Blekinge Institute of Technology
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Master Thesis in Business Administration, 10 credits

“Assessment of SOX implementation - from an Internal Audit perspective”

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Abstract

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Purpose: The purpose of this thesis has been to assess the workload, benefits, challenges, requirements and obligations that implementation of the Sarbanes Oxley Act of 2002 (“SOX”) has posed on Internal Auditors and their companies, from Internal Audits’ point of view. The analysis also compares one accelerated filer and one non-accelerated filer to understand difference and similarities between different sized companies in the initial SOX compliance and implementation phase (documentation, risk analysis, gap identification & remediation and testing).

Methods: Quantitative primary and secondary data was used for the research study using a qualitative collection approach. A questionnaire was used as the primary data and was sent to Internal Auditors’ for one accelerated filer and one non-accelerated filer. The secondary data used consisted of audit consultant reports were used to add substance to the empirical chapter.

Results: Internal Auditors are faced by challenges posed by the SOX law, but there are also many benefits once the internal controls are in place. Main benefits as perceived by the Internal Auditors in the study include an understanding of responsibilities within the organization as well as fraud, corruption, breaches of codes of conduct minimization and a more effective Board of Directors. Difficulties facing the Internal Auditors in charge of SOX were mainly concerning managements understanding of responsibilities that SOX adds to the organization and to the Internal Audit department, support to Internal Auditors and the audit committee’s lack of SOX knowledge. The most challenging areas of the implementation phase were documentation, testing process, gap remediation and senior management support. The big difference between the accelerated and non-accelerated filer were management’s knowledge about SOX; the accelerated filer has senior management who understand their responsibilities under the SOX Act, while this is not the case for the non-accelerated filer.

Keywords: Accelerated and Non-Accelerated Filer, Audit Committee, Governance, Internal Audit, Internal Controls, PCAOB, Risks, Senior Management, SOX.
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Further I would like to thank the questionnaire subjects for their input on the topic at hand and giving me their opinions about their experiences of the SOX implementation process. I appreciate the time they took to take time out of their busy schedules to answer my questions.

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Las Vegas, June 2007

_____________________________________
Linda M Palmer
Abbreviations and Definitions

10-K: Name of annual report filed with the SEC
AC: Audit Committee
AICPA: American Institute of Certified Public Accountants
Big Four: Group of accounting/auditing/professional firms including
PriceWaterhouseCoopers, Deloitte Touche Tohamatsu, Ernst & Young, KPMG
BOD: Board of Directors
FY: Financial Year
COGS: Cost Of Goods Sold
COSO: The Commission Of Sponsoring Organizations of the Treadway Commission
GAO: Government Accountability Office
Internal Audit: Internal Audit (depending on context) department or person
IIA: Institute of Internal Auditors
NASDAQ: National Association of Security Dealers Automated Quotation system
NYSE: New York Stock Exchange
SEC: Securities and Exchange Commission; all public companies must file their annual, quarterly and other required reports with this commission.
SOX, SOA or SARBOX: Sarbanes Oxley Act of 2002
Stakeholder: Anyone with an interest in the survival and longevity of a company: employees, management, investors, suppliers, customers, government and shareholders.
Table of Content

Chapter 1 Purpose. ................................................................. 1
  1.1 Introduction................................................................. 1
  1.2 Background................................................................. 1
  1.3 Research Problem......................................................... 2
  1.4 Purpose of the Study..................................................... 2
  1.5 Research Areas............................................................ 3
  1.6 Limitations................................................................. 4

Chapter 2 Method................................................................. 5
  2.1 Methodology................................................................. 5
  2.2 Theoretical Framework.................................................. 5
  2.3 Data Sources and Collection.......................................... 5
  2.4 Population................................................................. 6

Chapter 3 Theory................................................................. 7
  3.1 Theory definitions....................................................... 7
    3.1.1 Title I – PCAOB....................................................... 7
    3.1.2 Title II – Auditor Independence................................. 7
    3.1.3 Title III – Corporate Responsibilities.......................... 8
    3.1.4 Title IV – Enhanced Financial Disclosures....................... 9
    3.1.5 Title V – Analysis Conflict of Interest........................... 9
    3.1.6 Title VI – Commission Resources and Authority................. 10
    3.1.7 Title VII – Studies and Reports................................... 10
    3.1.8 Title VIII – Corporate and Criminal Fraud Accountability..... 10
    3.1.9 Title IX – White-Collar Crime Penalty Enhancements........... 10
    3.1.10 Title X – Corporate Tax Returns.................................. 11
    3.1.11 Title XI – Corporate Fraud and Accountability............... 11
  3.2 New Standards............................................................ 11
    3.2.1 Accelerated Filers.................................................... 12
    3.2.2 Non-Accelerated Filers.............................................. 12
  3.3 Governance............................................................... 13
  3.4 Internal Control Implementation Process............................. 13
  3.5 Benefits of Implementation............................................ 14
    3.5.1 Public Companies.................................................... 14
    3.5.2 Government.......................................................... 15
    3.5.3 Investors............................................................ 15
    3.5.4 Other Stakeholders.................................................. 15
  3.6 Issues of non-compliance............................................... 15
  3.7 Internal Audit Responsibilities........................................ 16
  3.8 Other SOX recommendations.......................................... 17
    3.8.1 About Consultants.................................................. 17
    3.8.2 Deloitte.............................................................. 17
    3.8.3 Protiviti.............................................................. 18
Chapter 4 Empirical

4.1 Empirical Approach

4.2 About the Questionnaire

4.3 About the Companies

4.3.1 Accelerated Filer

4.3.2 Non-Accelerated Filer

4.4 About Questionnaire Subjects

4.4.1 Internal Auditor 1: Accelerated

4.4.2 Internal Auditor 2: Non-Accelerated

4.5 Questionnaire Results

4.5.1 SOX Project initialization

4.5.2 Difficulties facing Internal Audit

4.5.3 Benefits of Compliance

4.5.4 Management’s understanding about SOX

4.5.5 Internal Audit’s support

4.6 Secondary Data

4.6.1 About the data

4.6.2 American Electric Power Company Inc

4.6.3 About KPMG

4.6.4 KPMG Findings

4.7 Best practice compliance of new requirements

4.8 Theoretical guides

4.9 Trends for Risk, Governance and Compliance

Chapter 5 Analysis

5.1 Introduction

5.2 Assessment of SOX implementation

5.2.1 Disadvantages of SOX

5.2.2 Benefits of SOX

5.2.3 SOX challenges

5.3 Accelerated vs. Non-accelerated filer

Chapter 6 Conclusion

6.1 Introduction

6.2 Research Purpose revisited

6.3 Conclusion from assessment of SOX implementation approach

6.4 Conclusion of comparison of filers

6.5 Recommendation for Internal Auditors

6.6 Recommendation for Management Support

6.7 Recommendations for further studies

Table of Figures

Table 3.2.1 Types of SEC Filer

Table 3.7 Typical Internal Audit Reporting Structure

Table 4.3.2 Key Statistics
List of Exhibits
A. Internal Audit Questionnaire .............................................. 41
CHAPTER ONE: PURPOSE

1.1 Introduction

In July 2002, US president George W. Bush signed the Sarbanes-Oxley act of 2002 (or “SOX” for short) into United States law. This law affects all companies (or “issuers”) that are registered on a US stock and which are required to file financial reports with the SEC (Securities and Exchange Commission) as defined by section 3 of the Securities Exchange Act of 1934 or the Securities Act of 1933 (Sarbanes Oxley Act of 2002, Sec 2, a 7). It is considered by many to be the most important piece of legislation affecting business practices in America since the creation of the SEC in 1934 (Jackson, 2006). The name itself and its abbreviation originated in the last names of the creators of the act: US Senator Paul Sarbanes and US Congressman Michael Oxley.

1.2 Background

The foremost objectives of the Sarbanes Oxley Act of 2002 is to set strict guidelines for the relationship external auditors should have with the companies they are auditing, how company committees should monitor Senior Management’s activities, and how to protect employees when reporting inappropriate behavior (harassment, fraud, insider trading and theft). The Act covers not only US companies but their foreign subsidiaries as well; at least 75% of a company’s foreign operations must obtain SOX certification from a PCAOB approved audit firm. The reason for the unusually rapid adoption of the SOX Act was the collapse of several US companies leaving creditors, shareholders and employees not only speechless, but without retirement investments and jobs. Corrupt Senior Managers in companies such as Enron, WorldCom, Tyco and Adelphia used creative accounting to present inaccurate financial statements (inflated/overstated revenues, disclosed losses as income), grant loans to Chief Officers, nondisclosure of Senior Management stocks and stock sales and post off-balance sheet transactions to hide losses (Welytok, 2006), just to mention a few improper business practices used. The SOX Act was introduced in 2002 by Congress House Representative Michael G. Oxley and then by Senator Paul S. Sarbanes as the main sponsors (hence the name of the Act) as a direct response to combat this type of misrepresentation and misusage of stakeholder confidence.

Depending on the size and type of company you study, the task of preparing for SOX implementation is done in many different ways. When the Act was signed into law it was not well defined when it came to limitations and obligation by the certifying external auditors, specifically in regards to section 404 which refers to effectiveness of internal controls. This has led many companies struggling to cope with consultant and compliance costs, especially for non-accelerated filers (as defined by the SEC). The deadline for SOX compliance has been changed many time to accommodate companies with smaller financial and manpower resources. Some companies started out employing consultant for a compliance project they thought would be completed within a year, but eventually had to shift to an in-house project due to soaring costs. One of the best
practice provisions states that each company should have an Internal Audit function to monitor the internal controls on an ongoing basis and therefore, the SOX compliance implementation project is often allocated to the Internal Audit Department.

1.3 Research Problem

When the Sarbanes Oxley act was signed into law, lawmakers thought that the problems with corrupt Board of Directors, Management and financial statements were resolved and that implementation would be a swift one or two year process. What they didn’t realize was that one of the titles within “the Act” would be the most difficult, costly and timely provision to implement (Hawser, 2007). In the actual Sarbanes Oxley Act of 2002, section 404 is given one paragraph, and sub-section “b” which talks about Internal Control Valuation and Reporting is roughly about 100 words long, yet companies spend millions of US dollars in their efforts to comply (and will continue to do so because compliance is continuous, not a one-time certification). In this study, all the SOX provisions will be given their due space in the theory section but the main research problem and questions will focus on section 404 implementation of this section which is the Internal Auditor’s main responsibility.

