

Shoes & SOX

Keep Your Organization Running
at the Front of the Pack

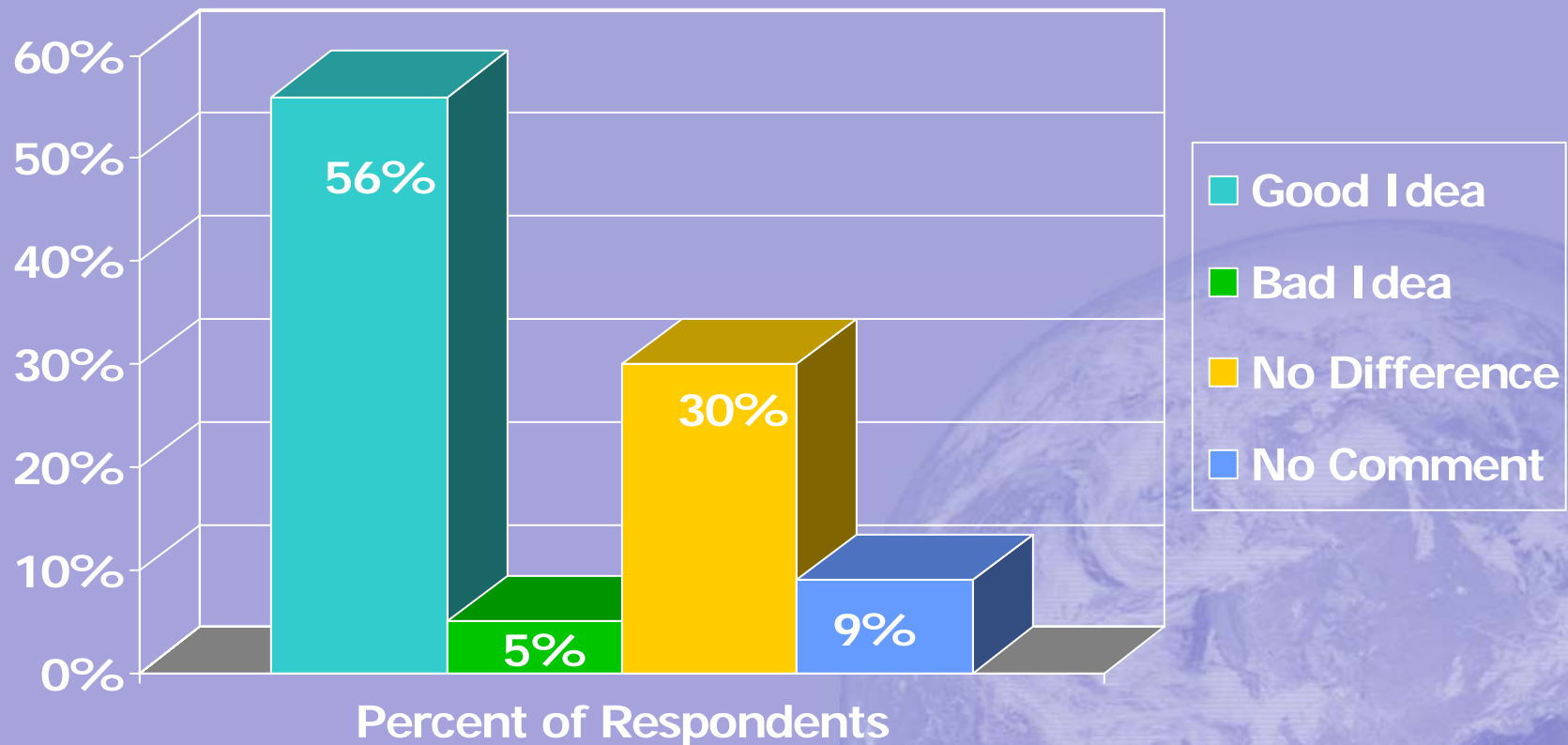
Presented by:
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Objectives of presentation

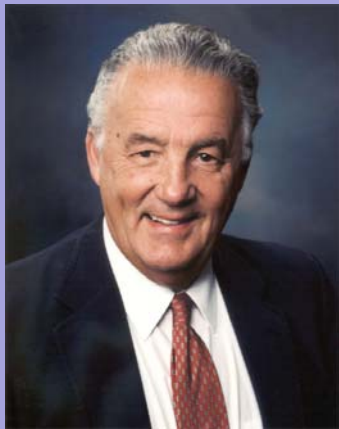
- Understand Sarbanes-Oxley (SOX)
- Know what parts of SOX apply to your organization and learn about other new and proposed legislation
- Use SOX provisions as guidelines to move your organization to the front of the pack

A recent survey released by the Center for Audit Quality says the passage of Sarbanes-Oxley was..



SOX: Sarbanes-Oxley Act

Official title: Public Company Accounting Reform and Investor Protection Act of 2002.



