Sarbanes-Oxley Act Guideline

What is the Sarbanes-Oxley Act?

The Sarbanes-Oxley Act was passed in the US in 2002, having been drawn up following a number of high profile accounting scandals, such as Enron, that seriously dented investor confidence.

The Act brought significant legislative changes to financial practice and corporate governance regulation with the stated objective to "protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws."

Which companies are affected by Sarbanes-Oxley?

The Act applies to US public companies and their global subsidiaries and from June 2005 it will also apply to any foreign company whose shares are traded on the US stock exchange and those who are contemplating such a listing.

The US Securities and Exchange Commission (SEC) have extended the deadline for non US companies to comply with section 404 of the Sarbanes-Oxley Act to July 2006. The 12-month extension will allow most UK companies a full financial year to deal with the International Financial Reporting Standard (IFRS), the European Union's financial services action plan and the new listing regime in the UK before full compliance with Sarbanes-Oxley.

Who will this affect?

The Sarbanes-Oxley Act is likely to affect the following:

1. Agencies with US parents
2. Agencies with non US parents but who have a listing on the US stock market
   Agencies who have clients that are traded on the US stock market may also find they are requested to indicate that they are Sarbanes-Oxley compliant

What does the Sarbanes-Oxley Act require?

The Sarbanes-Oxley legislation is wide ranging and establishes new or enhanced standards for all US public company Boards, Management, and public accounting firms.

Under the terms of the act the CEO and CFO must certify that company accounts and other financial statements fairly represent their firm's financial position. In addition the company's management must state annually that they are responsible for financial control within their company, have assessed the effectiveness of their internal systems and processes for financial control and have confirmed their operation in practice.

Sarbanes-Oxley Act Guideline

Sarbanes-Oxley law contains 11 titles, or sections, ranging from additional Corporate Board responsibilities to criminal penalties. The act requires Security and Exchange Commission (SEC) to implement rulings on requirements to comply with the new law.

There are two main requirements of the act:

1. Section 302 - Management assessment of disclosure controls
    a. Disclosure of material information to the SEC
    b. changes to disclosure controls
    c. changes to internal control over financial reporting all known control deficiencies and weaknesses any acts of fraud
2. Section 404 - Management assessment of internal controls over financial reporting
    a. This section requires public companies to verify that their financial-reporting systems have the proper controls, such as ensuring that revenue is recognized correctly. More specifically measures must be put in place to evaluate design & effectiveness of internal controls disclose all significant deficiencies and material weaknesses disclose acts of fraud

The Sarbanes-Oxley Act requires that these changes be made to safeguard against possibility of fraud through contract compliance, written policies and stronger internal controls to match the contract compliance in line with the policies.

What does this mean in practice?

Agencies will need to ensure that every process that impacts upon the financial processes of the agency is fully documented. This is likely to impact a range of departments across the agency not just those in the financial department. There is likely for example to a significant impact upon IT departments in an era where much information is generated and stored electronically.

Agencies will need to ensure that all key risks are identified and that the controls they have in place match those risks.

Agencies will need to ensure that the key controls they have in place are tested and that any gaps they have in those controls are reported upon and closed.

For well run agencies this will be:

- an exercise in documentation
- an opportunity to identify operational improvements

For agencies with unknown control weaknesses Sarbanes-Oxley offers an opportunity to fix them.

Sarbanes-Oxley Act Guideline

For agencies with known control weaknesses Sarbanes-Oxley offers the opportunity to set the record straight.

What are the implications for supplying information that is knowingly false?

The act makes the chief executives and chief financial officers of companies personally responsible for the information that is included in their financial accounts and systems of internal financial control.

The penalties for supplying information that is knowingly false are severe:

1. 20 years imprisonment
2. $5m fine

Are there any benefits to be gained from Sarbanes-Oxley compliance?

Agencies may find that there are benefits of upgrading their financial management systems such as:

1. operations that are more streamlined
   - a better linkage between project management and financial reporting better management of internal and external resources better and more timely information leading to better decision making implementing a modern business management and finance system and allow agency management and staff to focus on the core business of the agency
2. cost efficiency is likely to have an impact upon the bottom line
   - clients and/or procurement departments may prefer to deal with agencies that are Sarbanes-Oxley compliant as this gives an indication that financial operations are transparent, well managed and accurately reported.

Sarbanes-Oxley website: http://www.sarbanes-oxley.com/