

SARBANES-OXLEY

Lessons Learned: A Ground Level View of a Client Experience

Introduction

Recent events, including terrorist attacks and the collapse of corporate giants such as Enron and WorldCom, have resulted in a spate of new regulations. The intent of the regulations is not only to ensure accuracy in financial reporting, but also to restore and preserve investor confidence in the American capital markets.

One example of new regulation is the Sarbanes-Oxley (SOX) Act of 2002. The law essentially holds CEOs of public companies liable for the accuracy of the companies' financial statements. Its enactment was welcomed by the investing public.

Although beneficial in many respects, not the least of which is a mandatory review of the efficacy of affected companies' internal controls, the extra effort and expense comes at an inopportune time. As companies attempt to trim unnecessary expenditures and increase productivity, the requirement to document and test internal controls is a less than welcome addition to their list of priorities.

Jeremiah Associates worked closely with a major client to develop and install a process that would help to ensure the internal control requirements of SOX are met. It is from this perspective that we have transitioned into the "Phase Two – Lessons Learned from a Ground Level View" aspect of this undertaking.

Mid 2004 — Meet the Initial Deadline

In the midst of the usual set of competing priorities in a climate of reduced budgets and staffing, SOX was one of many projects facing tight deadlines. As would be expected, the tight deadlines resulted in less than the needed amount of planning, coordination and overall guidance for SOX. It quickly became evident that the hastily adopted process was sufficient for the initial round, but that significant changes would be needed thereafter.

Sorely missing were critical elements such as centralized coordination, standardization, guidance, training and quality assurance. The process encompassed too many internal controls, some of which were not applicable across the board. It also called for the redundant testing of multiple control points which would effectively uncover the same error(s).

Middle management, left largely on its own with the responsibility of putting in place the testing of established controls and retaining the documentation sufficient to demonstrate that the controls are in place also left a lot to be desired.

Complicating the job of SOX testers was the lack of project coordinators. In the absence of necessary guidance, issues such as frequency of testing, methods of testing and types of testing all generated an ongoing flurry of questions from SOX testers, who were constantly struggling to meet the progress checkpoints that management had established. As testing was completed, the absence of a unified MIS reporting system became apparent.

Although the initial effort sufficed for the first round, it created unnecessary difficulties for all involved parties. It soon became clear that a more streamlined and cost-effective process was needed.

Late 2004 — Learn From the Experience

Accepting the reality that SOX is an ongoing requirement is more than sufficient motivation to analyze the initial experience and apply time-tested management techniques to bring about the desired improvements. Many of the complications of the initial process immediately began to improve as centralized coordination, standardization, guidance and training were introduced.

A key element in progressing beyond the initial experience was the appointment of an internal SOX Coordinator. This paved the way for the needed improvements by establishing a process through which problems and shortcomings were carefully analyzed. Moving forward from the first objective, which focused mainly on meeting the deadline, the focus of the next iteration became how to achieve the objective of documenting and testing internal controls in the least costly and most efficient manner.

Early 2005 — Capitalize On the Lessons Learned

Centralized coordination now serves several purposes, namely to analyze the ongoing process, implement and announce needed improvements, and provide the necessary support. Standardization eliminates the confusion formerly caused by different meanings of key terms, and creates uniformity of testing and reporting of results. Guidance provides the all-important interpretation of the instructions issued to testers. Training facilitates the inevitable change of SOX testers as processes are either added or assigned to new sets of testers.

Finally, the planned implementation of a Quality Assurance Program serves as the pre-audit review through which the company ensures that it is not only complying with the requirements of SOX, but doing so in the most streamlined and cost-effective manner. QA will involve personal visits to SOX testers to ensure that they understand what is required of them, and to ensure that testing results meet the requirements.

Going Forward

Unless it is repealed or changed substantially, SOX is a part of our world. It is critical that SOX not be relegated to an onerous process that is performed in a perfunctory manner. This attitude would undermine much of the productive work that has been done to date. Obviously, the organization could then be at risk due to ineffective controls.

To prevent this, senior management must provide the positive example and encouragement needed by middle management and line staffers who serve as SOX testers. Senior management must also continue to drive the effort to streamline by adopting the appropriate data platform for recording and reporting testing results, and implementing measures which will continue to automate the manual aspects, such as the electronic retention of supporting documentation.

Here's another way to benefit: Make the most of this golden opportunity to analyze what processes should be re-worked, further automated or combined to create greater efficiency. And, utilize this forum, through which the company can analyze its errors in terms of causes, points of detection, timeliness of resolution and escalation of unresolved items. The quality control improvements which can potentially result from such a review can help to defray the costs of complying with SOX. Utilizing SOX in this way helps to achieve the elusive "win/win" that transforms your efforts into benefits.

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