"Can the costs of complying with SOX 404(a) be reduced without sacrificing the quality of a review of internal controls over financial reporting (ICFR)?

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Presenter #1

Bob Benoit is President of Lord & Benoit. He served on the most recent COSO Monitoring Project Task Force. He also served on AICPA Peer Review Acceptance Board for ten years. He is the author of the Lord & Benoit Reports, which have been referenced by the SEC, PCAOB, Wall Street Journal, Business Week, all Big 4 firms and over 150 newspapers, magazines, legal, educational and trade journals worldwide. Bob is also the first evaluator to use the 2006 COSO Guidance for Smaller Public Companies, and the inventor of Virtual SOX.

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Presenter #2

Michael Mooradian, CISA is Vice President, Operations & IT Compliance at Lord & Benoit, LLC, and a seasoned professional with over twenty years of senior management experience in the information technology field. Prior to joining Lord & Benoit, Michael directed IT organizations supporting multi-national locations for Digital Equipment Corporation, Brooks Automation and The Thomson Corporation. He has provided consulting services to clients such as AT&T, the Securities and Exchange Commission (SEC), Dun & Bradstreet, IBES, Business Wire, Ziff-Davis Publishing and Pfizer.

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Today's Webinar

Regulatory Update on SOX 404

Advantages of Virtual SOX

How and Why SOX 404(a) can be done remotely

Tools and Live Demo

SOX IT compliance

Lessons Learned

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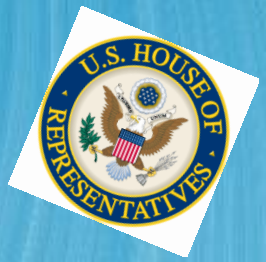
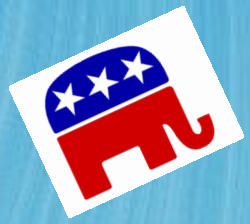
Regulatory Update





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Securities & Exchange Commission

"Since there will be no further Commission extensions, it is important for all public companies and their auditors to act with deliberate speed to move toward full Section 404 compliance."

SEC Chairman Mary L. Schapiro

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Securities & Exchange Commission

"The Commission is for the first time resolving that uncertainty by making it clear that all public companies, regardless of size, will be required to comply with Section 404(b) of the Sarbanes-Oxley Act."

Commissioner Luis A. Aguilar

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Public Companies Accounting Oversight Board

"In its latest summary of its inspections of the eight largest audit firms — covering four years of reviews — the Public Company Accounting Oversight Board pings the auditors for failing to use enough professional skepticism in their audits of companies' financial statements…

PCAOB®

CFO Magazine

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Public Companies Accounting Oversight Board

"A second area reviewed, actually a subset of the first, was the assessment of fraud risk."

"In a minority of audits, the board found failure to do more rigorous testing in areas of greater risk, and failure to test compensating controls."

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Public Companies Accounting Oversight Board

"The board also evaluated auditors' use of the work of others to cut down on their own work, a practice that AS5 specifically allows. But some audits didn't sufficiently assess the competency or objectivity of others' work, particularly when the work was performed by company personnel other than internal auditors."

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ALL Governing Boards

Smaller companies have a harder time performing SOX inhouse, because evaluators must be competent AND objective. Objectivity requires a person to be uninvolved in the process altogether. Otherwise they would be reviewing their own work, which is not considered a valid monitoring evaluation. Competence and objectivity are required by COSO, SEC Interpretive Guidance and PCAOB Standard 5.

PCAOB

COSO

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ALL Governing Boards

Smaller companies rarely have competent repeat skill sets in house. This is particularly apparent in Information Technology. A complete review of the IT function is required each year. Smaller companies typically have only one or two internal IT staff. Therefore it is difficult if not impossible to effectively objectively assess IT, since the assessor is probably the one doing the work.

