streetwise

BY STEPHEN BARLAS, CHRISTOPHER DOWSETT, MIKE OSHEROFF, KATHY WILLIAMS

[NEWS]

SOX Optimization Opportunities Still Exist

KATHY WILLIAMS

Although companies have been complying with the Sarbanes-Oxley Act (SOX) for a while now, significant opportunities still exist for them to reduce compliance costs and to use SOX to improve business operations. These are a couple of the findings from a new study by BMR Advisors and Financial Executives Research Foundation (FERF), the research affiliate of Financial Executives International (FEI).

Titled *SOX 404 Optimization: Operational Trends*, the report is based on in-depth interviews with more than 30 senior finance and internal control professionals during September and October. It identifies program *scope* and program *structure* as the principal drivers of SOX program efficiency. Also, two types of SOX operating models are emerging in which the main distinguishing factor is the extent to which responsibility for management and execution is either centralized or decentralized.

When citing what they thought would be good opportunities for their companies to benefit from SOX, executives identified four areas:

- Transformation of their control effort to focus less on manual controls and more on automated and entity-level controls.
- Consolidation of processes onto a reduced number of systems. Surprisingly, more of the companies interviewed had a fragmented IT architecture than an integrated enterprise resource planning (ERP) or financials platform, which made it difficult to move toward automated controls. The other approach is consolidating processes into fewer locations through a shared-services or business process outsourcing (BPO) approach for key elements of the finance function.
- Adoption of more sophisticated testing approaches, including remote testing.
- Selective strategic sourcing of SOX testing work.

Although most of the interviewees said they were satisfied with the benefits their companies have been reaping from the SOX compliance experience, they did have a few suggested improvements: There should be a degree of rotational testing instead of every year if a control doesn't change from year to year; SOX should be integrated into a broader, more holistic view of business risk; it should be simplified to better align with future migration to International Financial Reporting Standards (IFRS); and there should be a redefinition of the qualification criteria for smaller organizations.

For more information, contact Kristen Lewko at kristen.lewko@fd.com. ■

IMA LIFE

IMA members, we need your help. *Strategic Finance* is starting a new monthly column called "IMA Life," and we want your contributions.

Each column will be written by an IMA member and will be your reflections on some aspect of IMA. It can be about what IMA means to you, your experiences in IMA, certification, membership, how IMA has helped you, your work—your thoughts about your life in IMA or IMA in general.

We want the stories of all types of IMA members. You can be a student member, a young professional, in the middle of your career, or toward the end of your career. You can have been a member for less than a year or for 50 years. You can be a chapter member or a member-at-large, in a leadership position or not.

If you would like to write an "IMA Life" column or would like to recommend someone to be featured, please e-mail Kathy Williams at kwilliams@imanet.org. A team from the IMA office will make the final selections. ■

TRY THE NEW *STRATEGIC FINANCE* DIGIMAG

If you haven't tried the digital format version (or DigiMag) of *Strategic Finance* yet, now's the time. The DigiMag platform was redesigned, and the software was upgraded. Those of you who logged on to read the November 2008 issue may have been surprised by the new look that greeted you. Among the enhanced features are a simpler user interface, an improved Search function, thumbnail views to make browsing easier, quicker loading times, and sharper page images that make reading the text easier at both full-page and zoom views. Readers can also adjust the size of the DigiMag window and watch as the full-page view resizes automatically. DigiMag provides you with the familiar look of the printed magazine combined with the ease and convenience of being on the Web. The new platform is so easy to use that first-time viewers will be comfortable–just don't lick your finger before turning the page! IMA members can read the latest issue of *Strategic Finance* at www.imanet.org/publications_sfm_digmag.asp.

We welcome all opinions on articles and departments published in *Strategic Finance*. E-mail correspondence to Kathy Williams at kwilliams@imanet.org.

