



Corporate Transparency: Addressing Sarbanes-Oxley in Today's Insurance Industry



FileNet in Insurance

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"The Sarbanes-Oxley Act, designed to enhance and enforce corporate governance and accountability, contains serious provisions for the creation, management, security, distribution, archiving, and disposal of vast amounts and varieties of corporate content, including but not limited to trade reports, ledgers, electronic communications (e.g., email, IM, audio), memos, and correspondence - in both electronic and paper form. The need for companies subject to the Act to re-evaluate, consolidate, and integrate enterprise content management (ECM) strategies with records management (RM) has never been greater."

– META Group, 2003 ^[1]

Executive Summary

Within the Insurance industry, the advent of the Sarbanes-Oxley Act of 2002 has created an almost unprecedented level of concern and activity regarding financial reporting and regulatory compliance. Insurance organizations are being forced not only to assume full responsibility for the information included in their financial reports but also to review and certify the procedures by which they gather and compile this information in the first place.

In an industry that relies heavily on perceptions of credibility and trust, Insurance companies are particularly concerned with the issue of accountability. For them, compliance is more than a priority from a regulatory standpoint; compliance is absolutely essential to the integrity of the corporate brand and to retaining customers in a fiercely competitive marketplace. The direct costs of non-compliance through fines, penalties, and litigation can be high. Over time, however, indirect costs from lost credibility and corresponding loss of market share, customer loyalty, and revenue can prove even higher.

Many, including FileNet, see corporate transparency as one of the keys to regulatory compliance now and in the future. As William B. Harrison, Jr., Chairman and CEO of JP Morgan Chase states unequivocally in his 2003 annual letter to shareholders, "Any time there is the spectacle of fraud and corruption, it highlights the need for transparency, accountability, and strong corporate governance."

In essence, corporate transparency is the ability to gain a better view into business activity as it takes place throughout the enterprise and, from there, to control this activity. The enterprise achieves transparency when access to critical information is more immediate and decision-making is more rapid and effective. Therefore, technologies that enable organizations to actively monitor their business processes, produce meaningful and timely analytical information, and manage ever-increasing quantities of information have come to the forefront of the drive to compliance.

As a result, Enterprise Content Management (ECM) is rapidly becoming a leading solution for ensuring corporate compliance. ECM solutions are uniquely focused on managing complex business processes, and on the data and information that drive these processes. For this reason, ECM is ideally suited to address the complexities of Sarbanes-Oxley and other regulatory requirements. By combining process, content, and connectivity, FileNet ECM allows Insurance organizations to automate and control their reporting processes. FileNet ECM also provides a proven architecture for accomplishing process efficiencies and cost reductions, enabling Insurance organizations to reduce the cost of compliance and achieve meaningful competitive advantage.

In the following sections, we will detail some of the critical business issues associated with the Sarbanes-Oxley Act and then illustrate how ECM addresses these issues to accomplish a greater degree of corporate transparency.

Sarbanes-Oxley is one of many compliance issues that confront today's Insurance organizations. For years, Securities and Investment firms have been subject to SEC regulation and compliance requirements. And, in the coming months, a revised Basel Capital Accord (Basel II) will be rolled out to the industry, introducing a whole new set of risk management and compliance standards for Insurance companies. Following are just some of the regulations and standards to which Insurance companies must comply:

- *Basel II*
- *ACIPA, FASB, IASB*
- *HIPAA*
- *MISMO*
- *Patriot Act*
- *SEC Regulations (17a-4)*

Far from simply a point solution for Sarbanes-Oxley, FileNet ECM provides an enterprise platform for addressing a myriad of compliance-related requirements. From secure document retention to complex process management and automation, FileNet ECM forms a single, integrated, enterprise platform for accomplishing corporate transparency and ensuring regulatory compliance.

Sarbanes-Oxley: A Difficult and Costly Proposition

The Sarbanes-Oxley Act of 2002 was crafted in the wake of corporate investing scandals such as those involving Enron and WorldCom. In these instances, financial reporting was not only inaccurate but also deliberately misrepresented. Therefore, at its most basic level, Sarbanes-Oxley is about restoring investor confidence and mandating senior executive accountability for corporate financial reports. At the same time, compliance can be difficult and costly. For this reason, Insurance organizations are seeking solutions that will help them to comply with Sarbanes-Oxley while simultaneously delivering cost savings and even competitive advantage.

