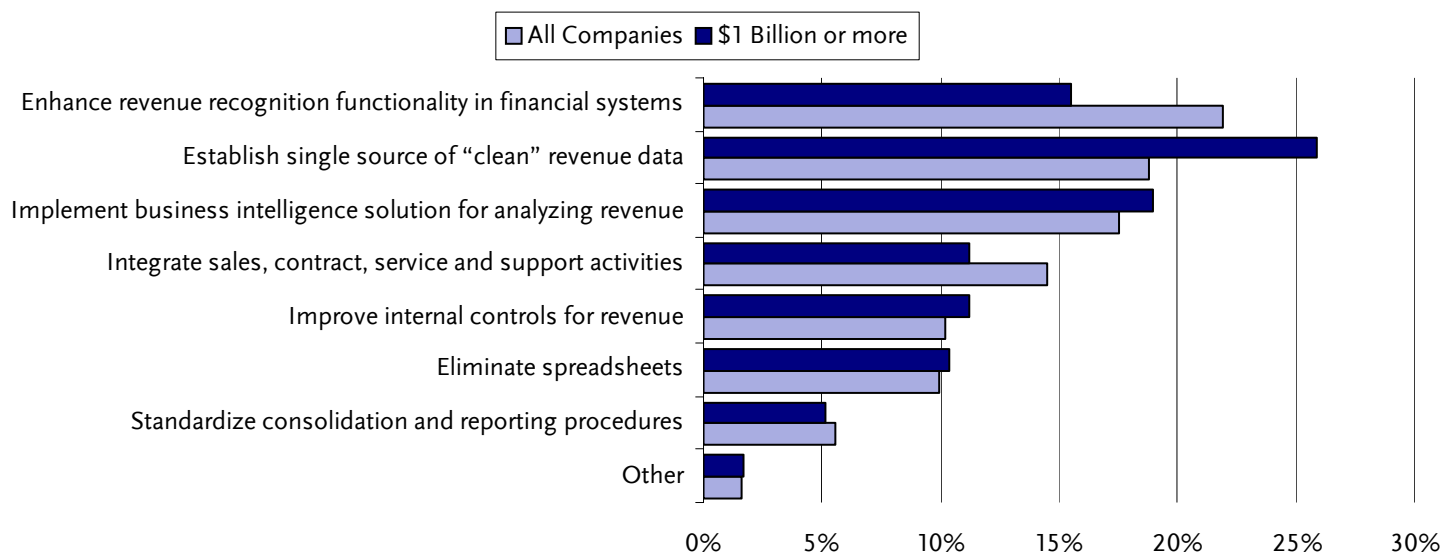
## IMPROVING THE REVENUE RECOGNITION PROCESS

When asked to identify the single most important change they would make to improve their revenue accounting processes, responses were spread across a number of key issues, as illustrated in Figure 10. The top three improvement areas all pertain to data integrity and validity. Enhancing the revenue functionality in financial systems was number one, with 22% of the vote. Establishing a clean source of revenue data (19%) and implementing business intelligence (BI) tools to analyze revenue (18%) were a close second and third. For companies with more than \$1 billion in revenues, establishing a clean source of revenue data was number one (26%), followed by BI tools (19%) and enhancing revenue functionality in financial systems (16%).

Collectively, these issues point to a need for automating the revenue recognition processes. “Revenue recognition processes are dependent upon information from multiple sources and typically cannot be executed in existing enterprise systems,” said Kathleen Wilhide, Director of Compliance and Business Performance Management (BPM) Research at IDC. “What is required is automation across this function which will yield a host of benefits, including: more accurate results, better internal controls, less reliance on uncontrolled spreadsheets, and freeing up time for performance analysis.”

