streetwise

BY GERALD ARANOFF, STEPHEN BARLAS, MIKE OSHEROFF, KATHY WILLIAMS

[NEWS]

IAESB Publishes Ethics Education Paper, Proposes IT Guidance for Professional Accountants

KATHY WILLIAMS

The International Accounting Education Standards Board (IAESB), an independent standards-setting body within the International Federation of Accountants (IFAC), has published two documents you might want to read.

The first is a new information paper titled *Approaches to the Development and Maintenance of Professional Values, Ethics and Attitudes in Accounting Education Programs*. The result of a research project examining ethics education in the accounting profession worldwide, the paper is designed to stimulate discussion and debate on the subject of ethics education. It also will serve as the basis for the development of International Education Practice Statement (IEPS) 4.1 on this same topic. An *Ethics Education Toolkit* is also in the works.

To download the publication for free, visit the IFAC website at www.ifac.org/store and click on Education on the left-hand side of the page. Scroll down the list of items until you see Information Papers, and click on the title.

IT Guidance

The second document is an IEPS exposure draft titled *Information Technology for Professional Accountants*. It provides details of the knowledge and skills that professional accountants working in the IT environment need. For example, it outlines the competencies required of a user of IT services, such as a financial manager, financial controller, or tax practitioner. And it describes what's needed to work as an assurance provider and evaluator (such as an internal financial or operational auditor or evaluator of information systems), as a manager of information systems (such as a knowledge manager or data center manager), and as a designer of business systems (such as a knowledge engineer or as an external advisor or consultant).

To download a copy, visit www.ifac.org/EDs. Scroll down until you see the section titled Issued by the International Accounting Education Standards Board (formerly the Education Committee), and click on the title of the document.

Comments about the exposure draft are due by November 15, 2006. You may submit them by e-mail to edcomments@ifac.org. ■

IFAC HIGHLIGHTS INTERNAL CONTROL DEVELOPMENTS

A new IFAC publication issued by the Professional Accountants in Business (PAIB) Committee, *Internal Controls—A Review of Current Developments*, describes much of the current thinking on internal control from various countries around the world. It also summarizes key internal control frameworks, highlights recent legislation, and discusses the role of internal control in enhancing corporate governance.

One of the main findings is that there's a general consensus worldwide that an internal control framework should take a principles- and market-based, risk-focused approach. "Prescriptive and legislative requirements are often not recommended as a means of encouraging good internal control systems, as under these circumstances organizations are more likely to view internal control as merely a compliance exercise rather than internal control as an integral part of good business practice," the publication notes.

You can download the report for free from the IFAC website at www.ifac.org. ■

Letters to the Editor

I enjoyed reading Thomas Corbett's "Three Questions Accounting" (April 2006). I think both sides are right in his second sentence: "Some people have called it a new paradigm in management accounting, but others have said that it's simply a new way of showing old cost accounting concepts, such as variable costing." I see a new model here, and I also see a new way to show old cost accounting concepts.

Corbett states at the beginning: "Throughput Accounting is only concerned with the relevant costs and revenues associated with a decision." This fits perfectly with Horngren's definition of relevant costs and revenues: "Relevant costs are expected future costs and relevant revenues are expected future revenues that differ among alternative courses of action being considered (Horngren's *Cost Accounting: A Managerial Emphasis*, 12th edition, 2005, p. 380).

Corbett's inset illustration is clear. He could've used Horngren's relevant revenues and costs terminology:

	Alt 1	Alt 2
Relevant revenues	R$ 103,320	R$ 67,680
Relevant expenses	R$ 15,000	R$ 15,000
Differential profit	R$ 88,320	R$ 52,680

Both Corbett and his critic, B. Douglas Clinton, (June 2006) discuss the dangers of oversimplification here. I take issue with Clinton's conclusion: "Finally, TOC [theory of constraints] is referred to as a 'management accounting system...,' an assertion that seems overly ambitious given the

continued on page 24

[GOVERNMENT]

Section 404 Saga Continues

STEPHEN BARLAS, EDITOR

The Securities & Exchange Commission will issue guidance for corporate management on how to comply with the provisions of Section 404 of the Sarbanes-Oxley Act, which requires companies to explain their internal controls and test them. The SEC issued a "Concept Release" in mid-July that outlined some of the areas it may address when the guidance is published. No date for publication was mentioned. Large companies, of course, have had to comply with 404 for two years. Smaller companies received an initial reprieve, but, with first-time compliance looming, they are pushing the SEC hard to make some changes in required compliance. The SEC Advisory Committee on Smaller Public Companies raised a number of concerns in an April report on the ability of smaller companies to comply with 404 in a cost-effective manner. That was followed days later by a U.S. Government Accountability Office report that said much the same thing.