Focusing on Sections 302 and 404

In developing their compliance strategies, most corporations have focused heavily on Sections 302 and 404 of the Sarbanes-Oxley Act.

In brief, Section 302 establishes corporate responsibility for financial reports, requiring that the organization's principal executive and financial officers certify the contents of their corporate reports. As signing officers, these senior executives are also responsible for establishing and maintaining internal controls for compiling financial information. Sarbanes-Oxley incorporates significant financial penalties and prison terms for corporate officers who certify financial reports that are prepared in a manner inconsistent with established controls or that deliberately contain false or misleading financial information.

While Section 302 addresses the most immediate compliance requirements for all corporations subject to the Sarbanes-Oxley Act, it is Section 404 that has created the greatest overall concern. Section 404 establishes direct management responsibility for the assessment of internal controls. In other words, for all annual financial reports produced after June 15, 2004, management is required to include an assessment of internal controls and procedures for producing financial reporting information. Additionally, the corporation's public accounting firm is required to attest to this assessment. Therefore, Insurance organizations must not only document their internal procedures but must demonstrate that they have strictly adhered to them. This effort represents perhaps the most difficult and complex aspect of compliance under Sarbanes-Oxley.

Compliance with Sarbanes-Oxley, and particularly Section 404, requires a remarkable degree of corporate transparency. Corporations must establish stringent controls not only to document critical processes but also to ensure that these processes are carried out. Additionally, senior management requires entirely new levels of visibility into reporting processes to gain the confidence to certify the content of their financial reports. Finally, corporations need to establish a complex, bottom-up approach for evaluating their internal controls,

"Indeed, in a survey released this week by Financial Executives International, executives at large cap public companies said the effort to comply with Section 404 of [Sarbanes-Oxley] has jacked up their external audit fees by 35%.

On average, the respondents said they expect to spend more than 6,000 hours – including internal resources, external resources and attestation time – getting their internal controls up to snuff."

– CFO.com, 2003^[2]

soliciting individual input and assessment from across the enterprise. Put another way, Sarbanes-Oxley solutions need to support top-down visibility and oversight while enabling bottom-up input into both reporting and control assessment.

ECM's ability to enable thorough and consistent information availability across processes allows corporations to make better decisions in compliance with Section 302. FileNet ECM helps allow executives to comply with Section 404 without requiring an exorbitant amount of time, cost, or risk to the individual or corporation.

The Spiraling Cost of Compliance

With the Sarbanes-Oxley Act serving as a goal for compliance, many Insurance organizations are scrambling to meet stated deadlines. This flurry of activity has created an unfortunate side effect: the cost of compliance has rapidly begun to escalate and, with other equally complex issues (such as the Basel II Capital Accord) forthcoming, the increase appears likely to continue.

To achieve compliance quickly, many Insurance organizations have invested heavily in consulting services. This has led to a substantial increase in both consulting and external audit fees industry-wide. A dramatic increase in insurance premiums has proven to be another, hidden, cost of Sarbanes-Oxley. Gartner, Inc. recently reported that, "in early 2003, director and officer insurance premiums had exploded by 300% to 900% over 2001 levels. Professional liability insurance costs for accountants have risen similarly, increasing the cost of outside auditing services."^[3]

Many organizations are now turning to the more complex, and costly, effort to document their internal controls in accord with Section 404. As they do so, they are looking not only for near-term fixes but also for compliance solutions that can address future regulatory requirements. While simple point solutions may address present-day Sarbanes-Oxley requirements, they may be unable to scale to address new Sarbanes-Oxley requirements as they evolve, not to mention other compliance requirements such as those associated with Basel II.