**Figure 10**

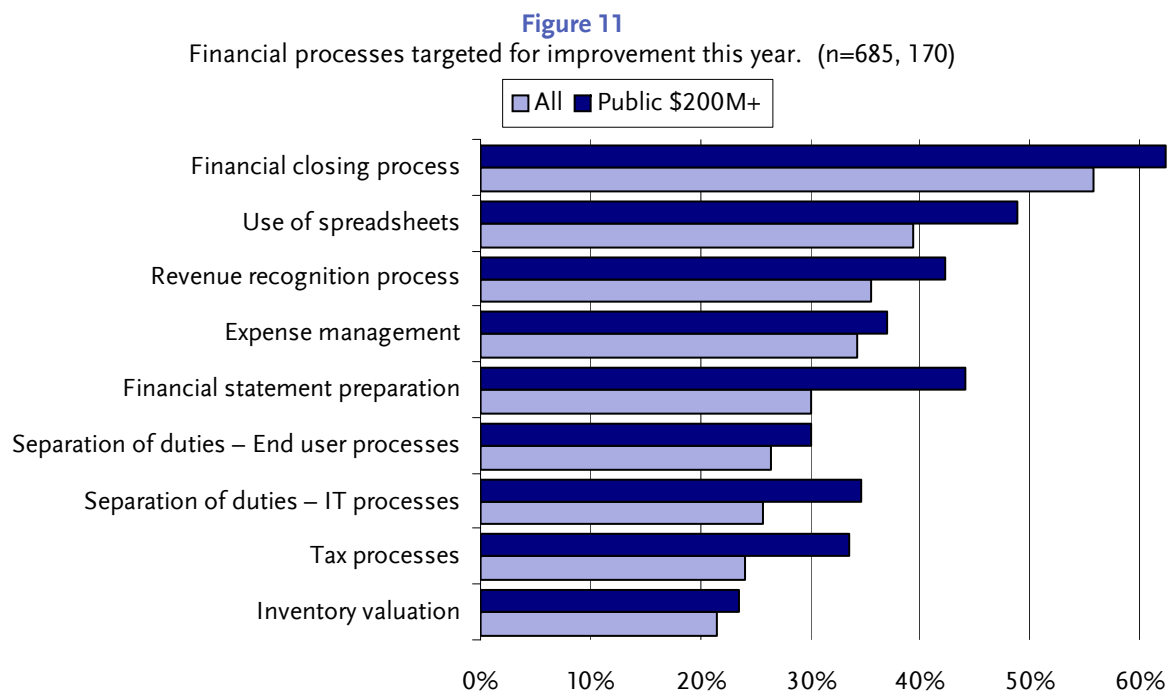
If you could improve your revenue recognition process, what would be the most important change you would make? (n=685, 116)



## IMPROVING OTHER FINANCE PROCESSES

Revenue recognition is one of several financial reporting processes needing improvement, as uncovered by our survey. The closing process is being addressed by more than half of all respondents this year. Use of spreadsheets and the revenue recognition process are being targeted by more than one-third of respondents. As shown in Figure 11, larger, public companies are actively addressing these issues across the board—62% are addressing the close process, while more than 40% are making improvements in each of the following areas: use of spreadsheets (49%), financial statement preparation (44%), and revenue recognition process (42%).

## IMPROVEMENTS UNDERWAY THIS YEAR



## IMPROVING OTHER FINANCE PROCESSES

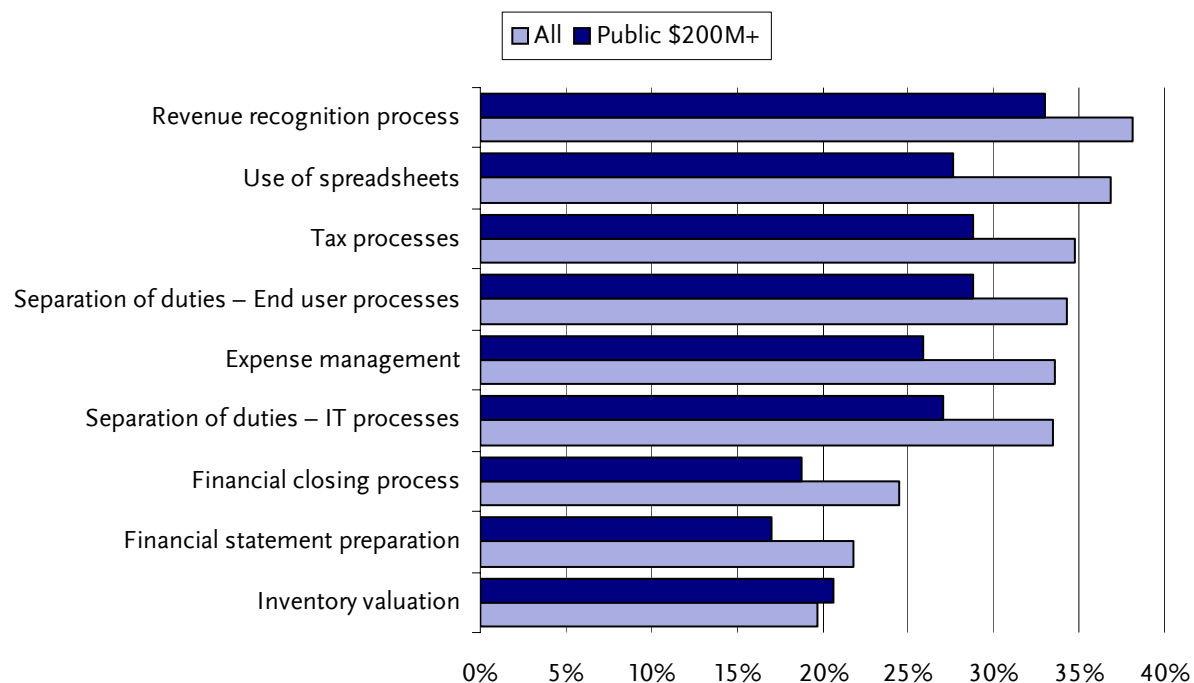
Looking to the future, Figure 12 shows that formal plans or assessments are being initiated in six key areas:

