SF bulletin

By Stephen Barlas, Noah Barsky, Mike Osheroff

GOVERNMENT

SEC Commissioner Opposes Additional Internal Controls SOX Exemptions

by Stephen Barlas

Now that companies with market capitalizations under $75 million have been freed from complying with Section 404(b) of the Sarbanes-Oxley Act (SOX), the question is whether the Securities & Exchange Commission (SEC) will recommend that companies up to $250 million be freed, too. One of the key provisions of Section 404(b) requires independent auditors to attest to management's assessment of the effectiveness of its internal controls over financial reporting. Companies under $75 million were relieved of that requirement by the Dodd-Frank Wall Street Reform and Consumer Protection Act, which President Obama signed on July 21, 2010. That bill also contains a provision that requires the SEC to conduct a study to determine how it could reduce the burden of complying with Section 404(b) for companies whose market capitalization is between $75 million and $250 million while maintaining investor protections for such companies. At least one SEC commissioner thinks narrowing the application of 404(b) is a bad idea. In a speech in Los Angeles on September 21, Luis A. Aguilar said, "These efforts to create a two-tiered market by stripping investor protections at smaller public companies are troubling. I do believe that investors in all public companies—large and small—should receive comparable protections and that the way these protections are provided can be scaled to the size and resources of a company."

The Center for Audit Quality's fourth annual "Main Street Investor Survey" of 1,001 individual investors found that 65% of investors expressed "concern," half of whom are "very concerned," that smaller companies won't be required to have their company's auditor attest to, and report on, management's assessment of the effectiveness of its internal controls over financial reporting. Even more investors say they would be concerned should Congress expand this exemption to companies with market capitalization of $75 million or more. Approximately 24% are "concerned" about the possibility of extending the exemption, and 57% are "very concerned" about this possibility (a total of 81% of investors have concerns in this area).

GOVERNMENT

Tax Increase for Multinationals Pays for Jobs Bill

Most of the talk about the Small Business Jobs Act (H.R. 5297) that President Obama signed on September 27 had to do with its provisions extending some depreciation and expensing allowances for small business, as well as the $30 billion in Treasury Department preferred stock investments in small banks, which would be expected to expand loans to small businesses. There weren't any ostensible "job-creating incentives" in the bill for larger companies. For example, there was no extension of the research and development tax credit that expired at the end of last year. The Obama administration supports extending it, but such a provision wasn't in the bill. What was worse was that bigger businesses, especially multinationals, will be paying for a portion of the $42 billion bill ($12 billion in extended tax breaks)

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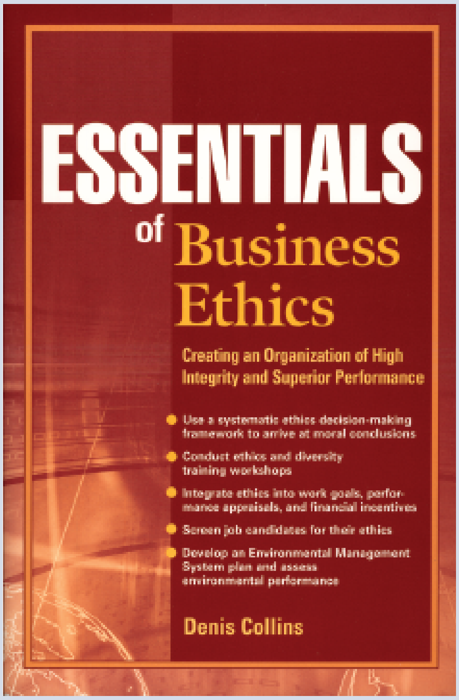
BOOKS

Creating an Ethical Business

In *The Wealth of Nations*, Adam Smith talked about how governments promulgated laws to prevent entrepreneurial excess, leading to the greatest benefit to society. But he also discussed what he called the invisible hand, which would help regulate the new business paradigm that was capitalism. His thesis assumed a belief in a higher power (i.e., God), a sense of community of business owners and workers, and the absence of environmental constraints—conditions that aren't necessarily as applicable anymore. In today's world, these three keys of business regulation would be viewed as part of business ethics. In *Essentials of Business Ethics*, Denis Collins goes beyond guidance by statute and law to focus on business conduct based on the benefit of all stakeholders, which extends far beyond short-term profitability.