With rising compliance costs for the companies, it is important to find out what the main problems are with the SOX implementation process from the people that actually have to perform the compliance work. In smaller companies, Internal Audit is left to fight for the implementation process on their own, without much needed Management support or understanding. Therefore it is important to research and document these problem areas, to seek a better understanding and expedite the implementation process.

1.4 Purpose of the Study

The interest for this subject arose from the Author’s own experience with SOX implementation work for the last 3 years. Objectives for the study are developed based on the curiosity of opinions of other Internal Auditors, to find out if their experiences are the same. During the SOX implementation phase there are many challenges but also benefits to the process and since not many studies exist from the Internal Audit’s point of view, these are some good questions pose to the selected study subjects.

The main purpose of this study is to assess the Sarbanes Oxley Act of 2002 from an Internal Auditor’s perspective in order:

- to assess the implementation phase of the Sarbanes Oxley Act of 2002 from an Internal Auditor’s perspective, and
- to compare and contrast challenges facing one accelerated filer and one non-accelerated filer’s Internal Audit function in their resources available, differences and similarities of how the implementation of the SOX project was set up and how it is handled now in order to:
help Internal Auditors starting SOX compliance understand the benefits, challenges, requirement and obligations posed upon them and everyone who interacts with company business, and

- help Senior Management and company Committee’s understand how they can support Internal Audit by identifying the main issues of SOX implementation.

To ensure that all aspects of the SOX implementation process is investigated and understood, the following research questions were identified:

1. What are the new requirements from SOX facing all companies?
2. What are the Internal Auditor's role; Internal Audit’s responsibilities, obligations, as well as rights enforced by this law?
3. What extra work is required, and are there benefits identified:
   a. to the company
   b. to the investors
   c. to the government
4. What is the overall assessment of the implementation phase and issues facing Internal Audit and the Company?
5. What does the theory (the Act and interpretations) say about to benefits and costs perceived and what does the Internal Auditors interviewed say? Is there a difference between the two?

1.5 Research Areas

During the research phase, the main research areas of study are:

1. How the development of the SOX project started and where it is now (use of external consultants or in-house resources).
2. Main difficulties in the documentation and implementation process facing Internal Audit.
3. The difference and similarities of the implementation between the Accelerated filer and the Non-Accelerated filer, from their Internal Auditor’s point of view.
4. Investigate how supportive is Management and Board of Directors / Audit Committee of the project and Internal Auditors.
5. Investigate if size of the companies and resources provided during the implementation phases of the SOX process which includes:
   a. Risk Assessment
   b. Documentation
   c. GAP analysis
   d. GAP remediation
   e. Testing of internal controls
6. What are the benefits of completion of the SOX project to the Internal Audit Department and to the Company as a whole.
1.6 Limitations

This study was developed based on the Author’s experiences as Internal Auditor in charge of SOX implementation in two different companies during the last 3 years (one Accelerated Filer and one Non-Accelerated Filer). Therefore, there may be some bias of expected results because it follows the perception of the Author. In addition, only one company was studied for each type of filer and the information received in the study may be limited to these particular companies. This is a very small sample to take when all public companies in the US are required to comply with the Act.

The study focuses on the initial SOX implementation phase and does not discuss continuous compliance once SOX certification has been obtained. The reason for this is that accelerated filers are only now in their first year of SOX compliance and for the non-accelerated filer, compliance will not be required until FY 2007 has ended.
CHAPTER TWO: METHOD

2.1 Methodology

Methods chosen for this study aims to tie the research questions to the theoretical framework, analysis and final recommendations. Practical experience is contrasted to the literature/theories by sending out questionnaires to experienced Internal Auditors and by discussing the research area stated in the previous chapter. The companies and persons involved in the study are kept anonymous due to the nature of the sensitive information that is often involved in the SOX process. Internal Auditors investigate the risks for their companies and gaps (where there is risk identified but not mitigating control exist) and search through companies information system, board of director minutes, transaction processing procedures and disclosure process to assess the internal control structure. Most companies would not like to openly admit to their problem areas and if they did, they wouldn’t be as precise.

In the sections below, the theoretical framework, data sources and collection and population choices are described in detail.

2.2 Theoretical Framework

For this thesis, one of the main texts studied is the actual Sarbanes-Oxley Act of 2002. It’s important that Internal Auditors understand all sections of the act, not just the one/s they are working on and each of the titles are therefore summarized in the theory chapter. After the Act was created, theoretical framework were developed and used to help interpret the legal technical language. The literature used in this thesis consists of textbooks and articles with interpretations and theories of how to comply in the most effective way called “best practice” procedures. These books and articles are written by experienced writers, consultants and analysts; people who has been in the consultant/audit business and have substantial knowledge of how to interpret the Act and how to best implement required provisions. The theories presents are best practice theories and suggestions for compliance with the SOX provision as well as required sections of the Act. The theories are discussed and presented in detail in chapter 3.

2.3 Data Sources and Collection

Data utilized for the research part of this study is both primary and secondary qualitative data, as described by Ghauri and Grønhaug (2005). The data collected was combined with the experience of the Author of this thesis. The main source for the study is the Sarbanes-Oxley Act of 2002 itself. There have been many studies of the implications of this act when it comes to Corporate Governance, cost/benefit analysis, etc, but few, if any, regarding the assessment of the act directly from an Internal Auditors point of view.

The primary data is the result of a questionnaire sent to Internal Auditors for one Accelerated Filer and one Non-Accelerated filer. Any follow up or additional questions
were followed up with said Internal Auditors. The selection of the companies was based on the Author’s previous employment. The main reason for this choice is that the topic of the study is very sensitive and there may not be a response from unknown Internal Auditors due to the lack of confidence and trust in what will happen to the information and disclosure of the source. In addition, the Author knows that the respondents have sufficient knowledge and experience to effectively answer the questions asked, since they are prior colleagues in the Internal Audit Department. The actual questions posed in the questionnaire were developed based on the Author’s experience and the research questions posed in chapter one. The respondents were given an opportunity to add anything that may have been missed by the Author in an open ended question section of the questionnaire. The questionnaire sought to obtain information that could be interpreted both quantitative (percentages, graphs) and qualitative (descriptive questions). However, only one Internal Auditor from each company answered the questionnaire and therefore, the answers were interpreted only in a qualitative manner. For a sample of the questionnaire guide, see exhibit A. The information from the questionnaires were then added to the Author’s experience with both companies and presented in the analysis chapter of this thesis.

The secondary qualitative data utilized in this study was collected from online sites (SEC, PCAOB, AICPA, etc), articles on Elin@bth.se, textbooks, consultant studies (KPMG and Deloitte) and magazines. The scope of the secondary data was expanded once it was clear that only one Internal Auditor from each company responded to the questionnaire. This decision was made to add substance to the results of the study and to cover all areas of the research questions. Combining the two types of data helps in understanding and explaining the purpose of the study, and gives reliability to conclusions and recommendations made at the end of the thesis.

2.4 Population

As mentioned in chapter 2.3, the population that was chosen included Internal Auditors from two different companies. The objective of the research study is to gain knowledge of Internal Auditors point of view and assessment of SOX, mainly, but not limited to, issues regarding implementation of section 404 because in the Author’s experience, Internal Auditors are in charge of process-level internal control implementation. Any issues pertaining to other sections/titles of the Act surfacing from the questionnaire will also be discussed in the study. The information obtained from the questionnaire, added with the Author’s experience, will be compared it to existing literature/theories. Since Internal Audit are in charge of making sure the company’s internal controls are in compliance with SOX, this is the appropriate group to interview. The sample size was limited to 4; 2 for each company investigated, plus the author’s own experience with both companies. Only one Internal Auditor from each company answered the questionnaire and additional articles and studies were chosen as secondary data to add substance to the research study.
3.1 Theory Definitions

In this chapter, any reference to the “Sarbanes Oxley Act of 2002” will be in a shorter version; either “the Act”, “the SOX Act”, or on some occasions “SOA”. Another important definition to understand the Act is that of references to an “Issuer”. Bostelman (2005, p.3) explains the term as:

“The definition of “issuer” in the SOA encompasses all types of registrants that file disclosure documents with the SEC, including all public companies in the United States and all non-US companies having listed on a U.S. exchange or traded in Nasdaq”.

There are some exceptions to the rule; companies may be exempt to file their financial statements by the SEC, but they are few and are evaluated by the SEC on an individual basis.

Any reference to the word “auditor” is meant as a reference to the independent auditors from public accounting firm. Every public company must obtain the opinion of this type of firm, in order to file their quarterly or annual report. When referring to a company’s own auditors, the term “Internal Auditor” or short, Internal Audit will be utilized.

Note that if no other reference is given, the information within the title chapter below is taken directly from the SOX Act of 2002 itself as well as relevant literature explaining the chapters within the Act. There are several sub-sections within each title which are summarized below under each main title. Note that only the most important (to public companies and its Internal Auditors) are discussed and mentioned in detail.

3.1.1 Title I – PCAOB

The first title of the SOX Act establishes the creation of the PCAOB – the Public Company Accounting Oversight Board. The main purpose of this commission is to regulate the work that auditors perform and set the standards and rules for the relationship between an audit firm and its client. All accounting firms must register with the PCAOB and be subjected periodic reviews of how audit assignments were conducted. The frequency of these reviews depends on the size of the audit firm. This title also outline specific requirements for the auditors, such as work paper retention, two audit partners must sign off when the audit is completed and perform an evaluation of internal control, in addition to the financial audit (Weytok, 2006).

3.1.2 Title II – Auditor Independence

The second title is very important because it outlines new requirements that are a direct result of the Enron collapse and the inappropriate actions taken by Enron’s external audit
provider: Arthur Andersen. The essence of the provisions in this title is that audit companies in charge of the financial audits are not allowed to provide any other service (such as the very profitable tax provision consulting service). The reason is that a conflict of interest may occur; the audit firm doesn’t want to report any irregularities because they are afraid to loose their other consulting services, and hence, the auditor’s independence is jeopardized. There is an exception to this rule in the SOX Act, stating that any additional service may be pre-approved by the audit committee. In addition, the audit committee is responsible for overseeing the work done by the auditors and make sure that auditors are rotated for each company on a regular basis (Jackson, 2006). Services that are absolutely prohibited for any contracted auditors are listed by Bostelman (2005) on page 11:

“In particular, an accountant cannot:

(1) audit its own work;
(2) function in the role of management; or
(3) serve in an advocacy role for its client.”