Achieving Competitive Advantage

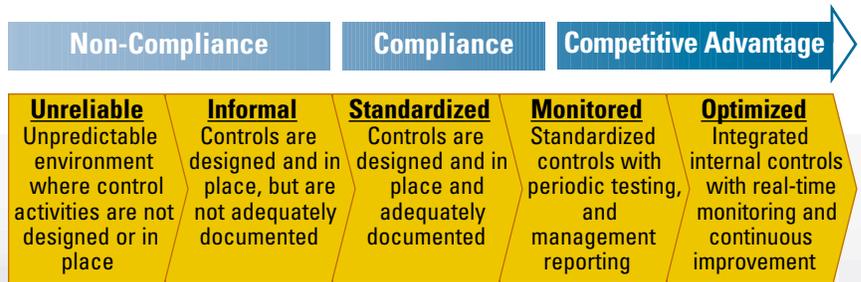
Compliance is inherently evolutionary. Regulatory initiatives, such as Sarbanes-Oxley, have developed relatively recently, and will continue to evolve. Among others, the Patriot Act is likely to undergo future iterations, and a new version of the Basel Capital Accord is expected in late 2003. In addition, regulatory agencies such as the SEC will also continue to evolve in their own understanding and interpretations of various compliance regulations and industry practices.

"Financial Services organizations that are struggling to come to grips with the full implication of Section 404 are not alone. In a recent industry survey conducted by PeopleSoft, seventy-one percent (71%) of respondents "believe that Section 404, which requires business process audits and documentation to support internal controls certification, is the most critical part of the Sarbanes-Oxley Act."

"Compliance with Sarbanes-Oxley and all federally administered corporate financial reporting requirements will be achieved most efficiently with enterprise-wide data transparency and real-time information sharing."

– Gartner, 2003 [5]

As a result, many Insurance organizations are pursuing Sarbanes-Oxley solutions not only from the standpoint of compliance but also from the standpoint of establishing sustainable competitive advantage. The graphic appearing below, originally developed by PriceWaterhouseCoopers, illustrates the general progression of compliance efforts. Currently, most public corporations are moving aggressively toward a "standardized" state defined by established and adequately documented internal controls. They are actively pursuing compliance with Section 404.



– PriceWaterhouseCoopers, 2002 [4]

However, a growing group of Insurance companies are looking to move beyond compliance in the narrowest sense. Instead, they are looking to derive additional value from their efforts to achieve relative competitive advantage. Confirming this, a recent PeopleSoft survey concludes that, "Sixty-five percent (65%) [of respondents] will seek to leverage their Sarbanes-Oxley initiatives to achieve process improvements that will increase business efficiencies and competitive advantage."

These organizations are working to implement compliance solutions that ultimately will enable an "optimized" environment that delivers real-time monitoring — true transparency — and continuous, rapid process improvement. Thus empowered, these organizations will be able to dramatically reduce the cost of compliance, accomplish near real-time reporting, and rapidly respond to current and future regulatory requirements.

Enterprise Content Management and Compliance

FileNet Enterprise Content Management (ECM) provides an ideal platform for ensuring enterprise compliance with the various aspects of the Sarbanes-Oxley Act. Beyond compliance, FileNet ECM can also enable corporate transparency, providing top-down visibility for management and allowing real-time reporting and ready access to information for investors, auditors, and regulators. FileNet ECM is designed to ensure regulatory processes themselves are effectively automated and adhere to appropriate controls.

FileNet ECM is comprised of three critical elements:

- **Process** – Process resides at the core of all Insurance organizations. Simply put, process is how business gets done. FileNet ECM incorporates Business Process Management functionality to automate, control, and accelerate

"The Sarbanes-Oxley Act (SOX) requires executive sign-off on process documentation and proof that the process executed. End users are inquiring whether business process management suites are useful tools in achieving compliance. Modeling provides self-documenting evidence of the process and the ability to embed controls; process orchestration engines automate much of the process, ensuring consistency and fewer errors; business rules ensure transactions are executed according to the expected process; monitoring and analytic tools provide audit trails for process execution and exception handling; and simulation/optimization provides a path for process improvement. Business process management implementations also include the ability to streamline and optimize business processes."

– META Group, 2003^[6]

business processes. More than simple workflow automation, FileNet ECM enables processes to be modeled, analyzed, and continually improved to help ensure ongoing compliance and maximum operational efficiency.

- **Content** – Content is comprised of information in one form or another. Content can include scanned images, electronic documents (e.g. MS Excel files), rich media, faxes, and even structured data (information that is typically stored in a database). Over its 20+ year history, FileNet has achieved an unparalleled track record in providing enterprise-class content management solutions for Insurance organizations.
- **Connectivity** – Technology cannot exist in a vacuum. To gain maximum value from both new and existing IT investments, systems must be able to connect to one another. FileNet ECM also incorporates business integration capabilities that allow Insurance organizations to leverage their legacy IT architectures in building new enterprise solutions.