- Revenue Recognition
- Use of spreadsheets
- Tax process
- Separation of duties for end user processes
- Expense management
- Separation of duties for IT processes

## IMPROVEMENTS PLANNED FOR THE FUTURE

**Figure 12**

Financial processes where plans for future improvement have been made or assessments are being conducted. (n=685, 170)

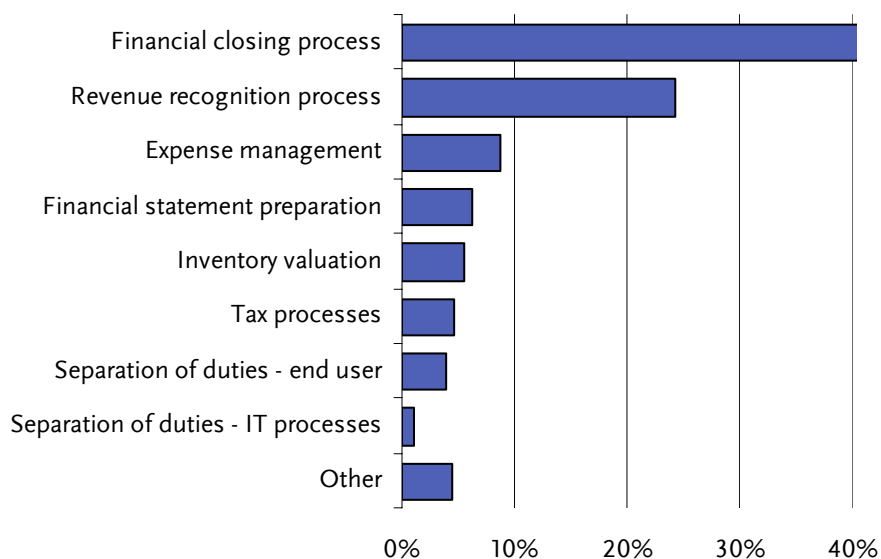


## THE IMPACT OF TECHNOLOGY

Companies are expanding their understanding of technology to support process automation. As shown in Figure 13, the top areas where respondents believe technology can be most beneficial are the financial close process and the revenue recognition process, followed by a number of other processes that companies perceive to be less of an issue.

**Figure 13**

Where do you believe software solutions would provide the greatest improvement? (n=685)

