

WHO OWNS THE GAPS: Sarbanes-Oxley Section 404

What catches chief officers' attention today is the provocative coverage of business leaders in jail without bond, on trial, fiefdoms lost. The Sarbanes-Oxley Act is bringing sweeping reforms that have an impact on broad areas of corporate governance, auditing and disclosure, and carry implications for nearly every CFO, CEO, COO, controller and board member in America.

When signing the Sarbanes-Oxley Act, President George W. Bush said, "Today I sign the most far-reaching reforms of American business practices since the time of Franklin Delano Roosevelt. This law says to shareholders that the information you receive from a company will be true and reliable, for those who deliberately sign their names to deception will be punished."

The Sarbanes-Oxley Act transfers liability and responsibility from the corporate entity to chief officers. Responsibility for implementing the act is assigned to the Securities and Exchange Commission, the U.S. investment markets regulator, and the new Public Company Accounting Oversight Board, which is charged with policing the accounting industry. The personal penalty for chief officers violating section 404, Management of Internal Controls -- the most complex and specialized to comply with -- is a fine of as much as \$5 million and/or imprisonment for up to 20 years.

Congress deliberately wrote Sarbanes-Oxley to ensure that CEOs would be held accountable for the accuracy of financial reporting and disclosure. Once the CEO signs the report that accompanies the annual filing, it is a done deal. Filing Sarbanes-Oxley section 404 is not like closing your financial books where you can, if you discover an error, file post-closing adjustments. Errors cannot be retroactively revised.

Section 404, often referred to as Attestation to 'Best Practice' Internal Controls, requires that management sign off on policies, processes, people and responsibilities, methodologies, and to verify that systems actually exist and are functioning effectively. Next, an independent auditor assesses and reports on the efficacy of internal controls.

The SEC has recommended section 404 evaluation criteria, COSO Integrated Framework <http://www.sec.gov/news/press/2003-66.htm>, which has, for more than a decade, provided auditors with the universal definitions of risk and internal control, as well as segregation of duties and competence, professionalism and responsibilities of management and employees.

The COSO triangle illustrates the way an organization is best managed. Its components are the evaluation criteria used to measure internal control. Working from the base to the tip, the evaluation criteria are: 1) Control Environment, 2) Risk Assessment, 3) Control Activities and 4) Monitoring. Wrap these principles with Information and Communication, and you are ready for section 404 Sarbanes-Oxley internal controls attestation.

The foundation of the pyramid, the control environment, establishes the values of the organization, providing direction and structure, and consequently affects the consciousness and actions of internal stakeholders. To ensure that your control environment is COSO-compliant and that your internal staff are accountable, a great portion of section 404 attestation-prep is management and employee skill-set registry, including core competency, identifying who is responsible for what transactions, and who monitors internal controls.

The level that the SEC and stockholders want is detailed. The audit is a snapshot of the organizational structure that also displays reporting relationships and duty-segregation. Gwen Thomas, Editorial Director SOX Online says: "This is data governance top down and data stewardship bottom up."

Innovative companies will need to create a knowledge management directory to control, monitor and track the risks required for corporate governance compliance. BetaWatch recommends proven, web-based data-gathering tools to build, monitor, evaluate, and continually refine the control environment, while at the same time monitoring the people, processes, and risks. The latter can be accomplished with the web-based data-gathering application KNETMAP™. The resulting knowledge-network map super-sizes information by visualizing the relationships between the people, processes and ownership.

The data gathered with web-based tools will be accurate and verifiable, enable corrective action and, most importantly, be adaptable to provide accurate and relevant information in a changing environment.

Thomas d'Aqino, president and chief executive of Canadian Council of Chief Executives recently said, "The biggest problem complying with corporate governance is that you are diverting your chief executive, and you are diverting your directors, and you are diverting your senior managers. What is it you are diverting them from? Well, you are diverting them from running the company."

Business process improvement web based tools help managers sign off on policies, processes, people and responsibilities. Use the best tools from COSO-competent consultants so you can manage a high-performance business and demonstrate good corporate governance too.

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