Of course, larger companies and the U.S. Chamber of Commerce have been arguing for the past year that Section 404 is too costly. The SEC took a first crack at quieting that murmuring when it issued limited guidance in April 2005 relating to the exercise of professional judgment, the concept of reasonable assurance, and the permitted communications between management and auditors. But this next round of guidance will go further. For example, the 2005 guidance stated that management needs to use "reasoned judgment" in identifying internal controls. But few understood what that meant. The July 2006 Concept Release maintains that "many companies did not efficiently and effectively identify risks to reliable financial reporting and relevant internal control functions, ultimately leading to the identification, documentation, and testing of an excessive number of controls. We are also skeptical of the large number of internal controls that some companies have identified, documented, and tested."

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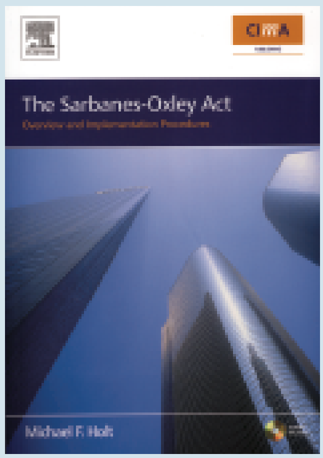
Part of the reason for that problem is that corporate management, in implementing Section 404, may have leaned too heavily on the Public Company Accounting Oversight Board (PCAOB) Auditing Standard No. 2 (AS2), *An Audit of Internal Control over Financial Reporting Performed in Conjunction with an Audit of the Financial Statements*. Published in June 2004, this was meant for outside auditors, not management. But many corporate financial and accounting departments interpreted AS2 very conservatively, increasing costs far beyond what was necessary. This is

continued on page 24

[BOOKS]

Tools for SOX Compliance

By now, every management accountant is aware of the Sarbanes-Oxley Act of 2002 (SOX), passed in reaction to corporate scandal and investor loss of the late 1990s. In *The Sarbanes-Oxley Act: Overview and Implementation Procedures*, Michael F. Holt presents an outline of SOX with emphasis on the sections that require action on the part of corporate personnel, usually the CFO and CEO. Instead of just indicating what has to be done to meet the requirements of SOX, Holt presents a survey of tools that can be used to put a company in compliance with the Act.



The heart and soul of a company's SOX compliance is its internal control system, which is defined as "a process, affected by an entity's board of directors, management, and other personnel, designed to provide reasonable assurance regarding the achievement of objectives in...operations,...financial reporting, and...compliance with applicable laws and regulations." Note the inclusion of operations and applicable regulations. SOX assumes that the existence of adequate internal control with appropriate monitoring and modification to meet changing business conditions for all three areas will ensure complete and transparent stakeholder information as well as achieve efficient company management.

All firms have some sort of internal control system. SOX compliance starts with identifying the parts of that system and fully documenting each step. Management's real task in compliance is to identify which tasks actually are—or at least should be—part of the firm's internal control system according to the above definition. Holt uses the historical framework of materiality of reporting to gauge which activities are part of the system of reporting. He also includes the same requirement for operations and legal areas. Management must identify each activity and process and ask if it is part of the definition of internal control and, therefore, needs to be addressed.

After the identification of processes that should be included as part of the internal control system, a large part of the initial cost of SOX compliance lies with system documentation. Documentation is best done by computer to ensure uniformity and storage. Holt summarizes a number of Sarbanes-Oxley compliance software titles in an appendix at the end of the book and includes Web addresses of the publishers so that interested readers can research a particular publication more thoroughly.

Most of the mentioned titles are project driven; that is, the software author regards each process of manufacturing, information recording, and external reporting as part of a process having an input, ownership, workflow, internal documentation, and output. Holt includes an entire appendix on one title that he feels closely resembles the COSO framework of internal control, Processes on Demand, by BOT International.

As a bonus, Holt's book includes a CD-ROM with management templates for customizing into a firm's own implementation. Included on the CD is a PowerPoint presentation of essential points of SOX that require a firm's action, which can be used in a presentation to boards of directors and senior management who will be involved in implementation.

