



Reporting Compliance with the Sarbanes-Oxley Act Using Repository-based Tools

“Good News/Bad News”

Now that publicly traded companies have first-year experience in reporting compliance with the Sarbanes-Oxley Act of 2002, lessons have been learned and improvement efforts are underway in anticipation of reporting compliance next year. The first year experience has had a substantial impact on companies.

“For publicly traded companies in the U.S., the good news is Sarbanes-Oxley section 404 compliance efforts are either completed or coming to a close [for 2004.] The bad news is the process has turned out to be substantially more difficult, time consuming and expensive than the U.S. government forecasted when it passed the law in 2002 (no surprise here). It also was much more of an issue than corporations anticipated. In a recent survey of its membership, Finance Executives International (FEI) found that first year compliance costs for section 404 averaged \$1.9 million, including an additional \$509,000 in auditing expenses and \$700,000 in IT consulting and software. The effort has cost the companies an average of 12,000 hours of internal time (*i.e.*, about seven ‘full-time equivalent’ years). For the largest companies (revenues in excess of \$5 billion), FEI found an even greater burden. Initial year expenses were \$4.7 million, including 35,000 hours (*i.e.*, 20 FTE-years) of internal time.”

--Sales Masters World¹

History of the Sarbanes-Oxley Act of 2002

On July 30, 2002, President Bush signed into law the Sarbanes-Oxley Act of 2002, consisting of 11 parts and 66 sections. The purpose of the Act is to restore investors’ confidence in the accounting profession, restore accountability and corporate governance at the executive level, and protect the public interest. This Act was the result of the large-scale corporate and accounting scandals in the United States involving some of America’s most well known companies. While the compliance reporting deadline has been extended twice, publicly traded companies using the calendar year as their fiscal year have at least one year’s experience as of 2004.

¹ <http://www.sales-masters-world.com>



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Though the Sarbanes-Oxley Act is complex and comprehensive, the major requirements for corporations are²:

- Section 302 – Corporate responsibility for financial reporting
- Section 404 – Assess internal controls
- Section 409 – Public disclosure
- Section 906 – Certification of financial reports on a periodic basis.

In particular, Section 302 requires CEOs and CFOs to certify in each annual and quarterly report filed by a public company that the report does not contain any untrue statement of a material fact or omit a material fact, and officers have evaluated and concluded on the effectiveness of the company's internal controls.

Section 404 requires a report on management's assessment of its internal controls with each annual report filed by a public company. This includes stating the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting and contains an assessment of their effectiveness. It also requires that each registered public accounting firm that prepares or issues the audit report for the issuer shall attest to, and report on, the assessment made by the management of the issuer, in accordance with standards adopted by the Public Company Accounting Oversight Board (PCAOB).

Section 409 requires disclosure to the public on a "rapid and current basis" information concerning material changes to financial condition or results of operations.

Section 906 requires that the period report containing financial information complies with the Exchange Act and fairly presents financial conditions and results of operations.

Client's Situation with Previous Compliance Reporting Efforts

Doreen Evans Associates' client, a Fortune 500 financial services firm, operates two primary businesses: asset accumulation and risk management. Within its risk management business its principal line of business is property and casualty insurance, with over \$2 billion in written premiums. Within its asset accumulation business is a closed block of business consisting primarily of variable annuities and life insurance, with \$14 billion in assets. Its companies employ over 7,000 employees worldwide.

One of the client's Business Operations Analysts was assigned the task of documenting internal controls over financial reporting in the annuity and life insurance death claims areas for compliance with Sarbanes-Oxley. He compiled a 14-column spreadsheet, which included items such as function, risk, mitigating control, control objective, control frequency, performer of the control, etc. Missing, however, was identification of where

² <http://www.CCIonline.biz>, "U.S. Securities & Exchange Commission (SEC) Compliance, Sarbanes-Oxley & FASB Rulings Overview," July, 2004.

these risks exist in the business processes, and where are the mitigating controls for these risks.

