

The *Sarbanes-Oxley Act of 2002* (the “Act”)

The following are questions posed by Niquette Kelcher of SmartPros to me (Gary Wyatt) on September 25, 2002. My answers are underneath each question in blue. The answers I have given reflect solely my own opinions, and do not necessarily reflect the views of Travis, Wolff & Company, L.L.P. or its other partners.

Questions and Answers:

What is of the utmost importance for finance and audit professionals (staff) to know (regarding the Act)?

The impact of the Act is different, depending upon your perspective. I will comment solely on the meaning of the Act to accounting firms and compensation/benefits consulting firms.

Accounting firms performing audits for public companies are precluded from providing some types of additional services, and must obtain audit committee pre-approval for other services not specifically precluded. Additionally, such firms will be required to register with a public oversight board.

For accounting firms with quite a number of public clients, the impact will be dramatic. It will change the way they do business. No longer can the financial statement audit be used as a “loss leader” in hopes of selling more lucrative tax and consulting services. The largest accounting firms will likely lose many tax/consulting clients to each other. Also, high-quality regional and specialty “boutique” accounting firms may pick up significant new tax and consulting engagements.

Even though the Act is generally applicable only to public companies, the principles may eventually spread into “best practices” affecting auditors of privately held companies.

It seems likely that some accounting firms may split advisory/consulting functions off into separate firms.

Switching gears, compensation and benefits consultants will likely be attentive to two general areas of the Act...the “blackout” rules, and the officer loan prohibitions.

In terms of a qualified retirement plan, including 401(k), a blackout is generally a period of more than three consecutive business days in which any ability of individual account plan participants or beneficiaries, which is otherwise available under the terms of such plan, to direct or diversify assets credited to their accounts, obtain loans from the plan, or to obtain distributions from the plan is temporarily suspended, limited, or restricted. If the plan involves publicly traded employer securities, executives are generally prohibited from trading any of their employer securities held outside the plan during a blackout.

Many popular executive compensation techniques involve loans from the company to an executive. Public companies will be precluded from using these techniques in the future. This may sound like a small change, but it will fundamentally change the way compensation is delivered to executives of public companies.

For example, it is not unusual for companies to make loans to executives to enable them to purchase stock of the company. From an outside shareholder’s point of view, this should be more favorable than a grant of options to the executive. If an executive holds options, he has only upside...no downside. If an executive is given a loan (with full recourse) to purchase stock, he can experience both gains and losses...just like an outside shareholder.

What are some steps managers can/should take to "get the ball rolling" to ensure their staff is well-educated on the Act?

There are numerous insightful summaries both on the Internet, and in traditional media. For accounting firms, the AICPA has produced a sample letter for dissemination to staff.

What policies do firms need to be sure they have in place? What's the best way of implementing them if they don't already have them?

For accounting firms with relatively few publicly held clients, deliberation is ongoing as to the proper response. Part of that will be determined by the extent to which principles in the Act may eventually be extended to all audit engagements.

Should a company, if it doesn't already have one in place, consider implementing an ethics program for employees? If so, how would you recommend.

In Texas, our CPE requirements already include a recurrent ethics course requirement. The challenge is to make business ethics a strong part of the culture of a firm.

What are some good (preferably time-efficient) resources for staff to utilize to get up to speed? Do you feel CPE courses are a good resource?

I sense that most accounting firms will conduct some sort of internal briefing on the Act. Additionally, as with anything new, accounting firms should encourage reading and study.

In your opinion, what will be the greatest challenge for companies with this new legislation?

Whether for accounting firms, consulting firms or client firms, the greatest challenge will probably be required compliance and reporting activities.