3.1.3 Title III – Corporate Responsibility

The third title of the Act outlines a public company’s audit committee responsibilities, obligations and rights as well as other corporate responsibilities. The audit committee is responsible of reviewing compensation of the Senior Managers (salary, stock options and other compensation as outlined in the proxy statement), how to deal with complaints, etc. It also states that Directors who are members of the audit committee must be otherwise independent from management, not be a consultant or other affiliate of persons or the issuer.

Section 302 of this title specifically states that CFO’s and CEO’s must certify the following every quarterly and annual disclosure opportunity:

- The officer signing the report has reviewed it
- That the report does not contain any untrue material statements
- Based on the officers knowledge, the financial statements are represented in fair condition and that internal controls have been established, any material information is made public, the effectiveness of the internal controls and the officers conclusions about the controls
- That all significant deficiencies have been reported to the board of director and the auditing firm, including fraudulent activities discovered
- If there were significant changes in the internal controls to the date of their evaluation
- That 302 applies to foreign issuers and the effectiveness deadline of the provision
The other sections of title III concerns bonus and profit forfeits if restatements are required, penalties imposed on officers and directors if they temper or omit significant and material issues, insider trading and blackout date requirements, attorney responsibilities and fair funding for investors.

3.1.4 Title VI – Enhanced Financial Disclosures

This is the most important title for Internal Auditors in regards to SOX because it outlines their main part of their work to obtain SOX certification. As mentioned in chapter 1.2, the interpretation of section 404 of this title is what keeps Internal Audit’s and management working ferociously because it’s the section considered most difficult to interpret requirements for. All the actual section 404 says is that any annual filing shall include and internal control report which outlines management’s responsibilities over internal controls, an assessment should be made by management by the end of fiscal year. It also says that any public accounting firm responsible with reviewing the issuer’s financial statement shall make an attestation of the assessment on internal controls done by the company’s management.

The other sections of title IV adds to this provision by stating that quarterly report (10-Q) shall adhere to GAAP, contain all material correcting adjustments as identified by the auditors and disclose any off-balance sheet transactions. It also outlines enhanced conflict of interest provisions: it is unlawful to issue any personal loan or extend credit to any director or executive officer of the company. In addition, all companies must file an 8-K report with the SEC detailing all principal stockholder, director or officer who owns more than 10 percent of any equity security.

The audit committee and senior management is also discussed in section IV; all senior financial officers must sign a code of ethics to ensure ethical and honest conduct in all areas that concern the company and to ensure “full, fair, accurate, timely and understandable disclosure of the periodic reports” (section 406 (2)). The audit committee must have a financial expert among them who is capable of reading and interpreting financial statements. Lastly, any information regarding material changes in the financial statement or the company’s operations must be disclosed immediately “in real time”.

3.1.5 Title V – Analysis Conflict of Interest

Title five is not aimed towards public companies per se, but instead to securities analysts. Anyone working within this field must adopt their own policies regarding conflict of interest when research analysts reports on securities and public appearances to improve reliability and objectivities of these reports and recommendations. This provision does not impact the public company’s compliance attempts and therefore not described in more detail in this section.
3.1.6 Title VI – Commission Resources and Authority

This title outlines the resources that are available to the SEC and Federal Courts. It also details funds that should be available; i.e. the budget of the SEC. It also dictates “qualifications of associated persons of brokers and dealers” in section 604. This provision does not impact the public company’s compliance attempts and therefore not described in more detail in this section.

3.1.7 Title VII – Studies and Reports

The seventh title of the Act outlines the studies and reports that should be conducted by the GAO or SEC regarding consolidation of public companies, credit rating agencies, violators and violations, enforcement actions and investment banks. This provision does not impact the public company’s compliance attempts and therefore not described in more detail in this section.

3.1.8 Title VIII – Corporate and Criminal Fraud Accountability

This title is also very important for public companies no matter the size because it criminalizes improper behavior and protects anyone who acts as a “whistleblower” (section 806). The name comes from “blowing the whistle” and exposing fraudulent activities, report discrimination, harassment or other to the auditor, board of director or management. Anyone in the company who is fired, demoted or suspended because they “blew the whistle”, can sue the company under this provision. Other sections under this title concern securities fraud and defrauding shareholders (Jackson, 2006) and outlines that anyone involved can be prosecuted in a federal case.

Another section (802) dictates preservation of documents for both auditors and public companies. Companies must retain certain documents for a period of 2-7 years (including email and other communication with certain stakeholders) or be charge with intentionally trying to obstruct a federal investigation (violations may result in imprisonment for up to 20 years). The auditors can also be charged under this provision if they don’t preserve the work papers used during an audit for a period of (currently) five years after the annual audit was completed. If the auditors does not adhere to the provision, they may face up to 10 years in prison and/or be fined (Jackson, 2006).

3.1.9 Title IX – White-Collar Crime Penalty Enhancements

This title outlines penalties for a variety of white-collar crimes such as:

- Attempts and conspiracy to commit criminal fraud offences
- Mail and wire fraud
- Violation of employee retirement income security
- Failure of corporate officers to certify financial reports
It also amends sentencing guidelines of certain offences to ensure that it reflects the nature and severity of the offence, that it’s adequately addressed, account for additional offences and ensure that any sentence is in line with other directions and guidelines. The provision of section 902 that must be certified by the CFO and the CEO has been included in the section 302 certification template (see 3.1.2 above for details).

### 3.1.10 Title X – Corporate Tax Returns

This is the shortest title of the Act, and its only section (1001) speaks for itself:

“It is the sense of the Senate that the Federal income tax return of a corporation should be signed by the chief executive of such corporation”.

### 3.1.11 Title XI – Corporate Fraud and Accountability

The last title outlines criminal penalties for tampering or altering records, give the SEC the right to freeze assets, amends federal sentencing guidelines for securities and accounting fraud, authorizes the SEC to prohibit certain persons from serving as officers or directors and finally, prohibits retaliation against informants.

### 3.2 New Standards

Not all provisions within the SOX Act is a new standard for public companies. Many titles and sections simply modifies a prior requirement issued by the SEC (first stated in the 1933 or 1934 Acts) and enforces rules or best practices already required by the US stock exchanges. However, the provision of Senior Management certification of internal controls is the main new standard because it holds the CEO and the CFO criminally responsible if they knowingly withholds information or significant deficiencies discovered in the internal control process from the government and the share- and stockholders. The other main standard is the establishment and the oversight responsibilities of the PCAOB. Audit firms are restricted in the way they do business and this new standards helps in keeping them honest. The periodic review of the PCAOB and registration requirement helps outline how audits should be performed and improve the procedures of the audit firms.

The difference of standards between accelerated and non-accelerated filers does not differ as much as one may think. The biggest difference of new standards for accelerated filers is an accelerated reporting schedule of the annual and quarterly reports. The general differences between accelerated and non-accelerated filers can be seen in Table 3.1 below. Note that any company may file for an exemption from the rules; the exemption is then granted (or not) by the SEC.
### Table 3.2.1: Types of SEC Filers

<table>
<thead>
<tr>
<th>Filer Category:</th>
<th>Accelerated</th>
<th>Non-Accelerated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Market Float:</td>
<td>Over US$75 Million</td>
<td>Under US$75 Million</td>
</tr>
<tr>
<td>Reporting Requirement: subjected to section 13(a) or 15(d) of the Exchange Act of 1934 for:</td>
<td>At least 12 months.</td>
<td>Less than 12 months.</td>
</tr>
<tr>
<td>Filing Requirement:</td>
<td>At least one annual filing</td>
<td>Less than one annual filing</td>
</tr>
<tr>
<td>Special SEC Forms for small businesses:</td>
<td>Not eligible</td>
<td>Eligible</td>
</tr>
<tr>
<td>SOX Compliance date, unless exempt by SEC:</td>
<td>FY ending on or after July 15, 2006</td>
<td>FY ending on or after July 15, 2007</td>
</tr>
<tr>
<td>Number of days to file annual 10-K:</td>
<td>60 days</td>
<td>90 days</td>
</tr>
</tbody>
</table>

Information Source: Welytook, 2006 and [www.SEC.gov](http://www.SEC.gov)

Note that compliance dates for non-accelerated filers and the SOX implementation process guidelines are still being discussed by the SEC, PCAOB, the US Senate and the US Congress. The call for stricter guidelines on what certifying auditors can demand from companies’ echoes through Washington DC. It has become very costly for companies to reach compliance because the scope of the internal controls demanded by the auditors is too big. Congressman (now retired) Michael Oxley himself has blamed the PCAOB for the problems that companies experience when trying to comply with the act (Claudia, 2007). Changes to the numbers displayed in the table above, can therefore change as clearer guidelines and deadlines are approved by the SEC.

#### 3.2.1 Accelerated Filers

In September 2005, the SEC modified the definition of an accelerated filer and adding a third category of filer called:

““large accelerated filers,” for companies that have a public float of $700 million or more and meet the same other conditions that apply to accelerated filers. The proposed amendments also would redefine “accelerated filers” as companies that have at least $75 million but less than $700 million in public float.”  (SEC press release: 2005-134).

However, from a SOX perspective, the large accelerated filer falls under the same deadlines as an accelerated filer and is therefore not discussed in detail in this study.

#### 3.2.2 Non-Accelerated Filers

Non-Accelerated filers have the advantage of not being required to comply until FY2007. Depending on when their financial year ends, the non-accelerated filers have up 1-1 ½ years longer to become compliant compare to accelerated filers. Meiselman (2007) notes that non-accelerated filers may benefit from lessons learned from larger companies and
have more guidance from government agencies such as the SEC, COSO and the PCAOB. COSO has published guidelines specifically aimed towards smaller companies. The guide discusses how non-accelerated filers can develop compensating controls for areas such as segregation of duties and approval controls. It also gives practical examples of what companies of various sizes has done to mitigate the risks identified for their companies.

3.3 Governance

The Governance standards outlined in the SOX Act is targeted to create Board of Directors who can’t be bought or compromised when making decisions that affects the company’s business. Although independent directors and an audit committee are already a requirement to be registered on a US stock exchange, SOX emphasizes and dictates additional obligations, responsibilities and rights for these boards. This is especially important for non-accelerated filers if a particular group or family has the majority of votes and ethical decisions may be compromised when this group exercises their power (Jackson 2006).