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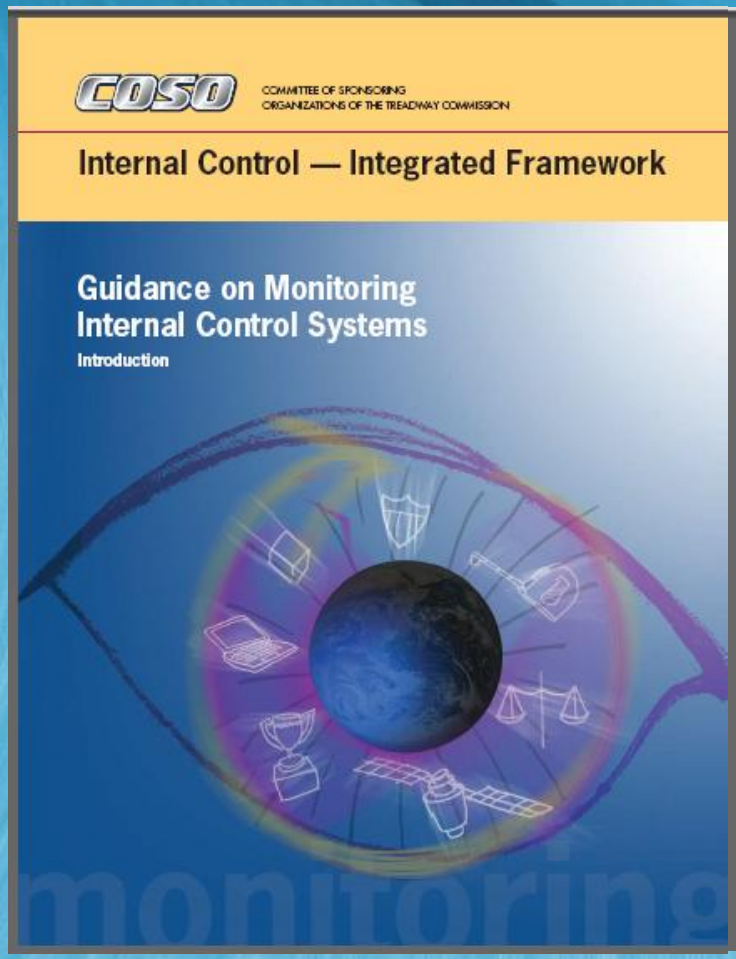
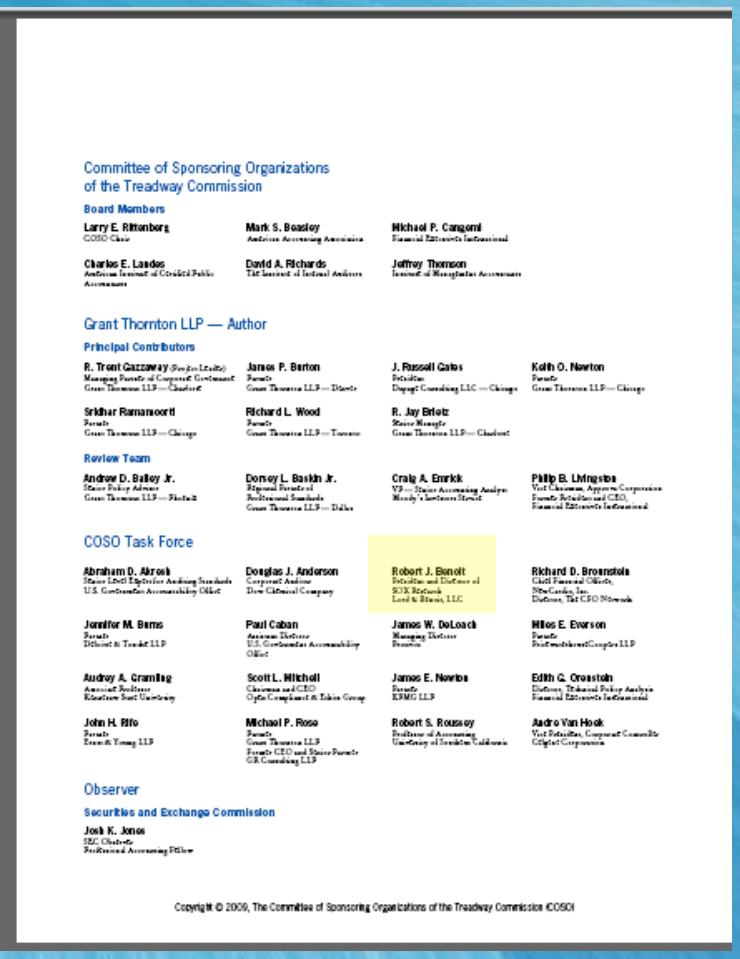
Committee of Sponsoring Organizations of the Treadway Commission