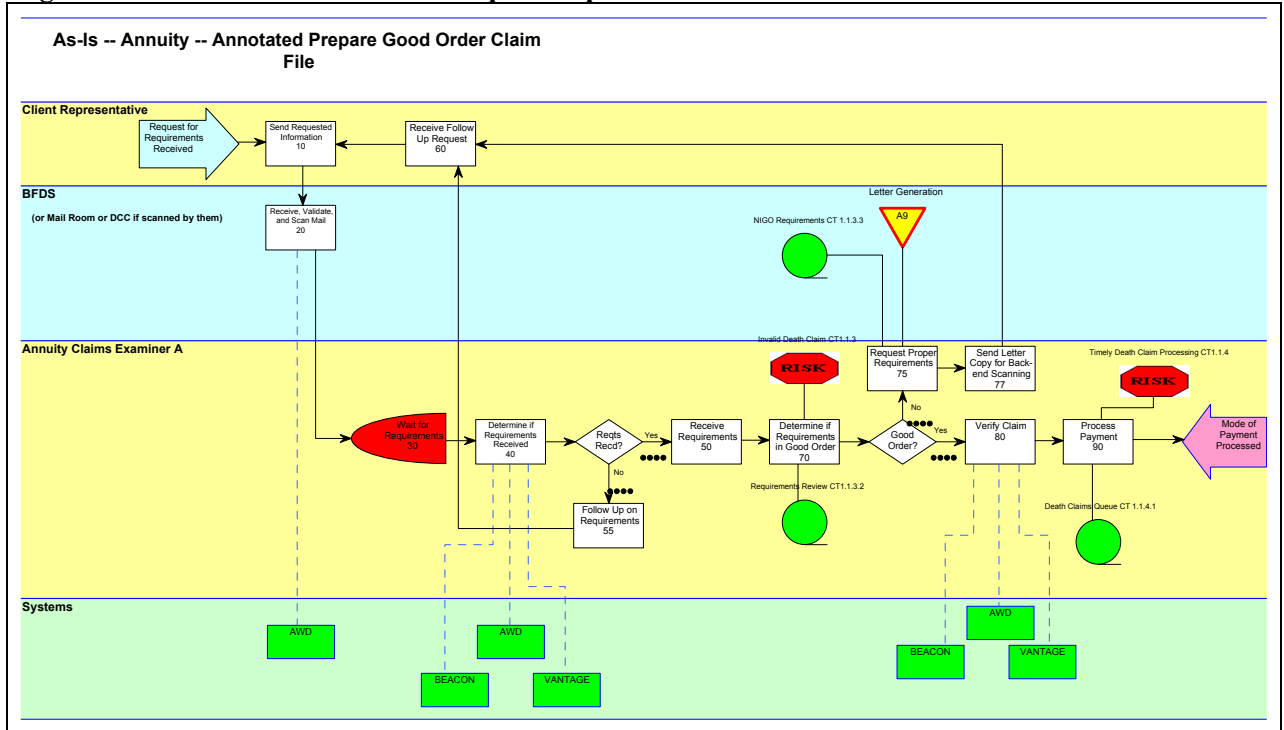
What Was Done

Doreen Evans Associates (DEA) was engaged to document the clients' business processes in the annuity and life insurance death claims areas. DEA, with input provided by the client's subject matter experts, mapped the current business processes using Popkin Software & Systems' System Architect™, a repository-based modeling tool. System Architect provides an underlying storage mechanism for its repository, based on either SQL Server 2000 Standard Edition or Microsoft Server Desktop Engine 2000 (MSDE 2000). In this multi-user/multi-database environment data is shared between a "Master Database" and individual databases. A multi-user/single-database architecture (i.e., with the database shared on a server) is usually implemented for deliverable printing, updating, and sharing among users.

The Process Flow Maps that were produced included the roles that perform the process, the process steps performed, the decisions that are made while performing the process steps, delays incurred in the process, information system interfaces with process steps, and the result of the process.

Subject Matter Experts reviewed and approved the Process Flow Maps. The Maps were then annotated to include where the financial risks exist, and where the financial controls are in place to mitigate these risks. Note that financial risks are indicated with a red stop sign symbol with the word "Risk" in the center, and controls are indicated as green traffic lights (circles), each with their respective names and reference numbers. (See Figure 1: Annotated Process Flow Map Example.)

Figure 1: Annotated Process Flow Map Example



All process documentation (including process step descriptions, frequencies, process delays, business rules governing decisions, role descriptions, financial risks and controls) was captured in System Architect. When an electronic file is open in System Architect all documentation is easily accessed.

However, for hard-copy reports DEA has developed proprietary Microsoft Word templates that were used to extract the process documentation from System Architect. These Word documents, namely, Process Flow Map Detail Reports and Inventory of Risks, provided text in support of the Process Flow Maps. The Process Flow Map Detail Report includes the process step reference numbers, the roles that perform the process, the process step name, process step description, the business rules used in making the process decisions, information systems interfaces with the process steps, and the potential financial risks in the process. (See Figure 2: Process Flow Map Detail Report Example.)