3.4 Internal Control Implementation Process

The suggested internal control implementation process is the same for accelerated and non-accelerated filers. COSO outlines the following framework in its executive summary of “Internal Control over Financial Reporting – Guidance for Smaller Public Companies” (page 8):

- Risk Assessment
- Control Environment
- Control Activities
- Information and Communication
- Monitoring

What this framework means is that the first step should be to assess the risk that may threaten the company. It includes, but is not limited to; fraud, corruption, harassment and natural/other disasters. It’s important for the company to understand that this assessment must be ongoing. The quarterly and annual SOX certification requirement seeks to enforce this process by making the CEO and CFO sign off on the internal control assessment.

Once the risks have been identified, the next step is to set up the control environment, also called the governance or entity-control process. Governance sets the very foundations for the internal control identification and enforcement process and includes factors such as ensuring that employees and management work and make decisions that have integrity, are ethical and that the employees are competent in their positions. Governance also covers Management Philosophy and Operating style, authority and responsibility assignments within the company, structure of the organization, training for employees and board of director / audit committee involvement.
If a company does not pass the Governance provisions during the testing process, it will be difficult to obtain the certification. How can a company as a whole have proper internal controls if the people making decisions are non-compliant?

The third step of the SOX implementation process involves the Control Activities, and this is what Section 404 is all about. As mentioned in section 3.4.1 above, this is where companies determine how the internal controls should be identified and monitored. One way of documenting the internal controls are using a mantra called “4 whiskeys and 1 hotel”:

- Who?
- What?
- When?
- Where?
- How?

For each controls these questions have to be answered; documented in a narrative, flowchart or a spreadsheet. The preferred method is using at least two of these three documentation methods, to ensure full disclosure and understanding on the internal controls.

Moving on to the fourth step of implementation; information and communication refers to the process of how the company handles both internal and external information. It must be communicated to employees and relevant external entities (shareholders, creditors, etc) in a timely manner. All employees must understand their roles within the organization to fully comprehend what their responsibilities are. Information must flow from the top down as well as from the bottom up so that problems that arise are dealt with in an appropriate manner (COSO Small Business Framework, 2006).

The last part involves how the internal controls should, and are monitored. Procedures of how ongoing monitoring must be set up and followed and procedures how serious breaches will be handled and dealt with. Management should assess the monitoring process and scope based on the level of risk, frequency and probability of occurrence in order to obtain a cost effective monitoring process (Anand, 2006).

3.5 Benefits of Implementation

3.5.1 Public Companies

There are benefits to SOX implementation that covers both accelerated and non-accelerated filers. The benefit to the provision of holding Senior Management criminally liable is that they have to learn how the business is run from the bottom up, not just from the top down. For small companies, the increased responsibility of the Audit Committee as an overseeing entity will encourage Management to take ethical and informed decisions and mitigate the power on one controlling CEO. Complying with SOX also means that the reliability of the financial statements are at an appropriate level. Banks and investors who infuse the company with equity are more likely to give a better interest
rate, payment and credit terms, if they know that they can depend on the internal controls (Jackson, 2006). SOX can also be used as a marketing tool if customers have several options to choose from and especially if the competitor cannot guarantee the same level of dependability. Since SOX requires Senior Management to assess risks posed to the company, they may be better prepared if a serious incident occurs.

3.5.2 Government

If the government can rely on the internal controls for the public companies, it benefits due to lower numbers of company collapses and loss in retirement for the employees. The law itself shows that the government is capable of creating a safer environment for investors and other stakeholders.

3.5.3 Investors

Investors will benefit from the transparency of the company, including for senior management in regards to travel and other reimbursement claims (Jackson, 2006). To comply with SOX, the company must disclose any material and significant deficiency in its internal controls to the auditing company. By doing this, the auditors can be satisfied that the company is looking to remediate these deficiencies because they know they will be audited on the deficient controls.

3.5.4 Other Stakeholders

There may be benefits to other stakeholders as well. If you count employees a company, the benefit is the longevity of the business and their jobs. It also secures that their retirement funds are not misused due to some greedy Manager with stock options. Anand (2006) lists job opportunities as one benefit, within all areas of compliance (mainly accounting and IT). SOX require an Internal Audit function (in-house or external) to perform the compliance testing and this often leads to a new in-house position that may be filled by someone from the company. Increased outsourcing activities may also be a benefit caused by SOX. In problem areas this may be a good way for the company to go, once a service is outsourced the company can request an internal controls reliability report (SAS70), from the service provider.

3.6 Issues of non-compliance

The main problems facing a company if they do not comply with SOX are the opposite of benefits listed in section 3.5 above. A company is less reliable when it does not establish and maintain internal controls as outlined in the SOX act. If a company is less reliable, any creditor may require worse terms and impose restrictions on leveraging the company. In addition, investors may be less inclined to purchase stock in a company where there is
no or less oversight in the activities of management and disclosure of financial statements and assets. Issues of non-compliance reflect negatively on the company, the managers, which in turn, affect the market value of the company and its owners (shareholders). A company with fewer controls may be a target for scrupulous Managers and may attract employees with less experience and less concern for the company and its assets (tangible and in-tangible).

3.7 Internal Audit Responsibilities

Readers of this thesis may wonder what the Internal Audit function is, what their responsibilities are, and why they are chosen for the SOX implementation in many companies. The IIA Audit – Institute of Internal Auditors define Internal Audit as (IIA “Standards”, 2007):

“Internal Auditing is an independent, objective assurance and consulting activity designed to add value and improve an organization’s operations. It helps an organization accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes.”

Many Internal Audit departments’ reports directly to the Audit Committee of the Board of Directors as well as Senior Management; see table 4.6.1. Note that for non-accelerated filers there may be only one or two Internal Auditors so the titles within the Internal Audit department may be different than shown in the table.

Table 4.6.1: Typical Internal Audit reporting structure

<table>
<thead>
<tr>
<th>Senior Manager</th>
<th>Internal Audit Director</th>
<th>Audit Committee</th>
</tr>
</thead>
<tbody>
<tr>
<td>Internal Audit Manager</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Internal Auditor</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>


Internal Auditors are used by companies because of their independence from preparing and processing accounting transactions and independence from operational activities (sales, production, etc). Because they are not part of these processes, they are more likely to identify fraudulent activities within the company. Achilles, Rieman and Greenfield Jr, (2007, pg.4) adds:

“Post-SOX Internal Auditors play a key role in corporate governance, risk management and quality assurance. Senior management and audit committees..."
rely heavily on Internal Auditors to help meet SOX requirements and provide assurance of strong internal control structure.”

Most companies have an Internal Audit charter where the responsibilities and obligations are outlined. Internal Audit’s are required to sign it before working with sensitive information (BOD minutes, stock option records, operational results, financial disclosures, etc) to ensure that this information is not leaked to improper personnel, or outsiders. When an Internal Auditor takes the oath/signs the charter, they are prohibited to talk about the information they have audited with others outside the Internal Audit department.

3.8 Other SOX recommendations

3.8.1 About Consultants

Deloitte are one of the “Big Four” firms that provide audit (external), tax, consulting and financial advisory (http://www.deloitte.com, 2007) on a global scale. Deloitte has around 135,000 employees all over the world. The “Big Four” partners often participate in forming best practices, evaluate COSO framework and create benchmark procedures for SOX and other projects.

Protiviti is a company with 2,900 employees in over 50 countries around the world. On their website (http://www.protiviti.com, 2007), they explain that:

“Since our inception in May 2002, Protiviti has become recognized worldwide as a leading expert in Internal Audit and risk management, as well as a thought leader in areas that include the complexities and challenges of complying with regulations such as the Sarbanes-Oxley Act. Further, in 2005, Forrester Research ranked Protiviti as one of four leaders in enterprise risk management (ERM) consulting.”

They serve a broad range of industries and provide solutions such as SOX implementation and companies can outsource their Internal Audit function to Protiviti instead of establishing an Internal Audit Department.

3.8.2 Deloitte

In 2004, Deloitte published and educational guide called “Taking Control – A Guide to Compliance with Section 404 of the Sarbanes-Oxley Act of 2002” where they list tips of how to implement SOX based on their experience of the process. Deloitte recommends that companies not only strive to comply, but that they should strive to excel and embrace the Act to make the company stronger and more reliable. Among other things they suggest (p. 2) “if you embrace the spirit of the law – strong ethics, good governance, reliable reporting – you just may get a re-energized company, reassured investors, and maybe even reduced costs”. Cost reduction is a possibility for companies that reviews and
removes unnecessary processes and complexities of the system and they way they do business. They also recommend that companies to plan the end of the SOX project (management and external auditors certification of the 10-K).

Deloitte also suggests that companies make the planning phase properly in order to focus on the right areas; where material weaknesses may occur. The Audit Committee should be encouraged to provide more oversight over financial reporting and really understand the provisions within the Act but also facilitate discussions between management, external and Internal Auditors in regards to quality and integrity. Another main area is to “Strengthen the Control Environment” (p. 3). The basis for this is that the control environment, or governance, is the foundation for the company’s internal controls. It covers management’s tone at the top, how the company is governed by management and the BOD/AC, how the company culture is and how the company is organized. Integrating IT into the SOX process is important because the more IT controls there are; the more mitigating controls exist for human errors in the financial reporting process. IT controls help in control process by segregating duties and authorizations when it comes to processing, reviewing and approving transactions.

Deloitte emphasizes that it’s important to consult with the independent auditors who at the end are reviewing management’s assessment of internal controls. If the company’s scope is out of sync with the auditors view; the company may not obtain the SOX certification. The auditors need to understand the scope, timing of testing of the controls and therefore it’s important to have talks early on in the SOX process and continue the connection throughout the documentation and testing phase. Deloitte also advises companies not to forget the other COSO areas and only focus on section 404.

3.8.3 Protiviti

Protiviti created a “Guide to the Sarbanes-Oxley Act: Internal Control Reporting Requirements” in 2003 to answer questions about challenges faced by many companies in their quest to comply with section 404. The suggestions by Protiviti personnel is based on their consultants’ experience with compliance documentation and the questions were originated by clients, attorneys and others who have to deal with the SOX requirements. The following is a summary of Protiviti’s suggestions to reach compliance.

The first thing is to choose a control framework for the assertions and evaluation of the internal controls. Protiviti recommends that the COSO framework is used because it is accepted by accounting and auditing professionals as well as the SEC. Using COSO means dividing the process into an entity (high) level and a process (activity) level. Entity levels cover the company and subsidiaries as a whole while the process level are the detailed controls of how numbers arrive and are presented in the financial statements (how revenue is processed/recognized or how cash is handled). They also point out that operational controls are only important when they overlap the financial reporting (valuation of inventory or COGS).

To get the project going, Protiviti lists the following points (p. 26).