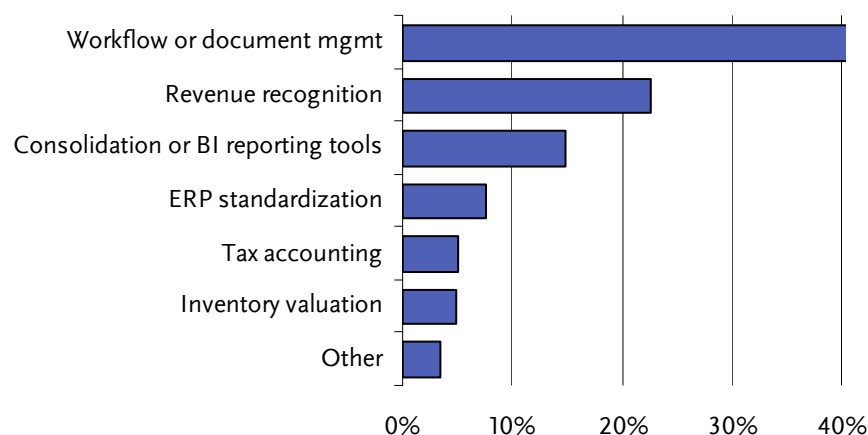


## IMPROVING THE FINANCIAL CLOSE PROCESS

When asked more specifically how the financial close process could be improved, “workflow or document management” to improve visibility and shorten the close process ranked first at 41%. Automating revenue recognition and BI tools round out the top three choices with no others receiving more than 10%.

**Figure 14**

Please identify where the financial close process could be most improved. (n=685)



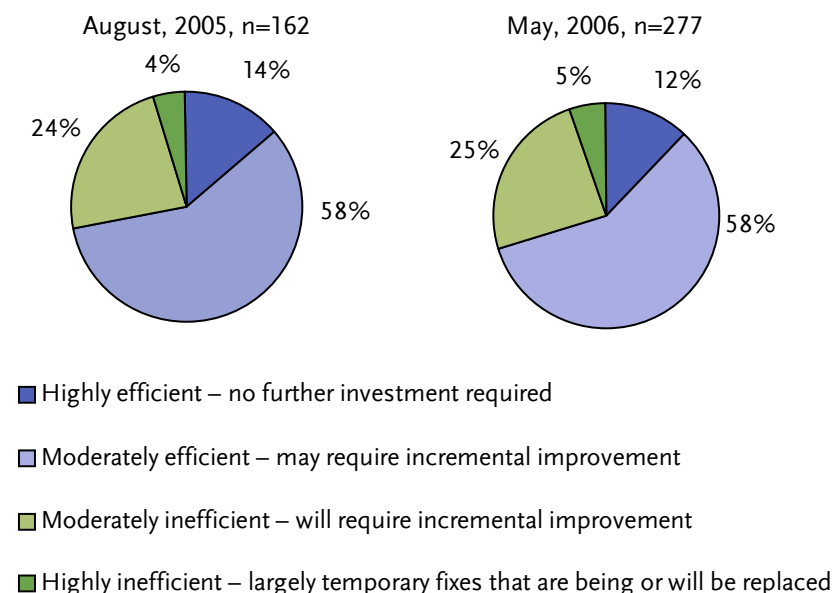
Revenue recognition is the top area targeted for future improvements, (previous page). This may be because it is an area that can be effectively impacted by technology, and improvements flow through to the financial close process.

## ANOTHER SNAPSHOT OF SARBANES-OXLEY 404 PROCESS EFFICIENCY

We first asked about the efficiency of Sarbox 404 compliance processes in August of 2005. The results for public companies are consistent between then and now, as the comparison in Figure 15 shows. Companies continue to question the value of excessive control activities, and are trying to determine the impact of recent guidance from the PCAOB on "top down, risk based" approaches.

**Figure 15**  
**Public Companies Only**

How would you rate the efficiency of your key compliance processes for Sarbanes-Oxley 404?