Together, these components of FileNet ECM constitute a solution that can address immediate compliance issues and respond to new regulatory requirements as they emerge. Additionally, FileNet ECM's inherent capabilities to drive process automation and efficiency can dramatically reduce the cost of compliance, shorten reporting timeframes, and enhance overall competitive advantage.

Ensuring Compliance in Financial Reporting

Responding to Section 302 of the Sarbanes-Oxley Act, organizations can use FileNet ECM to securely store and retrieve virtually unlimited quantities of information at any point in time during the required seven-year audit retention period (Section 103). FileNet ECM also provides robust search capabilities to rapidly locate and access information stored in the FileNet repository. In addition, ECM supports versioning control and check-in/check-out functionality, enabling management visibility and detailed audit trails.

FileNet Business Process Management capabilities enable a direct linkage between process documentation and execution. As a result, when changes occur in the documented process, they roll out immediately to the enterprise for day-forward adherence. FileNet ECM does more than simply document processes. By graphically modeling procedures, FileNet ECM allows them to be deployed immediately, accelerating and managing information gathering.

With ECM, management can also rapidly determine the source and approval process for critical financial information. Management can represent the process by which information was gathered, identify participants, and even modify the process for greater control at any point in time. In addition, FileNet ECM can track versions of the processes, and roll them back to a specific point in time to enable companies to review and represent how the processes themselves have evolved.

"Bottom Line: Process definition and monitoring are at the heart of compliance. Enterprises with multiple complex needs should consider using general-purpose business process management tools to build compliance solutions that are flexible and that can be used to build processes to comply with any existing or future legislation."

– Gartner, 2003^[7]

FileNet ECM introduces an exceptional level of control and ultimately helps enable corporate responsibility for financial reports. To provide top-down visibility, FileNet ECM also incorporates audit and management capabilities via a number of industry-standard portal products, providing a dashboard view of compliance content and processes to key internal and external participants. With FileNet ECM, management can identify the point at which required information is being created, compiled, or approved and can review the corresponding controls to rapidly assess process adherence.

FileNet ECM also allows auditors to directly view compliance processes, documentation, and reporting information. With secure, yet direct access to financial reporting documentation and process information, corporate transparency greatly increases. As a result, organizations can achieve meaningful cost reductions from more efficient auditor assessments and rapid response to regulatory inquiries.

Assessing Internal Controls

Beyond being required to assume full responsibility for the information included in their financial reports, organizations must review and certify the procedures they use to gather and compile this information in the first place. FileNet ECM can help organizations eliminate this area of concern.

- First, FileNet ECM provides a single, secure, enterprise platform for storing critical process documentation. This documentation can be effectively managed and rapidly retrieved across the enterprise, ensuring that managers, auditors, and others can access critical compliance information.
- Second, FileNet ECM supports the rapid development and modeling of business assessment processes from the bottom-up. From there, FileNet ECM provides full automation and responsive control. Management can assign specific tasks and activities to key personnel to assist in the complex process of gathering detailed assessment information. Management can also monitor the process in real-time to immediately determine the status of any or all tasks and activities.
- Third, FileNet Forms Manager can streamline the assessment process itself, allowing management to solicit specific information – within the context of a controlled, automated business process – to accumulate required documentation and attestations.

Making use of FileNet's Business Process Management capabilities, procedures can be immediately implemented once they are created and documented. As a result, changes to documentation are immediately executed and, conversely, changes in process are instantaneously documented as well. As noted earlier, FileNet ECM is also capable of maintaining previous versions of business processes, ensuring that an accurate historical record of assessment procedures is preserved.

"Transparent, real-time systems will lower the overall cost of compliance with the greatest efficiency in data reporting and verification.

Compliance with Sarbanes-Oxley magnifies the advantages of real-time information management and straight through processing."

– Gartner, 2003 ^[8]

Moving to Real-time Reporting

Compliance also drives the need for accelerated or even real-time reporting. In Section 409 of Sarbanes-Oxley, publicly traded corporations are required to "disclose to the public on a rapid and current basis" any material changes in the financial condition of their organization. Moreover, the definition of a "material change" is rapidly expanding to include items as detailed as the loss of a principal customer or account. In addition, Insurance companies will have to view changes to loss reserves in a totally new light. Insurers will have to gain a clearer understanding of reserving practices for claims, as well as other events that have an impact on underwriting results.