In *The Sarbanes-Oxley Act*, Holt presents a brief outline of the Act's requirements, coverage of the tools an accountant needs to actually fulfill those requirements, and reviews of software that mainly use the project management paradigm for attacking any problems in business: identify the process, document how it works, monitor it for effectiveness, modify it to meet changing business needs, and then start over for the next relevant process of internal control. By doing this, management will not only go a long way toward satisfying external auditors and SEC requirements of SOX but also make their companies more efficient and improve profitability.—*Mike Osheroff*, osheroff@worldaccessnet.com.

[ACADEMIC] cont'd from p. 20

submitted, in total, to each professor. While each case contains discipline-specific questions, both faculty members review and grade the entire case. Subsequent classroom discussions follow. Using perspectives from both disciplines during discussions helps students form tangible connections between accounting and finance information, especially when both instructors together present ideal solutions to cases in one classroom setting. While optional, the team-teaching approach reinforces the interdependence of each discipline.

Anecdotal evidence suggests that these linked courses have been received favorably by both faculty and students. More importantly, feedback from both suggests that our main goal of increasing students' awareness of the interconnections between accounting and finance is being accomplished. Given the newness of the course, outcome assessment data isn't available yet. Overall, exposure to faculty members from distinct disciplines in such a tangible linked manner forces our students to recognize the relationships between the subjects much earlier in their educational process. ■

NOTE: *This column is based on a longer version of a manuscript that has been accepted for publication in* Advances in Accounting Education.

Bruce A. Leauby, Ph.D., CMA, CPA, CFE, is associate professor of accounting at La Salle University, Philadelphia, Pa. You can contact him at (215) 951-1490 or leauby@lasalle.edu.

Kristin Wentzel, Ph.D., is associate professor of accounting at La Salle University. You can contact her at (215) 951-5176 or wentzel@lasalle.edu.

[GOV'T] cont'd from p. 22

the problem that the SEC hopes to resolve with its new guidance, which the agency emphasized will be "scalable." That apparently means the guidance won't be written only with small companies in mind but also will take the concerns of *Fortune* 500 companies into account.

New Chief Accountant

With more expansive 404 guidance now in the SEC pipeline, Conrad Hewitt, the SEC's new chief accountant, joins the Commission at a critical time. The post was vacant since Donald Nicolaisen departed last fall. Hewitt, who had been serving on three corporate board audit committees, had otherwise been retired from a full-time job since 1998, when he was a California state banking official. From 1972 to 1995, Hewitt was the managing partner of Ernst & Young and its predecessor firm, Ernst & Ernst, in the firm's Northern California (1986-1995), Seattle (1979-1986), and Honolulu (1972-1979) regions. In his statement upon joining the SEC, Hewitt noted that he has worked with many of the big accounting firms to implement Sarbanes-Oxley and looks forward to working with the PCAOB "to maximize the protection of shareholders while eliminating excessive costs and burdens both here and abroad."

Bill Would Eliminate Some State Taxation of Corporations

Protests from states and local governments forced House Republican leaders to postpone a floor vote on a bill limiting state taxation of corporations. A spokesman for Rep. John Boehner (R.-Ill.), the House Majority Leader, said, "Some misperceptions about [the bill's] effect on states" resulted in the vote being delayed, probably until after the August recess. The bill (H.R. 1956) would establish a national standard for when states can collect business activity taxes from multistate companies whose principal locations are outside the state but who have many customers within the state. The bill has been strongly supported by companies in the retail, financial, and medical industries. The bill would require companies to have a physical presence in a state for at least 21 days before they could be taxed. But there would be some exceptions. The National Governors Association spooked both Republicans and Democrats in the days prior to the scheduled House floor vote by publicizing a study that projected revenue losses to the states would be nearly double the annual losses of $3 billion by 2011 that the Congressional Budget Office projected. Besides business activity taxes, states couldn't levy gross receipts, license, or franchise taxes. ■

[LETTERS] cont'd from p. 22

host of decisions for which it apparently cannot provide adequate decision support information."

Horngren also discusses potential problems using relevant-cost analysis. He analyzes a wide variety of decision-making problems with both a relevant-cost analysis and with a total-cost analysis. In my teaching, I use the relevant costs and revenues approach exclusively notwithstanding potential problems. Maybe this is why I like Corbett's paradigm.

Corbett is expanding the knowledge of cost accounting and is giving instructors like me more material to teach. Hopefully this will lead to better decision making. Corbett is making an important contribution to management accounting.

Gerald Aranoff