[GOVERNMENT]

Changes to SFAS No. 157 Less Likely

STEPHEN BARLAS, EDITOR

A Democratic-led Congress means less likelihood that any Securities & Exchange Commission (SEC) recommendations to ease the terms of Statement of Financial Accounting Standards (SFAS) No. 157, "Fair Value Measurement," will bear actual fruit. The SEC must submit a report to the new Congress in January on mark-to-market accounting as a result of a provision in the Emergency Economic Stabilization Act of 2008 (otherwise known as the bailout bill). Corporate CFOs would like to see that report recommend some easing of the Standard, which the SEC and the Financial Accounting Standards Board (FASB) tried to do, though not very aggressively, with guidance they issued at the end of September. Thomas Quaadman, executive director for financial reporting policy and investor opportunity at the U.S. Chamber of Commerce, not only wants major changes to SFAS No. 157, but he's also pushing for a "broad review of accounting standards and a comprehensive plan of action to address shortcomings in the financial reporting process." Quaadman pushed his many-faceted deregulatory proposal before Barack Obama won the election. The Chamber's hope that Congress might buy another one of their suggestions—testing accounting standards for "economic impact"—has undoubtedly deflated like a punctured balloon. Obama and his Democratic cohorts running Congress are much more likely to listen to traditional Democratic constituencies such as the Council of Institutional Investors and the Consumers Federation of America. They want the SEC, which has authority over FASB standards, to stand pat on SFAS No. 157. Is there a viable middle position? Some accounting firms think there's room for compromise—whether it's politically viable is another question. For example, Vincent Colman, U.S. assurance managing partner and national professional practice leader at PricewaterhouseCoopers LLP, supports exploring possible refinements in fair value reporting, possibly separating for accounting purposes the periodic changes in fair value into two components: (1) incurred credit losses and (2) all other changes in fair value (including, for example, liquidity discounts).

Is there a viable middle position on SFAS No. 157?

CD&A Disclosure at Issue in Bailout Reporting

With the Democratic Congress and Obama administration, expect attention on executive compensation early on in Congress. First up on that agenda may be the provisions in the Troubled Assets Relief Program (TARP) Capital Purchase Program (CPP), which was set up as part of

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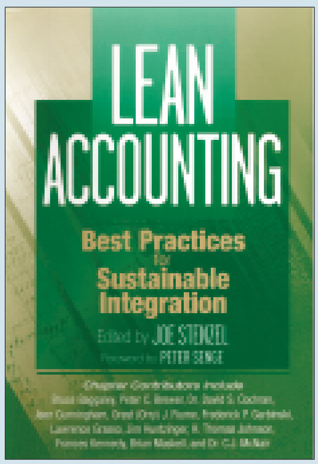
[BOOKS]

Implementing Lean Successfully

Management accountants are familiar with lean production methods and Lean Accounting, the term used to describe the information management system of those methods. For example, using lean has made Toyota one of the best auto manufacturers in terms of customer service, product innovation, and profitability for years. Yet why do so many other firms attempt implementation only to achieve less than expected process improvement or fail outright? *Lean Accounting: Best Practices for Sustainable Integration*, edited by Joe Stenzel, looks at that question with 11 articles by experts in the field of lean practices, all addressing basics of implementation and obstacles to successful integration within existing businesses. Without adequate planning by management, the teamwork of management and line employees, and continued reintegration of the lean system as business requirements change, the initial conversion from a traditional manufacturing system to lean will only lead to temporary success.



The articles in *Lean Accounting* point to several reasons for the failure of lean integration. Most can be broken down into disagreements regarding the definition of the firm's basic business units and their output and the arrangement of these units into the total firm. The lean firm must not only focus on its smallest manufacturing or service components, where internal and external consumer satisfaction is determined, but also on the goal of all these units combined, where cost and resource use is determined.

Lean Accounting has several chapters explaining basic lean business processes and how to evaluate their performance. Basically, business units must be organized in a physical layout so that both input and output can be identified clearly. Internal control of the basic business unit isn't established by a detailed written procedure but, rather, by closely monitoring various unit metrics per benchmark. Changing metrics per benchmark are readily displayed to employees so that physical resource consumption and manufacturing methods can be adjusted to minimize cost.