While law is "thou shalt not," business ethics would be based on the Golden Rule of "do unto others." Collins outlines how to bring and keep ethical practice—as opposed to mere legality—in all businesses. As with most business behaviors, ethical practice really begins at the top, and the "tone at the top" works its way down to the rank and file. If the business owner or CEO is ethical and takes into consideration the long-term benefit for all stakeholders, there's a good chance that most employees will temper their legal activity with ethical constraints.

Notice that says "most employees." The bulk of *Essentials of Business Ethics* is a guide to ensuring that employees are ethical and that they continue to hone their decision making to meet changing business conditions in an ethical way. Since it only takes one unethical employee to bring a firm to its day of reckoning, companies should use an in-depth interview and screening process to ensure they are hiring ethical employees in the first place. Hiring ethical employees and showing them what is expected of them is the first step to good business ethics.

Firms should have a code of ethics that formalizes their highest values and a code of conduct that translates the ethics code to meet myriad business situations, providing a rough blueprint for ethical behavior. Collins presents an outline of ethical review within a company to ensure that everyday decisions are ethical and that new circumstances are evaluated in the light of the firm's code of ethics. This review includes annual ethics training, a decision-review framework, rewards and punishments for ethical behavior or lack thereof, empowerment of employees to make their own ethics decisions, community outreach beyond providing just goods and services, environmental concerns for areas that will affect the firm's operations in the future, and letting all stakeholders know that the firm's actions are based on total community welfare rather than just on consumer benefit.

An unethical firm can certainly make a killing in the market in the short run, but its long-term survival is in doubt. In *Essentials of Business Ethics*, Collins shows how firms can operate and prosper using an ethical business plan for the long run. While readers might focus on the bottom line, they must understand that ethical behavior factors into that bottom line through employee morale, customer loyalty, and lack of adverse governmental regulation. Isn't that really the best way to run a business?—Mike Osheroff, osheroff@wa-net.com

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via new tax payment obligations.

The big new obligation, pitched as one of a number of Democratic initiatives to prevent overseas outsourcing of jobs, would affect the treatment of guarantee fees under source rules. I won't get into the complexities of this provision, which are ample. Suffice it to say that the provision penalizes some U.S. companies doing business overseas—to the tune of $2 billion in new tax payment obligations over 10 years. But big corporations didn't take quite as big a tax hit as they would have had Congress passed a second bill hatched by Senate Democrats: the Creating American Jobs and Ending Offshoring Act. That was the anti-offshoring bill (S. 3816) that was defeated on the Senate floor on September 28. The idea there was to give U.S. companies payroll tax relief when they hired new employees to replace existing employees working overseas. That payroll tax reduction would have been paid for by repealing tax deferral for firms that move operations from the U.S. to other countries and then import their products back home. Groups such as the Business Roundtable and the National Association of Manufacturers are unalterably opposed to killing the deferral provision, even at the expense of losing the new payroll deduction, which some business analysts don't believe would stop outsourcing anyhow.

LETTERS

Middle East Salary Survey

I am absolutely amazed and disappointed that Professor Lawson's "IMA Middle East Salary Survey" (October 2010), sent to more than 4,400 professionals in over a dozen countries, failed to include the most modern, democratic, capitalist economy in the region—Israel.

According to recent reports by the Bloomberg news service and others, the performance of the Israeli economy compares very favorably to its Middle Eastern neighbors, as well as large, industrialized Western economies such as the United States. Israel's prime stock index (the TA-25) is up over 20% year-to-date, unemployment is around 6%, and the economy is expected to grow over 4% this year and next. Exports have grown by 13%, consumer spending is up over 5%, and housing starts have increased at 11%. Consumer debt levels remain low and saving rates remarkably high. Such a robust and thriving economy provides innumerable career opportunities for the accounting and financial professionals that IMA serves. Salary survey data from this overlooked Middle East nation would likely provide meaningful and intriguing comparisons to the study's reported regional and U.S. results.

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Author's Note:

Thank you for your message! There was no overt intent to exclude Israel, and its omission was solely due to an oversight. It would have been interesting to see salary levels and the impact of the CMA® designation in that country. I'm guessing that members there earn way more than elsewhere in the region. Hopefully this will be an annual survey, and the suggestions we received this time around will help us do even better next time.

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IMA Professor-in-Residence and Vice President of Research

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We also invite you to post your opinions and questions at *LinkUp IMA*.
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