Sections of SOX

- I. Public Company Accounting Oversight Board
- II. Auditor Independence
- III. Corporate Responsibility
- IV. Enhanced Financial Disclosures
- V. Analyst Conflicts of Interest
- VI. Commission Resources and Authority
- VII. Studies and Reports
- VIII. Corp. and Criminal Fraud Accountability
- IX. White Collar Crime Penalty
- X. Corp. tax returns
- XI. Corporate Fraud and Accountability

Section VIII – Corporate and Criminal Fraud Accountability

- Applies to all entities
 - Criminal penalties for altering documents
 - Policy should be implemented to ensure compliance with legal provisions to preserve documents and when it is ok to shred documents
 - Protection of employees who provide evidence of fraud (Whistleblower protection)
 - Create a confidential reporting system
 - Fraud hotline
 - Audit committee
 - Policy should be implemented to protect whistleblowers

Section XI – Corporate Fraud and Accountability

- Defines that those who tamper, alter, destroy or conceals documents during and official proceeding or otherwise obstructs, influences or impedes any official proceeding, can be fined or imprisoned for not more than 20 years!
- Provides for no retaliation against whistleblowers



Utilizing SOX to Create the Gold Standard



- II. Auditor Independence
- III. Corporate Responsibility
- IV. Enhanced Financial Disclosures

Section II – Auditor Independence

- Provisions – applicable only to publicly traded companies
 - Requires Audit Committee to be responsible for oversight of auditors
 - Rotation of reviewing audit partner every 5 years
 - Prohibits certain services that can be provided by the independent auditors

Prohibited Services



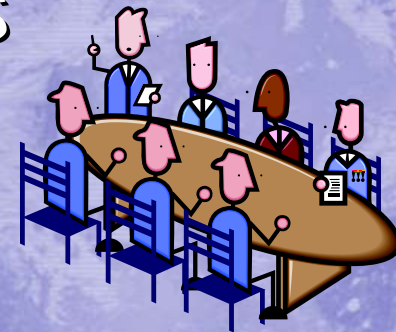
- Sarbanes-Oxley – publicly traded companies only
 - Bookkeeping
 - Financial systems design and implementation
 - Appraisal or valuation
 - Actuarial services
 - Internal audit
 - Management functions or human resources
 - Broker or investment advisor
 - Legal services
- AICPA – Many of the same types of services. However, less strict.

Section III – Corporate Responsibility

- Provisions – applicable only to publicly traded companies
 - CEO and CFO sign annual and quarterly reports
 - Audit committee's role defined

SOX Audit Committee

- Comprised of independent board members
- Must establish procedures for receipt, retention and treatment of complaints regarding accounting, internal control and auditing matters, including when received in confidence or by anonymous submission.
- Hire the independent auditor



Audit Committee

- Understand the entity
- Understand the entities environment
- Understand internal controls
- Communicate with the auditor
- Communicate with management

Section IV – Enhanced Financial Disclosures

- Provisions – applicable only to publicly traded companies
 - Disclose all material off-balance sheet transactions
 - Enhanced related party disclosures
 - Code of ethics for senior financial officers, with disclosure
 - Requires one member of audit committee to be a financial expert, with disclosure
 - Management assessment of internal controls and report

SOX – Code of Ethics

- Disclosure whether or not, and if not, the reason therefore, if a code of ethics for senior financial management has been adopted
- Code of ethics should include statements regarding:
 - Honest and ethical conduct, including ethical handling of conflicts of interest
 - Full, fair, accurate, understandable and timely disclosure of financial reports
 - Compliance with laws and regulations

SOX – Financial Expertise

- Understanding of GAAP
- Experience preparing or auditing financial statements of similar type of organization
- Experience applying principles of GAAP at similar type of organization
- Experience with internal controls
- Understanding of audit committee functions

Expertise vs. Literacy

- Only one member of the audit committee must be a financial expert
- Entire board should be financially literate
 - Know how to read basic financial statements
 - Can perform basic ratio analysis
 - Horizontal
 - Vertical
 - Understands industry benchmarks



SOX – Management Assessment of Internal Controls

- Requires management to report on internal control including:
 - Management's responsibility for design and implementation of internal control structure and financial reporting
 - An assessment of the effectiveness of internal control structure and procedures for financial reporting

Other Best Practices from Sarbanes-Oxley

- Conflict of interest policy development
- Business continuity planning
- Internal control policy development
- Board responsibility for financial reporting
- Board financial literacy
- Board industry awareness
- Client files and privacy issues

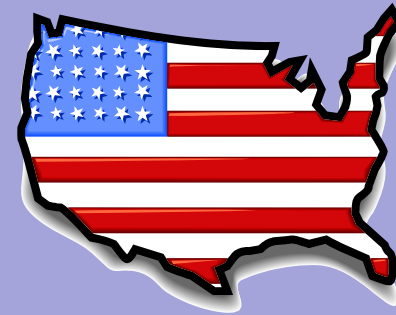
Back to survey by Center for Audit Quality

- 79% believe the requirement to establish independent audit committees has had a positive effect.
- 76% say that external audits reporting to independent board-based audit committee has had a positive effect.