Flexibility of physical operation is a paramount concern. Several chapters point out that processes should no longer be designed for economies of scale. They must be designed to meet incremental customer demand (whether from a consumer or from other business units). Employees must be cross-trained in physical operations to satisfy this demand, enabling them to be transferred to other basic business units when changes to resource use per benchmarks warrant it. Instead of just being a resource, employees must be encouraged to adopt an attitude of identification with the goal of the firm—satisfying customer demand and rewarding employees' contributions to total firm profitability.

Instead of employing a demand-driven system where each business unit tries to minimize its costs, lean is based on a customer-driven pull system. Lean ensures that business unit costs and, therefore, total firm costs are as low as possible while satisfying consumer demand. Instead of bottom-up costing, lean is top-down: Costs increase or fall only as customer demand does. Instead of producing for lowest cost, business units must produce to only fulfill the needs of the next-higher business unit, beginning with the consumer and working down.

Lean Accounting ends with an approach to sustaining lean and Lean Accounting in a changing business climate. Since the lean model is based on top-down planning, it must begin, by definition, by considering customer demand. For most firms, customer demand changes. A sustainable lean initiative will always consider this changing customer demand. Efficiency of operations and cost will very quickly be noticed in changing business unit costs per benchmark, but

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[GOV'T] *cont'd from p. 22*
the Emergency Economic Stabilization Act. The Treasury is making investments in financial companies with bailout funds in exchange for those companies adopting limits on executive pay. The Treasury put out interim rules, some of which bear on financial reporting. Business groups think those rules should be loosened in some areas, not tightened, as Democrats are likely to do. Tim Bartl, general counsel for the Center on Executive Compensation, which is composed of *Fortune* 500 companies, supports a certification by a board of directors that its corporate pay plan doesn't encourage "excessive risk." But he disagrees that the certification should be in the Compensation Discussion and Analysis (CD&A). "Because the CD&A is a report that is signed by management, the inclusion of the Committee's certification in the CD&A stands corporate governance on its head by having management certify that the compensation committee's certification is correct," Bartl states. The Center believes that the certification should be included in the compensation committee report rather than the CD&A.

Corporate Treasurers to SEC: "Keep Credit Rating Agencies for Money Markets"

Credit rating agencies have taken it on the chin for their role in the financial meltdown, and the SEC, which has received its share of criticism for complicity, is now trying to lessen reliance on the nationally recognized statistical rating organizations (NRSROs), which are now operating under a new regulatory regime specified by the Credit Rating Agency Reform Act of 2006. Believe it or not, both business and labor groups want the SEC to maintain its current statutory requirement that money market funds, a big investment option for corporations, continue to rely on credit rating agencies. What gives? At issue is an SEC-proposed rule from July that would eliminate reference to NRSROs in a couple of rules, such as SEC Rule 2a–7, which now requires a money market fund's portfolio investments to have received credit ratings from the NRSROs in one of the two highest short-term rating categories. The SEC wants to eliminate that requirement. Even Dan Pedrotty, director of the office of investment at the AFL-CIO, who admits "significant shortcomings in the NRSROs' rating methods," otherwise believes that the SEC's concern that the money market funds have come to place "undue reliance" on NRSROs is "misguided." John Grout, policy and technical director for the Association of Corporate Treasurers, says, "At a time when investing in the banks is perceived as much more risky, any changes to 2a-7 funds could have a destabilizing effect in the market." ■

[BOOKS] *cont'd from p. 23*
the key is communication between production supervisors and management. Meeting customer demand at the lowest cost is a sure way of guaranteeing profitability—or at least minimizing loss.

In traditional management accounting systems, the controller and CEO may feel responsible for the profitability of the firm. In the lean firm, profitability is the responsibility of everyone. The CEO and controller in the lean firm are responsible for organizing business units and identifying customer demand, but line employees are responsible for cost. Until the CEO and controller accept their roles as resource managers and true teamwork among management and line employee is exercised, lean will forever remain just another fad theory that can deliver only partial success.—*Mike Osheroff, osheroff@wa-net.com*