The Inventory of Risks includes the risk name, risk description, impact, which Process Flow Maps include these risks, the financial control name, and control description. Thus all related documentation is in one repository. (See Figure 3: Inventory of Risks Example.)



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Figure 2: Process Flow Map Detail Report Example

Step No.	Role	Step Name	Description	Business Rules	Systems	Risks
20	BFDS	Receive, Validate, and Scan Mail	Receive mail, validate originals, and scan documents. The images are then indexed by the Document Control Center.	<u>Death Certificate Validation</u> If the death certificate is not original, stamp it "Not Original" before it is scanned.	* AWD	
30	Annuity Claims Examiner A	Wait for Requirements	Wait for requirements to be received while claim is in pend status.			
40	Annuity Claims Examiner A	Determine if Requirements Received	Determine if all requested requirements have been received. Check file to determine what was needed, add comments into "additional info" icon.		* AWD * VANTAGE * BEACON	
70	Annuity Claims Examiner A	Determine if Requirements in Good Order	Determine if the Requirement received is in Good Order.	<u>Good Order</u> A Requirement is in Good Order if it includes the names of the intended beneficiaries with their applicable percentages, their relationship(s) to the insured/annuitant/owner, their social security number, their addresses, their Dates of Birth, and signature of the owner.		* Invalid Death Claim CT1.1.3



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Figure 3: Inventory of Risks Example

Risk Name	Risk Description	Impact	On Process Flow Maps	Control Name	Control Description
Invalid Death Claim CT1.1.3	Death Claim is not valid.	Medium	* As-Is -- Annuity -- VANTAGE -- Annotated Record Claim and Request Requirements * As-Is -- Annuity -- BEACON -- Annotated Record Claim and Request Requirements * As-Is -- Annuity -- Annotated Prepare Good Order Claim File	NIGO Requirements CT 1.1.3.3 Review Requirements CT1.1.3.2 Request Requirements CT1.1.3.1 Contestable (Homicide) Claim CT1.1.3.4	<p>Pending death claim work items remain in the system until the requirements are received and the death claim is processed. The work item cannot be deleted from the system to ensure all death claims are processed. Outstanding pending death claim work items are followed up for NIGO (Not In Good Order) items. Once NIGO items are received the death claim work item is processed. Supervisor can check the Claims queue at any time to review items that are outstanding.</p> <p>A claimant's statement signed by the beneficiary and a certified death certificate stating manner or cause of death are required for a death claim to be processed. Upon receipt of the documentation the examiner reviews and verifies to ensure valid death claim.</p> <p>Claims examiner reviews the contract for outstanding requirements and immediately sends out requirements letter requesting appropriate documentation to establish a valid claim.</p>



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Results and Benefits

While it is difficult to quantify the benefits of the use of System Architect to assist in compliance reporting, anecdotal comments by those who are responsible for the reporting give an indication of the value. The following comments were made by two individuals who have been directly involved in the compliance reporting process.

“Man, these Process Flow Maps with the financial risks and controls are the greatest things since canned beer! I wish I had had them six months ago when I had to compile that darned Sarbanes-Oxley spreadsheet! The last time it took me three months to compile that spreadsheet, but now I can update it in 30 minutes.”

--Client Business Operations Analyst

“I attest that these Process Flow Maps illustrating the financial risks and controls provide the best documentation the Government could ever hope to be given in order to satisfy legislative requirements, and I have no reservations whatsoever in certifying this company complies to the fullest extent possible.”

--Client External Auditor

Conclusion

With the annotation of the Process Flow Maps to include the financial risks and financial controls, it is easily seen where in the processes potential risks exist, and where controls are in place to mitigate these risks. Furthermore, all documentation is in one database, where it can easily be accessed, updated, and shared electronically. As business processes and information systems change, the impact on the financial risks and controls can be easily assessed and updated, thus facilitating compliance reporting, with a minimum of cost and effort.

About Doreen Evans Associates

Doreen Evans Associates (DEA) is a professional services firm that focuses on business process improvement. We can help you change a process, build an enterprise architecture, or define requirements for your systems and technologies. Founded in 1992 as a woman-owned, privately-held small business, our mission is to ensure that business need drives solutions.

Bibliography

¹Sales Masters World

http://www.sales-masters-world.com/printpage.php/153_0_6_0/

²<http://www.CCIonline.biz>, “U.S. Securities & Exchange Commission (SEC) Compliance, Sarbanes-Oxley & FASB Rulings Overview,” July, 2004.

“Sarbanes-Oxley Act: A Long-Term Opportunity Awaits,” Steve Dwyer, Senior Editor, Insurance Working News, March 2004, pp. 8 and 10.