- Organize the project
- Develop a project plan
- Agree on project approach and reporting requirements

This means extensive planning before risk assessment and documentation can take place. A steering committee with periodic meetings would help keep the project on course. Members should include certifying officers, operating representatives, department managers affected by the controls, IT and Internal Audit. Once the objectives are determined it’s important to communicate the plans and request cooperation from other employees. The purpose must be explained, who is responsible for what functions and what is required from everyone to obtain SOX compliance.

Protiviti also recommends that the company forms a disclosure committee that deals with SEC requirements, that can identify issues discovered, develop of infrastructure and ensure that any material or significant activities are presented to Senior Management in a timely manner. A project sponsor should take charge of the project and it should be a senior officer who really emphasizes the importance of compliance and cooperation with the project team. For this to happen, the sponsor must be someone who is credible in this task. The overall company sponsor should then be a certifying officer such as the CEO or CFO (p. 61).

The Internal Audit function is also an important one. Protiviti recommends that companies either establishes this department in-house or outsource the function. Protiviti does not think that Internal Audit should have the primary ownership of section 404 implementation (it should be a certifying officer), they recommend that the head of the Internal Audit department reports directly to the audit committee.
CHAPTER FOUR: EMPIRICAL

4.1 Empirical Approach

The empirical approach of the study has been to create a questionnaire to obtain the primary data directly from experienced Internal Auditors and to see if they confirm or alters the author’s own experience with the companies chosen. One Internal Auditor from each type of company responded to the questions in the questionnaire. Due to the few answers received, additional secondary data were added. The secondary data utilized and the information obtained are taken from published informational reports from consultant companies or from articles published in various magazines.

4.2 About the Questionnaire

The questionnaire was developed and sent out to the research subjects in the month of April and May, 2007. Any statements regarding the size and other key statistics of the two types of SEC filers were valid at the time the questionnaires, however, it may not be true at the time of publication of this thesis. Key statistics for the two companies were taken online from Yahoo! Finance (http://finance.yahoo.com/).

4.3 About the Companies

In this section there will be information pertaining to the characteristics of the companies as well as current SOX Act titles other than 404. However, requirements and compliance with SOX that is also necessary for incorporation of the companies as required by the stock exchanges (Audit Committee with Independent Members etc) will not be detailed. The reason for this is that the companies must comply with these requirements to be able to trade stock on the stock exchange.

4.3.1 Accelerated Filer

The Accelerated Filer chosen for the study is a corporation operating in 11 different countries with 2900 full-time employees. It’s headquarter is located in California, USA, and it was established in 1994. The company is considered part of the service sector (Yahoo! Finance, 2007) and sells wholesale merchandise but does not produce or manufacture the products sold. This company has had an established Internal Audit department dating back before the SOX project began (project started 2005).

Management decided to start the SOX project by bringing in one of the “Big Four” consulting companies to structure the compliance and documentation process. These consultants worked out the risk assessment and scope with management and decided to first focus on one of the subsidiary countries, in addition to the corporate headquarter in mainland USA. Six of the subsidiary countries were added to the scope.
and internal resources were added for training in the first compliance country. The internal resources consisted of the Internal Audit department and other personnel with project or IT experience and were assigned to the SOX project. They temporarily left their normal jobs within the company for the first phase of the project. The idea was to train the internal personnel in the first country and then send them back to continue the documentation process for the rest of the countries within the scope. This would save the costs of using external consultants and train Internal Audit in the internal control assessment process.

At the time there were little guidance from PCAOB, SEC or other governmental bodies and therefore, the initial scope was very large. Operational activities were included and very detailed internal controls were identified. Once guidance were presented that restricted the external auditors requests for total coverage of all activities, the scope was re-defined and controls were scaled down to include only the ones that directly affected the financial statements. The company also decided to include internal controls that were not key controls because they feared that if the controls were not part of SOX, they wouldn’t be performed effectively. The COSO framework was used to structure the internal controls.

At the corporate headquarters, a SOX steering committee was created with members of senior management, management, Internal Audit and the project team who would monitor the progress and timelines.

Since the start of the project, the Internal Audit team has been split and there are now two teams within Internal Audit: one team that tests the controls and another who works on documentation, implementation and gap remediation. The total number of Internal Auditors within the organization is 7-10 persons. In the company there is an established reporting hierarchy with the Internal Audit Director reporting directly to the Audit Committee and a Senior Vice President (who also is the SOX “champion”).

### 4.3.2 Non-Accelerated Filer

The Non-Accelerated Filer chosen is a corporation operating in the consumer goods sector (Yahoo! Finance, 2007), with 870 full-time employees. The headquarters of the corporation is located in Nevada USA, and there are manufacturing operations in two other countries. The company sells their product directly to its customers, without middleman intervention.

In this company there was initially a resistance to SOX and the attitude that compliance would not be required since they were considered a small company, a “non-accelerated” filer. There was an effort to assess the internal controls and risks that were assigned to the CFO who in turn recruited an external consultant company for the job. The external consultants spent about a year developing the scope using the COSO framework and started documenting the processes within section 404, but there were little or no oversight by anyone other than the CFO. The CFO in turn did not get involved in the process and let the consultant’s document operational controls in detail, such as production of each of the product sold by the company, and did not focus on the financial statements. However, in the foreign subsidiary, that country’s CFO had immediately
retrieved an Internal Auditor and fired the external consultants, after only 3 weeks of the project initialization.

In 2006 the corporate office discovered that the project had not moved along very far even though a massive amount of money had been paid to the external consultants. The corporate CFO and the consultants were fired and a SOX Compliance Manager was hired, with the plan to create an Internal Audit department along the way to compliance. The corporate office then continued documenting their internal controls as a separate entity to the subsidiary. Meetings were held to ensure that the countries were covering the same controls. A SOX Steering Committee with members of the corporate office and the foreign subsidiary was established who’s members met weekly over a video conference system to ensure that the project was moving along. The meeting started out with Senior Management present, but after a few weeks only the compliance team was present at these meetings.

This company also established an Internal Audit department as part of the SOX project implementation in 2007. The Internal Audit of the subsidiary now reports to the corporate Internal Audit Manager who in turn reports directly to the Audit Committee and the CEO. However, there are no SOX “champion” in the management team and currently no proper oversight over the Internal Audit department.

<table>
<thead>
<tr>
<th>Filer Category</th>
<th>Accelerated</th>
<th>Non-Accelerated</th>
</tr>
</thead>
<tbody>
<tr>
<td>Number of employees</td>
<td>2900</td>
<td>870</td>
</tr>
<tr>
<td>Year Established</td>
<td>1994</td>
<td>1963</td>
</tr>
<tr>
<td>Market Cap (in Million US$)</td>
<td>505</td>
<td>127</td>
</tr>
<tr>
<td>Number of Locations</td>
<td>11</td>
<td>3</td>
</tr>
</tbody>
</table>

Information Source: Yahoo! Finance

### 4.4 About Questionnaire Subjects

#### 4.4.1 Internal Auditor 1: Accelerated

Internal Auditor no 1 has been involved in the Internal Audit function for 2.5 years, and has been working with SOX for those 2.5 years with the Accelerated filer. This person has previous experience with the company in a different position and is an expert in the operating system. Current responsibilities include document and test internal controls, evaluate and suggest GAP remediation in all the subsidiary countries within the SOX scope.

#### 4.4.2 Internal Auditor 2: Non-Accelerated

Internal Auditor no 2 has worked for a total of 3 years in an Internal Audit position and
has worked with SOX for the last 2 years with the Non-Accelerated filer. This person came in to the company as a consultant but was transferred into an employee and has prior experience in external auditing as well as internal auditing. Current responsibilities include documenting processes, evaluating GAP’s, remediating GAP’s, developing test scripts, test internal controls, and finally, evaluate any significant or material weaknesses.

4.5 Questionnaire Results

4.5.1 SOX Project initialization

The initialization for the SOX project involved external consultants for both the accelerated and non-accelerated filer. One senior manager was assigned as the company’s project sponsor for both companies. However, while the non-accelerated filer relied entirely on the consultants for risk assessment, process documentation and GAP identification, the accelerated filer included the Internal Audit department to help out with this process. The resources used were also different between the two companies; the non-accelerated filer had a team of 1-3 persons working on the initial phase while the accelerated filer had between 4-6 people performing the same task. In addition, the accelerated filer had 10-13 additional in-house people working on the first phase, while the non-accelerated only had 1-3 additional persons. That totals a number of 11-16 persons working for the accelerated filer in the first phase, while the non-accelerated only had 2-6 persons doing the same for that company.

4.5.2 Difficulties facing Internal Audit

When it comes to difficulties facing the Internal Audit department, the areas with most problems vary between the two types of companies. The accelerated filer’s Internal Auditor lists the documentation, testing and unclear approaches and timeline for the Internal Audit department as main problems. This has become especially difficult since the split into one testing team and one documentation team (all within Internal Audit department). These are the heavy, slow areas and for the accelerated filer, this process was performed for all the countries within the determined SOX scope. The documentation was also done in two languages during the documentation process because most corporate staff does not speak the language in the operational countries. Another problem for the accelerated filer’s Internal Auditor’s were the understanding of SOX from Management, see chapter 4.5.5 below for detail.

4.5.3 Benefits of Compliance

SOX compliance requires a lot of work and dedication by many persons in the company. The question is often posed as to what benefits come out of compliance with the Act. For the accelerated filer, Internal Auditor 1 believes that the main benefit to the company is
that it brings an understanding of responsibility. During the implementation process, the Internal Auditors are often left to explain the purpose of the SOX project to clerks, supervisors and middle management. They ask the employees to always consider what each person’s responsibilities are and question transactions or other activities that they suspect are improper or erroneous and report that via the whistleblower process.

For the non-accelerated filer, the main benefits are several according to Internal Auditor 2 and include: minimization of fraud, corruption, breaches of codes of conduct, understanding of responsibilities and a more effective board of director’s. In the non-accelerated filers’ company structure, the Internal Auditors have direct access to Senior Management such as the CFO, COO and CEO and can impact and develop the SOX process in direct way.