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Observer

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Professional Accounting Fellow

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House of Representatives

H.R. 4173, Wall Street Reform and Consumer Protection Act would exempt companies with market caps of $75 million or below from Sarbanes-Oxley Act's Section 404(b). Section 404(b) requires a company's auditors to document and test its internal controls over financial reporting (ICFR).

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Senate Finance Committee

The exemption of SOX 404(b) is notably absent from the Senate version of the reform bill drafted by Christopher Dodd, Chairman of the Senate Finance Committee.

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Senate Finance Committee

Sen. James DeMint mentioned he will introduce an amendment to the Senate's proposed regulatory reform bill that would exempt non-accelerated filers from compliance with Section 404(b) of the Sarbanes-Oxley Act.

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What is Virtual SOX?

What is Sarbanes-Oxley Section 404(a)?

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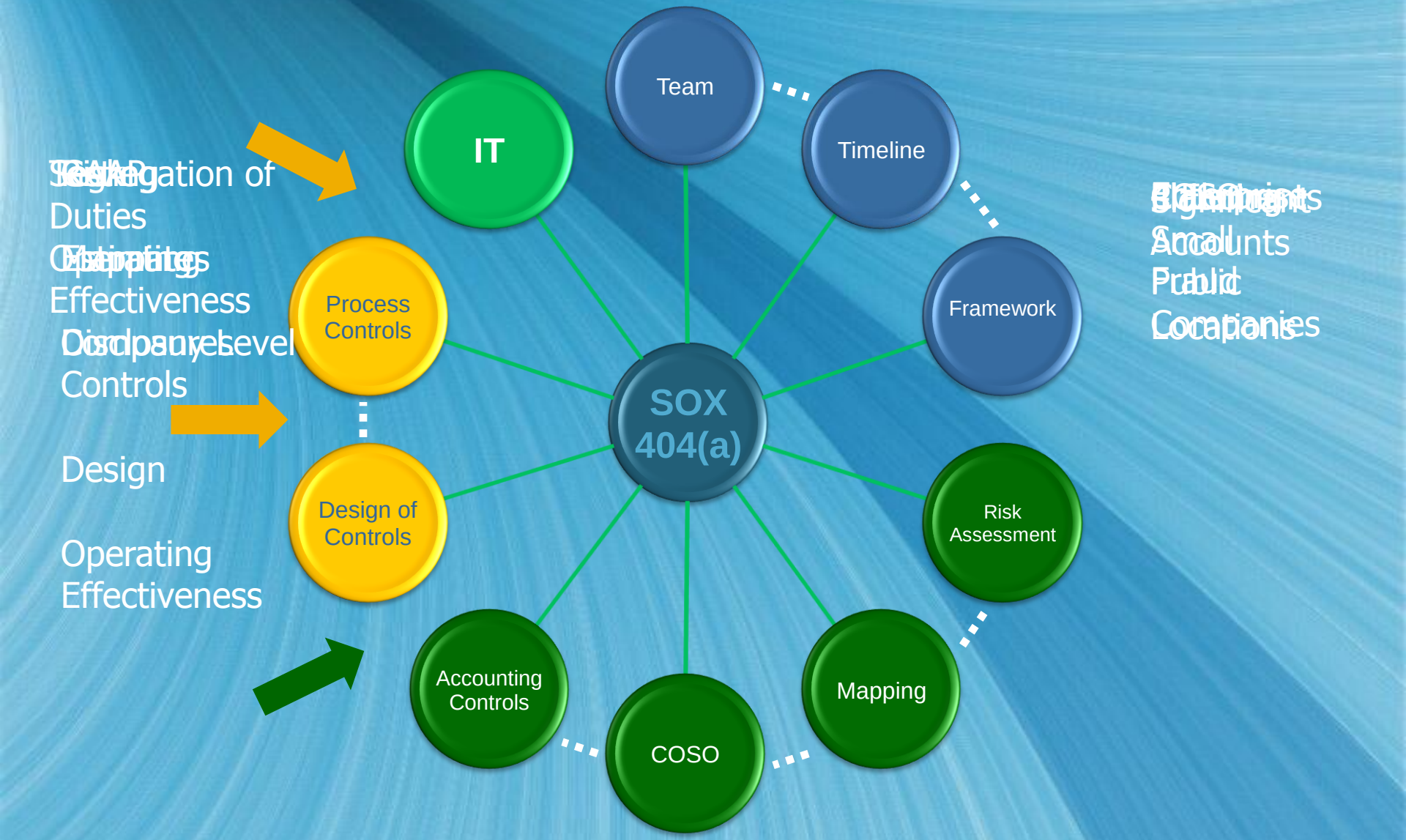
Lord & Benoit's Framework