## SUMMARY

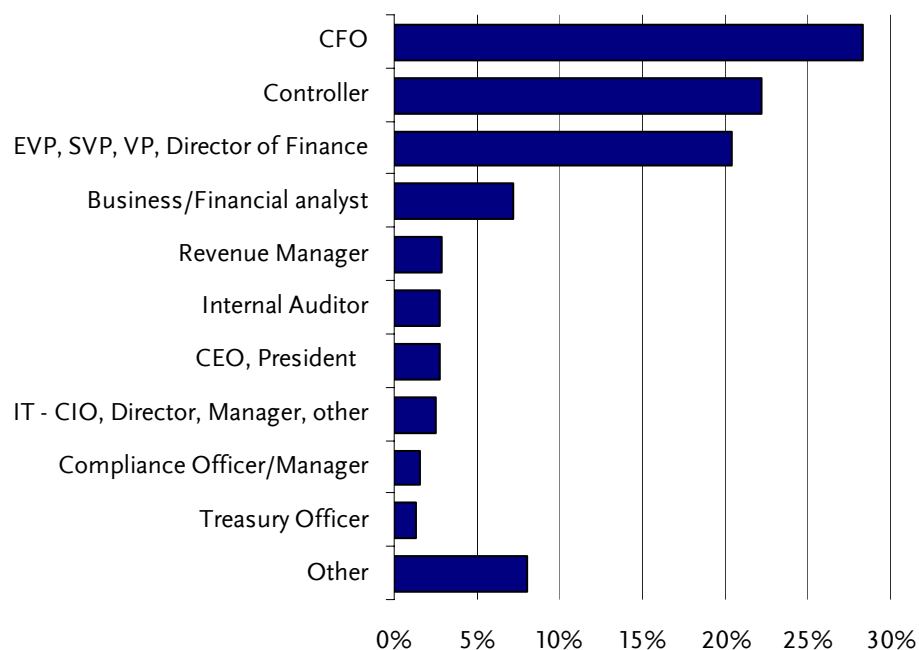
This survey highlighted three key themes: 1) Key control weaknesses in the revenue recognition process; 2) The pervasive use of spreadsheets in finance, and 3) Increasing attention on the elements of the financial close process. Revenue recognition and related reporting processes are not well-supported by Financial/ERP systems. Companies are filling the gaps with spreadsheets despite the fact that they violate key compliance principles. Clearly, new capabilities are needed.

Many of the risks, productivity sinkholes, and infrastructure challenges discussed in this report are interrelated. Companies should look at key areas of risk, such as revenue recognition, and explore solutions that automate these processes *across* enterprise systems. According to IDC's Wilhide, "The concept of intelligent process automation that enhances but does not necessarily replace enterprise systems, as an emerging standard that can close the missing link in operational efficiency."

## DEMOGRAPHICS

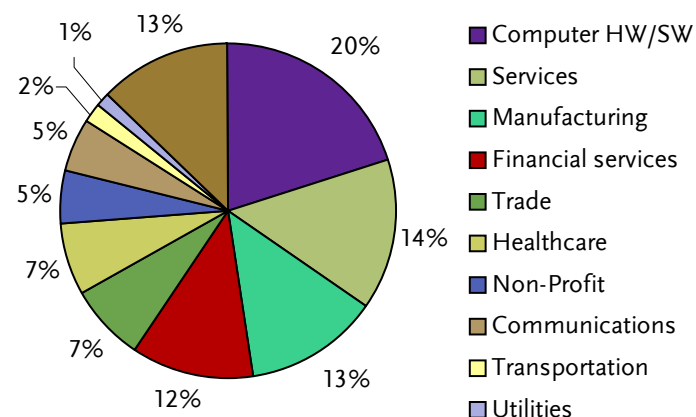
**Figure 16**

What is your title? (n=685)



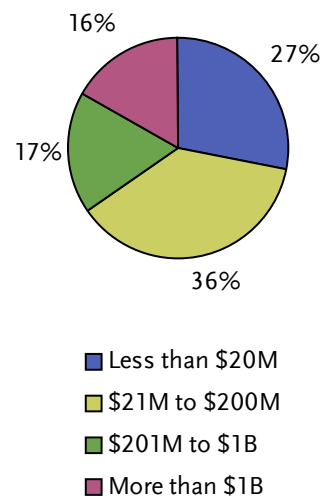
**Figure 17**

What is your company's main industry? (n=685)



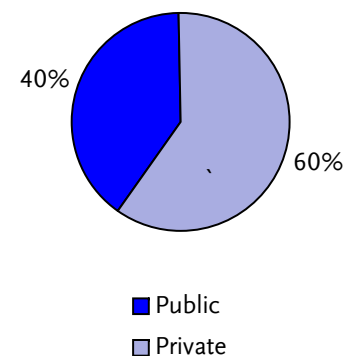
**Figure 18**

What was your company's approximate revenue in 2005? (n=685)



**Figure 19**

What is the ownership structure of your company? (n=685)



## ABOUT REVENUERECOGNITION.COM

RevenueRecognition.com is dedicated to educating finance professionals on revenue management and related issues. The site focuses on revenue recognition, Sarbanes-Oxley compliance, internal controls, corporate governance/ethics, SEC and FASB guideline compliance, M&A issues, contract management, revenue accounting, revenue reporting and forecasting, and industry specific revenue challenges. Contact us at: [info@revenuerecognition.com](mailto:info@revenuerecognition.com).

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