### 4.5.4 Management’s understanding about SOX

When it comes to the Internal Auditors understanding about the SOX knowledge of management and other personnel within the companies; the results are very different. The accelerated filer works through a well established reporting hierarchy, while the non-accelerated filer is in the process of determining how the Internal Audit should function and currently reports directly to Senior Management. When it comes to the understanding of SOX itself, the accelerated filers’ Senior Management (including BOD, AC) is perceived by the Internal Auditor to fully understand all the provisions required by them under SOX. The non-accelerated filer’s Senior Management on the other hand, has a medium understanding of what is required of them. For the rest of the company personnel (d-g in the questionnaire, see appendix A), the two companies are very similar with a medium level of understanding for middle management, operation and accounting personnel. Internal Audit’s personnel are considered to fully understand its responsibilities for the non-accelerated filer and almost fully understand it in the accelerated filer.

### 4.5.5 Internal Audit’s support

In the non-accelerated filer’s case, Internal Audit thinks that there is no support for them because Management does not understand what SOX really is and what it takes to be compliant. Management understands that the company must comply with the provisions but does not have any idea of how to get to that point. The SOX process is delegated to Internal Audit completely and by doing that, management thinks that the job will be done. There have been promises of support and extra resources, but there is no follow through from management. The SOX process is downgraded to a review to be performed at a later stage, after the disclosures, after month’s closing, etc. Making SOX a priority, which is needed, just isn’t communicated or demonstrated to the Internal Auditors.

For the accelerated filer, the support from Management is there: there is an Internal Audit team and an Internal Control team with specific responsibilities and a committed Senior Manager. However, the understanding on the workload for each team and each subsidiary within the SOX scope is missing for each of the teams. Each Internal
Auditor has a specific performance target and due to the lack of experience on the manager’s side, the demands to perform are out of sync with time it actually takes to do the tasks assigned to each member. For the Internal Control team, upper management (Internal Auditor #2, 2007):

“is not conscious about the time that the documentation of all our processed in the six in-scope countries takes. Management ignores this fact too and because of this lack of knowledge, the workload is not equally divided by the Team.”

4.6 Secondary Data

4.6.1 About the data

The secondary data was chosen from an article in an accounting trade publication (CPA Journals, Compliance Week, and Internal Auditing) about the American Electric Power Company Inc as well as interpretations and surveys from consultants and accounting firm: KPMG.

4.6.2 American Electric Power Company Inc.

AEP falls under the definition of large accelerated filer with around 20,400 employees in the United States, and is considered part of the utilities sector (Yahoo! Finance, 2007). In an article called “Power Up Compliance Work” published in The Internal Auditor, Charles T Sauders details this AEP’s SOX compliance process and development of a SOX software. For this company, the Internal Audit function was assigned with the SOX process because they would be in charge of future compliance with the Act.

The company decided to develop and implement a “centralized automated data management system” (p. 34) across the subsidiaries in order to get a firm grip on controlling not only access to reporting information, but also standardize the SOX process. The first step was then to set clear goals of how compliance could be achieved in time for the FY2006 deadline. Production and launch dates were identified for the software solutions and for each business unit identified. When the due dates were set, the Internal Audit department involved personnel that were going to be affected by the new procedures and systems. Personnel ranging from process owners, vendors, external auditors to senior management were all contacted by the Internal Audit department to ensure that the new software was developed according to user and business needs. In addition, new needs were identified and added to ensure that it incorporated all areas of SOX and make sure that it would be easily adapted to the documentation process. When the needs were identified, selected software vendors were evaluated by Internal Audit management and by the AEP’s Information Systems department and the software were selected accordingly.

Once the software was chosen, the company continued to form an implementation team which included Internal Auditors, the vendor of the system and IT department.
After the team was established, the functionally was matched to the needs of the process and work flow design was developed, software was tested and additional resources were acquired. Live tests of the system were performed, training was given by Internal Auditors and other business owners and finally production of the system went live. The company credits the skills of the project managers, auditors with the success of implementation of the system in time and within budget. Now, all significant managers and outside consultants to share the internal controls management of the SOX project.

4.6.3 About KPMG

KPMG is one of the “Big Four” firms that provide audit (external or internal) solutions, tax, consulting and financial advisory (http://www.kpmg.com, 2007) on a global scale. KPMG has about 113,000 employees all over the world. They provide both consulting services for SOX compliance and serve as SOX certifying external auditors for various companies.

4.6.4 KPMG Findings

KPMG conducted a study in late 2003 to get an understanding of Senior Management’s perception of the introduction of the SOX Act. The results are presented in: “Sarbanes Oxley section 404 An Overview of the PCAOB’s Requirements” (2004). The areas that were considered most challenging were documentation (section 404) and testing of the internal controls. Out of 175 people interviewed; 68% said that the Act has increased investor confidence in the corporate life and 58% said that the act is an “important regulatory legislation” (p. 2). KPMG also outlines Management’s responsibilities as four steps (p. 3):

- Accepting responsibilities for evaluating effectiveness of the internal controls over financial reporting
- Use suitable criteria when performing the evaluation (COSO framework)
- Support the evaluation with evidence, including documentation
- Present a written assessment about the effectiveness over internal controls by the end of the compliance year for the company

4.7 Best practice compliance of new requirements

The accelerated filer is well under way with SOX compliance process and is now in its first year of mandatory compliance. The company has adopted all of the best practices to ensure improvement to the company’s internal controls. These best practices have become a non-mandatory standard for non-public companies as well because they increase the company’s attractiveness to actual and potential stakeholders. (Jackson, 2006)
An important best practice that the accelerated filer has established is the audit committee with a minimum of 3 directors who are independent from management and from the company, other than their services on the board of directors (COSO, 2006). The members of this audit committee are dedicated, sufficiently educated and there is at least one financial expert on the committee. The non-accelerated filer has an audit committee, but at the moment it has not fully established appropriate procedures that are in compliance with SOX. All doubt of independence from management must be cleared up and procedures must be established by the audit committee by the end of the financial year.

Companies must also establish certain codes: code of ethics, code of conduct, at least for employees and management involved in the financial reporting process (Anand, 2006). This has been done in both companies in the study. When looking at this requirement for foreign subsidiaries, it’s important to make sure that country law allows such codes, and if the codes have to be approved by a governmental body before requiring the employees to sign. Once the codes have been established and adopted, they should be sent out once a year so that the employees, and management, review the provisions again. If the company has a newsletter or an intranet, this is an effective way to communicate any updates to any of the codes.

Another best practice suggestion is to involve the CFO and the CEO more into the financial reporting process because they are required to sign off on the financial reports (Jackson, 2006). They can be held criminally responsible if disclosures are deliberately altered and not complying with GAAP and legal requirements. In the case above, the assurance of effective controls has been delegated to the Internal Audit department in the case of the accelerated filer. In a large company it is difficult for the certifying managers to know exactly what is going on in the company. However, with an Internal Audit department consisting of competent personnel and effective department management, the certifying manager should be confident that the results coming out of the audits are effective.

Policies and procedures is an effective best practice that transfers some responsibility to the employees, once these policies are approved by management (Jackson, 2006). The policies and procedures are established to communicate management’s standings on treatment of accounting areas according to GAAP. This tool is effectively used for the accelerated filer. Corporate polices have been reviewed as part of SOX and new polices were developed in areas of financial reporting that were not previously identified. The polices are kept in an internal database so that they can be accessed at the same place from each of the subsidiaries. The non-accelerated filer must make sure that management reviews the existing policies since they date back several years.

The use of IT has not been mentioned much in this study, but it is a part of compliance that is very important for all companies. If management realizes that IT can help mitigate many controls in areas of high risk, or risk of errors due to manual input, the process can become much more reliable. It is also important to see IT as part of a process that has to be reviewed, if there is a flaw in the IT system it may be considered a deficiency if not resolved and mitigated (Jackson, 2006).

One requirement of the SOX Act is for the Audit Committee to (Sarbanes Oxley Act of 2002, section 301; 4):
“Complaints.-Each audit committee shall establish procedures for-
“(A) the receipt, retention, and treatment of complaints received by the issuer,
regarding accounting, internal accounting controls, or auditing matters; and
“(B) the confidential, anonymous submission by employees of the issuer of
concerns regarding questionable accounting or auditing matters.”

This together with section 806 falls under what is called the “whistleblower”
procedure. In other words, the audit committee must ensure that all complaints regarding
misconducts must be reviewed by the committee and they have to decide if this is a
genuine whistleblower case (harassment, demotion, suspension, mistreatment of funds,
employment termination) or just a compliant. To be able to cope with this a best practice
has been developed that calls for the use of an anonymous hotline that the employees can
use to report their claim. Anand (2006) suggests that the hotline is made available 24
hours a day, 7 days a week, and 365 days a year. There are several providers that
facilitate this service and report the claims directly to the audit committee and if
requested by the company, to other employees such as legal counsel, Internal Audit or
human resources. For the companies studied, this hotline is working very well for the
accelerated filer. All the subsidiaries have posters with the phone number and the website
address where claims can be submitted in the native languages of the subsidiary
countries, as well as English. For the non-accelerated filers all that exist is an address in
the code of conduct to the corporate office, addressed to the audit committee. This
procedure is one of the most important ones. The audit committee for the non-accelerated
filer must educate themselves and realize that this is not a sufficient communication
channel. At the moment, employees do not feel that they can remain anonymous this way
and a better system must be implemented.

Ways of analyzing the best practices that the company already has and what it
should have are listed in 5 major steps by Jackson (2006):

1. Evaluate the company’s style and culture (p. 93)
2. Evaluate what could damage the company’s operations or reputation (p.
   94)
3. Evaluate the company’s standard operating procedures (p. 97)
4. Ensure that everyone in the company is understands what is expected (p.
   114)
5. Make sure that the standard operating procedures are effective and
   compliant with SOX requirements and best practices (p. 114)

Once these areas have been assessed, the company can just fill in the areas where
compliance with best practices and required sections of the Act are missing.
4.8 Theoretical guides

Using theoretical guides such as interpretations of the Act itself is very useful for the SOX compliance process. Internal Auditors should understand what the whole Act requires even though they typically focus on section 404 in title four because testing also includes the rest of the required provisions. The Sarbanes-Oxley Act of 2002 can be obtained without cost on the SEC website (www.SEC.com). I have noticed that very few people (internal auditors, senior management, employees, process owners) use the source itself and rely on what consultants (used in the compliance process) say each person within the organization is responsible for. Currently there are a lot of books written and it is much easier to obtain recommendations compare to when companies started the SOX process after the Act was passed in 2002. It may be wise to go back and review these books to make sure the scope is not over or understated depending on the type of company. Many consultant companies issue guides that can also be obtained on various websites without cost; that deals with suggested implementation process. It’s important that Internal Auditors realize that not every company is the same and that the internal control system must be developed for each particular company. Some controls are the same in many companies but they have to be assessed individually and a benchmark document shouldn’t be followed without questioning. When the Internal Auditors use theoretical guides and standards, they can discuss and argue with the external auditors when it’s time for the certification process and explain why a controls is customized a certain way for their company.