This is an issue of transparency and an aspect of compliance that FileNet ECM is uniquely suited to address. FileNet's ECM architecture is event-driven, meaning that it allows critical events to be identified within the context of a business process and initiates an automated response or corresponding set of activities. Organizations can thus leverage FileNet ECM to actively monitor for events that represent "material changes" and trigger a responsive, controlled process to ensure that required disclosures are generated within the time period prescribed by regulation.

FileNet ECM also offers rich rules engine integration, enabling Insurance companies to separate their automated processes from the business rules that drive them. FileNet ECM integrates with industry standard rules engines that allow companies to define complex business rules in natural language. This way, Insurance organizations can establish business rules that define material changes in the organization and require subsequent action. As the prescribed list of material changes continues to expand, organizations can rapidly modify these rules without complex and costly recoding of their business processes.

Lowering the Cost of Compliance

An effective solution for addressing corporate compliance, FileNet ECM is an enterprise-class platform that can deliver significant business value across the enterprise. In addressing compliance requirements, the tremendous opportunity for cycle-time reductions often goes overlooked, as do the cost savings from preparing financial reports and assessing internal procedures.

Simply put, compliance is a cost of doing business. From this perspective, Insurance companies should pursue solutions that are also able to drive efficiency and enable automation. To this point, FileNet's ECM solutions are designed to reduce the overall cost of compliance to the organization and provide added benefits in terms of brand integrity and competitive advantage.

FileNet literally invented the concept of workflow and has significant experience in accomplishing efficiencies and meaningful cost savings for leading Insurance companies. With FileNet's robust Business Process Management capabilities, FileNet can help reduce the timeframes and costs associated with financial reporting and compliance. FileNet ECM also enables ongoing process improvement, allowing Insurance organizations to refine their compliance processes over time and achieve additional cost savings as a result.

"Organizations must balance the tactical investments required to meet short-term regulatory deadlines with the long-term requirements to strategically manage overall regulatory demands while simultaneously improving business performance and efficiency."

– META Group, 2003 ^[9]

Conclusion

The Sarbanes-Oxley Act of 2002 is the latest and perhaps most stringent of a series of regulatory initiatives that applies to the Insurance industry. Perhaps more so than any other regulatory issue, Sarbanes-Oxley has highlighted the need for greater accountability to management, shareholders, auditors, investors, and even customers. Sarbanes-Oxley has also illustrated the continuously changing nature of corporate compliance and the need for solutions that can adapt to future regulatory requirements.

FileNet ECM is uniquely suited to address the varied requirements of Sarbanes-Oxley. By combining process, content, and connectivity, FileNet ECM allows Insurance companies to automate and control their reporting processes. Additionally, FileNet ECM provides an ideal platform for documenting, assessing, and monitoring internal controls in compliance with Section 404.

More than a point solution for Sarbanes-Oxley, FileNet ECM is an enterprise platform for content and business process management that can scale to address the many compliance-related issues that Insurance companies confront. Not only can FileNet ECM help to ensure enterprise compliance, it can also help to reduce the cost of compliance through enabling greater efficiency and automation.

In summary, response to Sarbanes-Oxley is more than a matter of compliance. It is also a matter of improving corporate transparency rapidly to efficiently respond to new and evolving regulatory policies. Sarbanes-Oxley and other compliance issues are the catalysts for such corporate initiatives, laying the framework for corporations to realize meaningful competitive advantage in brand and customer service.

About FileNet

FileNet Corporation (NASDAQ: FILE) helps organizations make better decisions faster by managing the content and processes that drive business. FileNet Enterprise Content Management (ECM) solutions allow customers to build and sustain competitive advantage by managing content throughout their organizations, automating and streamlining their business processes, and providing the full spectrum of connectivity needed to simplify their critical and everyday decision making.

Headquartered in Costa Mesa, California, FileNet serves nearly 3,900 customers, including 21 of the top 30 US bank holding companies, more than 350 global banks, and nearly 1000 Financial Services organizations.

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