Back to survey by Center for Audit Quality

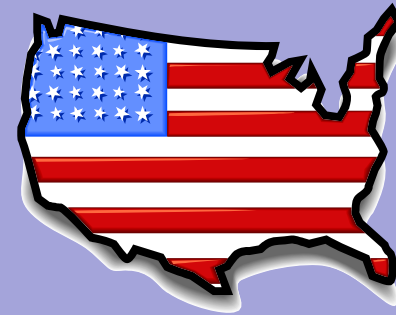
- **76%** believe the requirement for companies to evaluate and disclose their internal controls and for external auditors to attest such disclosures has been positive.
- **74%** say that certification of financial reports by CEOs and CFO has had a positive effect.

Other Legislation



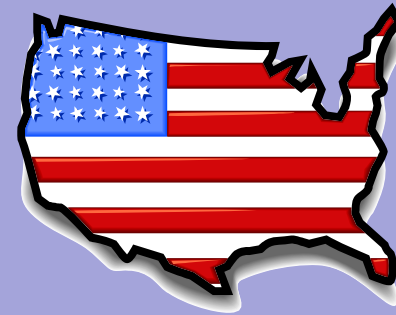
- California – Nonprofit Integrity Act of 2004
 - All NFPs with > \$2M must have audit
 - Audit must be by independent CPA
 - Must be overseen by audit committee, which must be made up of > 50% of non-finance committee members
 - Audit must be made available to public and attorney general just like the Form 990

Other Legislation



- Massachusetts – to be voted on later this year – Act to Promote Financial Integrity of Public Charities (Similar to California)
- Massachusetts – passed in October 2004
 - All NFPs with > \$500K must have audit
 - All NFPs with \$100K to \$500K must have a CPA review
- New Hampshire – passed in 2006
 - All NFPs with > \$500K to have and audit along with Form 990
 - All NFPs renewing registration must submit audited financials and Form 990

Other Legislation



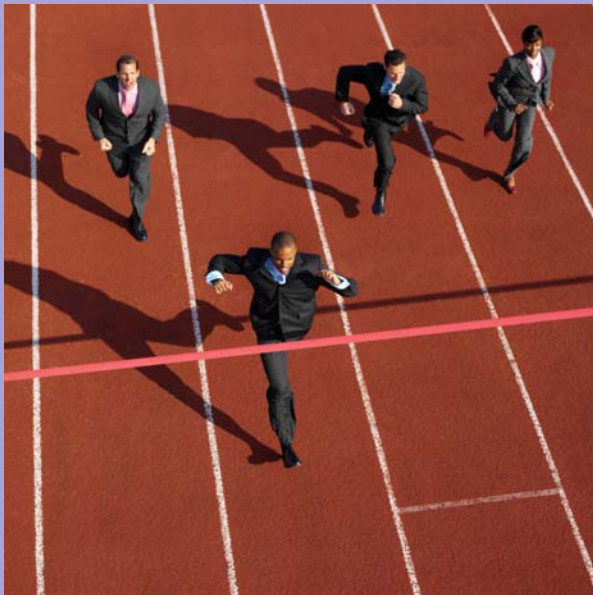
- Connecticut – passed June 2005
 - All charities must submit a financial report to Department of Consumer Protection
 - All NFPs > \$200K must also file audit report
- Kansas – passed May 2005
 - All charities must submit a Form 990 before soliciting funds
 - All NFPs with contributions > \$500K must submit audited financial statements
- More states also have bills proposed in 2007

Action Items

- Ensure compliance with applicable provisions for document retention and whistleblower policies.
- Outline policies to implement
 - Audit committee
 - Board financial literacy program
 - Internal control review
 - ED and Finance Director sign financial reports



Conclusion



- Understand SOX
- Know what part of SOX applies to your organization and awareness of other new and proposed legislation
- Use SOX provisions as guidelines to move your organization to the front of the pack

Resources

- Handouts
 - Audit committee responsibilities related to fraud
 - Sample whistleblower policy
 - Records retention schedule
 - Audit committee self-evaluation
 - Independence guidance, including sample conflict of interest policy
- Books, Articles and Websites
 - SOX for Nonprofits, by Peggy Jackson and Toni Fogarty, Wiley & Sons, 2005.
 - Full text of Sarbanes-Oxley Act of 2002
 - Guidestar www.Guidestar.org
 - Center for Audit Quality www.thecaq.org
 - PPC Nonprofit Update & Guide to Audits of Nonpublic Entities, 2007.
 - “What has Sarbanes-Oxley Done for You Lately?” Wisconsin Law Journal, Tracy Coenen, 2006.
 - National Council of Nonprofit Associations www.ncna.org
 - American Institute of CPAs www.aicpa.org