4.9 Trends for Risk, Governance and Compliance

In an article, Jennifer Meiselman (2007) discusses trends for SOX compliance and it’s relation with risk and governance. She says that in the fourth years since SOX was signed into law, there is a trend towards a “holistic risk assessment” (p.40). This means that companies are now trying to move towards assessing risk for the whole enterprise/corporation for bigger companies. Smaller companies are just getting used to the process and they will aim to establish an Internal Audit department (if none exist) in order to assess financial statements and operational risks and controls. New fraud prevention programs will be adopted by many companies since the SOX assessment process exposed many of the areas that are vulnerable to this type of risks. Meiselman also believes to make the shift into a holistic approach companies will build stronger boards, senior managers and stronger governance procedures. For small companies, they will benefit from the lessons learned by the accelerated filers’ compliance process and improved guidance in regards to section 404 will be developed by PCAOB and adopted by the SEC.
CHAPTER FIVE: ANALYSIS

5.1 Introduction

In this chapter I will analyse and interpret the empirical results from the Internal Auditors and the secondary data presented in the previous chapter with the recommendations and requirements presented in the theory chapter. When possible, the requirements of the Act itself will be incorporated into the analysis.

When reading the analysis, remember that the main purposes of this thesis and the study are to assess SOX implementation from an Internal Audit point of view: the overall requirements for the company, benefits to company stakeholders, management support and challenges and legal requirements that face Internal Audit and any SOX compliance team. In addition, the two types of SEC filers will be compared to each other and to existing theory/recommendations.

5.2 Assessment of SOX implementation

5.2.1 Disadvantages of SOX

The disadvantages with SOX have more to do with the interpretation of the Act than anything else, especially for section 404. The way it was originally issued without any particular guidance from governmental bodies gave the external auditors free range to demand an enormous scope of the SOX project. This became very expensive for complying companies, especially for the non-accelerated filers. Some companies de-listed from the US stock exchanges and became private, others de-listed and re-listed themselves on foreign stock exchanges (such as London) to avoid the cost of having to comply with SOX.

Another disadvantage with SOX is the initial confusion of what the scope is and should be. Companies can determine themselves what should be included in the documentation, but there is no help to be received from the external auditors. They are not allowed to give exact guidance to companies of what controls are missing until the opinion is given at the end of the financial year. This makes it hard for small companies to know if they are on track with compliance or not.

5.2.2 Benefits of SOX

The study found that both Internal Auditors believe that a main benefit of SOX compliance is an understanding of responsibilities. This follows along the line of benefits considered by Jackson (2006, p. 53) as the ROI (Return On Investment) for SOX. Jackson lists that management and employee responsibility leads to more reliable financial reporting and evidences the existence of solid internal controls. One of the auditors’ list SOX benefits as minimization of fraud, corruption, breaches of codes of conduct and a more effective board of directors. Making the boards more effective and
more responsible was a must after the scandals that hit corporate US in the time that preceded the created of the SOX Act. According to Welytok (2006), the behavior on boards such as Enron and WorldCom when it came to overstatement of revenue, ignoring auditor’s suggestions regarding adjustments, selling stock when the employees could not, required a drastic change in the board’s responsibilities for the financial statements and the ethical conduct of the directors within. Once the board of directors take responsibility for the oversight and have the right independence mix of members, it will be hard for management to deceive the employees.

Other benefits that were listed in the theory chapter such as transparency of the company, confidence of lenders, investors and others (Welytok, 2006, p. 56) are not observed by the Internal Auditors in the study. This can depend on the fact that compliance has not been obtained yet and therefore these are benefits that come after continuous SOX compliance.

5.2.3 SOX challenges

Challenges that face the Internal Auditors in this study and the main concerns they had was the understanding and support of management in regards to SOX workload, responsibilities and obligations. They perceive that management does not understand how long the different processes takes, starting from documentation to testing the controls. The non-accelerated filer does not perceive that senior management or the board have full knowledge of what SOX really mean for them and for Internal Audit. When management and/or, the board and the audit committee do not understand their responsibilities, there will not be an effective internal control environment. Jackson (2006) points out that it is the audit committee’s responsibility to make sure that management and employees understand their roles and how to fulfill the requirements as outlined by SOX. Because this is a problem for the non-accelerated filer, they may experience problems in obtaining SOX certification. The employees can’t be expected to comply and adhere to company codes, if management does not.

In the study performed, one Internal Auditor lists the documentation, testing and the lack of agreements between the Internal Audit department managers as the most challenging during the first implementation phase. The KPMG study also states that the documentation and testing phase were considered the most challenging in the study they made based on their customer’s views. These processes are very lengthy and time-consuming during the first phase because processes are added and removed and test scripts are changed to ensure that they are operating and designed effectively.

5.3 Accelerated vs. Non-accelerated filer

The initialization of the SOX project was executed the same way for the two types of companies. An external consultant company was brought in to perform the initial risk assessment and the scope evaluation (how much of the company’s operations and subsidiaries need to be covered) based on a materiality value provided by management. As recommended by Protiviti in the theory chapter above, both companies followed the
COSO framework and assessing internal control as an integrated process of activities (COSO, 2006). The use of an approved framework is required for SOX compliance and most companies, and even though companies can choose to develop their own approach, most follow COSO. External auditors always review which framework was used and how it is applied when they assess SOX compliance for a company. COSO defines effectiveness of internal control over financial reporting as:

“a process, effected by a company’s board of directors, management and other personnel, designed to provide reasonable assurance regarding the reliability of published financial statements” (2006, p. 1).

The accelerated filers’ SOX project team received extensive training in the COSO framework when the project was first initialized by the external consultants. This improved the Internal Auditor’s understanding of their responsibilities during the implementation phase. For the non-accelerated filer it is clear that the COSO framework was used, but there is no information of how much training was received since the first documentation process was done by entirely by external consultants. COSO has developed an additional guide to its published “Internal Control – Integrated Framework” guidance that specifically targets smaller businesses. This guidance details how non-accelerated filers can utilize cost effective controls and compensating controls for their assessment. After moving the process in-house and creating an Internal Audit department the non-accelerated filer now adheres to this framework when evaluating governance and process controls. This improves the reliability of the assessments made by the non-accelerated filer because and validates the use of compensating controls when it comes to lack in segregation between preparers, reviewers and approvers of transactions within the scope. The updated small business COSO framework considers financial and resource constraints facing many non-accelerated filers (Jackson, 2006). Due to the sheer size and structure of the company, this is not a problem found with the accelerated filer because there are more layers within the financial reporting process.

Both companies utilize the Internal Audit department for their SOX implementation process. However, for the non-accelerated filer, an Internal Audit charter adoption has been delayed and SOX compliance team reports only to the CFO. Since the company is not in its compliance year yet, this is not a direct risk, however they may experience concerns with this structure from the external auditors when it comes to the reliability of the results of the internal testing. If the Internal Audit and SOX compliance is not independent from management, it may be reluctant to report any issues that concern the Senior Manager since they are reviewing the audit results and a conflict of interest arises. Anand (2006) points out that to have autonomy and opportunity to report honestly the Internal Auditors “should not be under any undue influence from executives” (p. 37). The accelerated filer on the other hand is utilizing its Internal Audit department in an effective manner and reports directly to the Audit Committee as well as to Senior Management. They utilize the Internal Auditors for the SOX compliance testing, physical inventory and financial audits. To segregate the process of SOX documentation and testing, they have created two teams that deal with SOX. This division helps ensure the objectivity of the review of the internal controls. One team suggests and implements controls and another
audits the effectiveness of those controls. The process could be more effective if management take the time to understand the work process before setting the individual objectives for each Internal Auditor. Right now both team feel like the work is not distributed evenly and this may lead to friction within the both teams.

The way management deals with the Internal Audit team is different between the two companies. For the accelerated filer there is much support from a senior manager acting like a SOX champion and driving the project forward. There is also an Internal Auditor Director and Manager who helps keep the compliance on track and who are available to answer questions about where the company stands in particular areas. The non-accelerated filer is left with little support from the senior manager responsible for the project. It will be hard for anyone in the company to take the SOX project seriously this way. There were a lot more resources available for the accelerated filer and more internal involvement than for the non-accelerated filer where the process has been managed by external consultants and Internal Audit, without any other personnel involvement.

The start of the SOX project was different between the two filers when it comes to the number of people and resources allocated to the first phase. The accelerated filer had many people working for one country at the same time and then these persons were sent out to the various subsidiaries. Even though they had sufficient manpower working on the implementation, problems arose because the scope of the documentation was very large. A year after the documentation process begun, all the Internal Auditors were brought back to the original country to reevaluate the scope of section 404. It meant that a lot of work had to be re-done since the original focus was wrong. If the project had been properly planned as suggested by Protiviti and a clear understanding of the objectives had been developed, the documentation phase could have been finalized sooner. For the non-accelerated filer, the scope was too detailed in the beginning, with operational processes documented first and financial reporting prioritized last. The work for the two counties within scope for the non-accelerated filer were conducted separately from each other but since the legal obligations and systems used in the different countries were so different, this was not a problem for the company. The difference between the two in regards to manpower and resources had much to do with the size of the companies and the financial capabilities for this type of project. The accelerated filer had more experienced and committed senior management than the non-accelerated filer. The best way to handle the situation is to wait until the scope has been finalized and narrowed down according to the latest guidelines available from the PCAOB, COSO and the SEC and to know the deadlines for compliance.

Both companies began compliance process in 2005. To date the accelerated filer is within its first year of required SOX compliance while the non-accelerated filer has until the end of 2007 until the CFO and the CEO have to assess their effectiveness over internal controls. A problem for the non-accelerated filers Internal Audit department is that senior management and the board considers the cost of the external auditors when evaluating the cost of what it will take to reach compliance. They do not want to spend more money and does not realize that the money paid to the externals consultants are now a sunk cost and should not be considered when evaluating new compliance investments.
The accelerated filer on the other hand has learned that the compliance process works better with one documentation team and one auditing team. When the duties are segregated there can be more reliance on the end result because Internal Auditors are not evaluating their own work. It gives the certifying officers a comfort to know that they are independent of each other.
CHAPTER SIX: CONCLUSION

6.1 Introduction

In this chapter, the whole thesis come to an end and final conclusions of lessons learned during the research process are summarized. After receiving the questionnaire answers and reviewing the secondary data findings it is clear that are similarities between the different types of companies when it comes to problems experienced during the implementation and testing process which are discussed in the sections below.

From the questionnaire and the secondary data, I have concluded some final recommendations for Internal Auditors and Management that are starting out with SOX, see section 6.3 below. I hope this will give some insight to what other Internal Auditors are experiencing and how they can try to resolve the problems before even starting with the documentation process.

6.2 Research Purpose revisited

Revisiting the research purpose helps in understanding the conclusions and the recommendations listed below. The main purpose of this study and this thesis was to get an overall assessment of SOX implementation from Internal Auditor’s point of view. The reason for this was that Internal Audit are often the ones recruited as the in-house resources and actually be the ones who documents controls, risks, gap’s and perform the testing of the effectiveness of the internal controls. There have been many studies and articles regarding SOX from a risk assessment, cost, governance and compliance best practices, but not many directly from an Internal Auditor’s point of view. This thesis has sought to explore their experience of what implementation is actually like and what they feel their obligations, challenges, requirements and ultimately what the benefits for the company and other stakeholders will be. Then these experiences and views were analyzed to come up to pinpoint for new Internal Auditors, where they may experience challenges and problems and where to turn theory wise to obtain solutions and support.

6.3 Conclusion from comparison of SOX implementation approach

The research revealed that there are similarities between the different sized companies based on their assessment of SOX implementation. SOX implementation increases an understanding of responsibilities with other employees within the company; from operations personnel to middle and senior management. SOX is the tool used to put the controls in place to keep the company honest by minimizing corruption and fraud.

There are also challenges with SOX and in the study it mainly comes down to managements understanding, or lack thereof. Either there is no support in understanding the principles of SOX or lack of understanding of the time the various areas of implementation takes.
6.4 Conclusion of comparison of filers

The research revealed that there are similarities between the different sized companies and although the accelerated filer has more manpower to perform the SOX implementation, the process is not perfect. There are gaps in senior management’s knowledge of the implementation of the SOX project, its requirements and the time that compliance takes; whether its documentation or testing. It is clear that more research has to be done to get to the bottom on factors are to why this is the case 4 years after the SOX Act was signed into US law. This area needs to be investigated because for all companies, no matter the size, July 15th 2007 is the SOX compliance deadline. All CFO’s and CEO’s must sign off on the effectiveness of the internal controls on the Financial Year (FY) ending on or after that date and must be aware of the details of what is going on in their companies. They must be prepared to assess risks based on the COSO model, be certain of how trustworthy their testing structure is and what level of risks are facing their companies. This is especially important for the non-accelerated filer used in this study; right now the Internal Audit department does not seem to be confident that senior management and the board has the right knowledge to comfortable sign off at the end of the year. SOX compliance implementation process is very long and management must ensure that they have the right people for the job and that they are reporting independently and free of bias.

Both companies used external consultants to set up the initial scope of SOX. However, the accelerated filer included internal audit in the initial phase of documentation which will benefit them because the internal staff was able to take over the documentation process and thus costs were saved. The non-accelerated filer did not use internal resources for the initial project and they may pay for that later on if key personnel involved in the SOX process leaves the company and someone else has to start all over again.

6.5 Recommendation for Internal Auditors

The first recommendation for Internal Auditors starting out on the SOX project is to make sure that senior management and the Board of Directors are educated in their responsibilities according to SOX. For accelerated filers, the Internal Auditors may be unable to assess the knowledge of the board, but try to get some information from the director or manager of Internal Audit in that case. When possible, outline each group’s responsibilities and explain that it is in their best interest to implement the best practices and not rely on Internal Audit to complete the compliance process. Without support by senior management and the Board, the internal control implementation will not be effective. Show what the benefit of compliance is at the same time as outlining management’s responsibilities. This will help them understand how SOX compliance can be used as a competitive tool and benefit the whole organization. Boards and senior management often benefit from detailed examples of the work done. When they have something tangible to look at, it’s easier for them to connect with the work.
Keep up to date on new SOX legislation and review the governmental or professional organization’s websites (PCAOB, AICPA, IIA, SEC and COSO) or use an online data base/service from a consultant firm specializing in this type of service. Even if the SOX Act is here to stay there may be amendments to it, changes to best practices, requirements for non-accelerated filer’s compliance or changes in due dates. Some of the sites explained above issue standards and comments on new legislation and it’s important that Internal Auditors keep up to date or they may get overrun by the external auditors requiring too much documentation or scope.

6.6 Recommendation for Management Support

The support from management and the board is crucial for SOX implementation. When the Internal Auditors go in and implement SOX they make a lot of changes in how the work is performed by clerks and supervisors in various departments. If management is not available to support the process, it makes it very difficult for the Internal Auditors to do their job. Protiviti recommends that the project sponsor should be someone who takes the project serious and that the best choice is for a certifying officer (CEO or CFO) to be a SOX “champion”. The study showed that the Internal Auditors do not feel supported or that the understanding is there from management. Senior Management must enlighten themselves about SOX and not demand that Internal Audit tell them exactly what to do. It’s important that management follow the project all the way from assessment to implementation, for it to be a success.

Senior Management must also understand the implications of the SOX process. For the compliance year, the CFO and the CEO must sign that they are aware that the internal controls are working and are effective within the organization. For controls or high risk areas that are not in compliance or are without a proper control, they must certify that they have disclosed this in detail to the external auditors.

6.7 Recommendations for further studies

I hope that the results and analysis presented in this thesis will open the eyes of management and boards so that they understand the challenges facing Internal Audit, and how important it is that they are supported from the top of the company. I also hope that an interest has been developed to further investigate SOX implementations from in-house Internal Auditors. Further research could mean to increase the scope of the companies investigated, or focus on one type of company at a time (large accelerated, accelerated or non-accelerated filer). Since provisions are reviewed by US governmental agencies, it would be interesting to see where recommendations have changed of how to implement the Act the best way, especially for non-accelerated filers.
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Websites:

# Index

<table>
<thead>
<tr>
<th>A</th>
<th>12, 21, 27</th>
</tr>
</thead>
<tbody>
<tr>
<td>Accelerated filer</td>
<td>12, 21, 27</td>
</tr>
<tr>
<td>Audit Committee</td>
<td>8, 13</td>
</tr>
<tr>
<td>C</td>
<td>IV, 13</td>
</tr>
<tr>
<td>COSO</td>
<td>IV, 13</td>
</tr>
<tr>
<td>D</td>
<td>17</td>
</tr>
<tr>
<td>Deloitte</td>
<td>17</td>
</tr>
<tr>
<td>G</td>
<td>5, 14, 16</td>
</tr>
<tr>
<td>Governance</td>
<td>5, 14, 16</td>
</tr>
<tr>
<td>I</td>
<td>16</td>
</tr>
<tr>
<td>Internal Audit</td>
<td>16</td>
</tr>
<tr>
<td>Internal Controls</td>
<td>17, 21</td>
</tr>
<tr>
<td>K</td>
<td>26</td>
</tr>
<tr>
<td>KPMG</td>
<td>26</td>
</tr>
<tr>
<td>N</td>
<td>12, 21, 27</td>
</tr>
<tr>
<td>Non-accelerated filer</td>
<td>12, 21, 27</td>
</tr>
<tr>
<td>P</td>
<td>7</td>
</tr>
<tr>
<td>PCAOB</td>
<td>7</td>
</tr>
<tr>
<td>Protiviti</td>
<td>18</td>
</tr>
<tr>
<td>R</td>
<td>3, 36</td>
</tr>
<tr>
<td>Risks</td>
<td>3, 36</td>
</tr>
<tr>
<td>S</td>
<td>1, 6, 7</td>
</tr>
<tr>
<td>SEC</td>
<td>1, 6, 7</td>
</tr>
<tr>
<td>SOX</td>
<td>1, 7</td>
</tr>
</tbody>
</table>
Exhibits

Exhibit A: Internal Audit Questionnaire

A. Demographical Data

1. Years of Internal Audit working experience
2. Years of SOX project involvement for the company
3. Current position

B. SOX Project

4. How was the SOX project initialized?
   a. By hiring External Consultants
   b. By utilizing Internal Audit department
   c. Both a and b
   d. Don’t know
   e. Other
   If Other, please describe:

5. How big is the Internal Audit department in your company?
   a. 1-3
   b. 4-6
   c. 7-10
   d. 10-13
   e. 14 or more

6. How many Internal Auditors were actively working with SOX project during the first phase (documentation, control/risk assessment, gap identification/remediation and 1st testing)?
   a. 1-3
   b. 4-6
   c. 7-10
   d. 10-13
   e. 14 or more
7. How many other persons (consultants or from other departments) were actively working with SOX project during the first phase (first phase definition, see Q6)?
   a. 1-3
   b. 4-6
   c. 7-10
   d. 10-13
   e. 14 or more

8. What has been the most difficult part of the SOX project during the first phase (first phase definition, see Q6)?
   a. Risk Assessment
   b. Documentation (controls and risks)
   c. GAP analysis
   d. GAP remediation
   e. Testing
   f. Senior Management support
   g. Other
   If Other, please describe:

9. By implementing SOX, what do you believe are the main benefits to the Company?
   a. Minimization of Fraud, Corruption
   b. Minimization of Breaches to Codes of Conduct
   c. Understanding of Responsibility
   d. More effective Board of Director
   e. All of the above, a-d
   f. No benefits
   g. Other
   If Other, please describe:

10. What level of knowledge and understanding of SOX do you perceive the following have?
    Rank each from 0-7, where 0 is “no understanding at all” and 7 are “fully understand” all provisions required by them, under SOX:
    a. Board of Directors
    b. Audit Committee
    c. Senior Management (Sr VP, EVP, CEO, COO, CFO)
    d. Middle Management (Controller - VP)
    e. Operations Personnel
    f. Accounting Personnel
    g. Internal Audit Personnel
11. What level of support and understanding towards Internal Audit SOX workload, obligations and responsibilities do you feel from the following have: Rank each from 0-7, where 0 is “no understanding at all” and 7 is “fully understand” all provisions required by them, under SOX:

a. Board of Directors  
b. Audit Committee  
c. Senior Management (Sr VP, EVP, CEO, COO, CFO)  
d. Middle Management (Controller - VP)  
e. Operations Personnel  
f. Accounting Personnel  
g. Internal Audit Management

**Your additional comments to any questions posed in the questionnaire:**

Thank you for your time and consideration!