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Four Resource Requirements

High Level Internal Control

Low Level Internal Control

Financial Reporting (EITF, SOPs, FASBs, SABs)

High Level IT

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Advantages of Virtual SOX

- Least vexing way to comply SOX Section 404(a) - without compromising quality
- Multiple locations
- Most cost effective: no travel time or travel costs
- Evaluators are well trained and supervised

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Advantages of Virtual SOX

- Minimal management disruption
- Convenience to outside auditors
- Engagements are well planned
- Meetings are scheduled, min ad hoc
- The right questions are asked in advance

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What is Virtual SOX?

- Background
- Definition of "Virtual SOX"

  "The process of using remote technologies to reduce the costs of complying with SOX Section 404(a) without sacrificing the quality of a review of internal controls over financial reporting (ICFR)

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Why can Virtual SOX be done remotely?

- Not an audit
- Management Self Assessment
- Local administrative personnel
- As long as objective
- Relationship of objectivity to size of business

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How can SOX be done remotely?

- Use of simple and affordable technology tools.
- Good communication
- Good project management, planning, scoping, sampling
- Choices of evidence: inquiry, reperformance, inspection, observation

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Virtual SOX 404 - TOOLS

- Teleconferencing, online audio visual meeting tools
- Web-based presentation tools using screen sharing (our machine or the client's machine could be viewed or changed real time)
- Share contact lists including the outside auditors
- E-mails for copies of financial statements, spreadsheets, journal entries and disclosure checklists

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Virtual SOX 404 - TOOLS

- Document scans
- VPN connections
- Screen shots
- Version control and access control tools to prevent unauthorized on inadvertent file changes.
- Shared site for sharing any documents, secure, SSL certificates, encrypted uploads and downloads to/from the site

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Virtual SOX 404 - TOOLS

- Agreed upon Timelines
- Project tracking
- Scheduling
- Automatic notification of document updates

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Virtual SOX Site

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Virtual SOX IT

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Virtual SOX IT

Can it work? Yes!

- CHALLENGE: perform SOX IT assessment remotely due to schedule conflicts, multiple locations, resource restraints
- SOLUTION: a Virtual SOX IT engagement
- RATIONALE: efficient, unobtrusive, cost-effective

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Virtual SOX IT Implementation

- Risk Assessment/Mapping/Narratives/Design of Controls and testing—can all be easily accomplished remotely
- Collaboration tools such as Windows Live Meeting or WebEx , audio/video conferencing, web-based content management system

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Virtual SOX IT Data Collection Technology Guidelines

- Deploy technologies that can be implemented and maintained with a minimum of effort
- Implement simple solutions in order to avoid the costs associated with complexity
- Standardize on as few software and hardware platforms as possible to benefit from economies of scale

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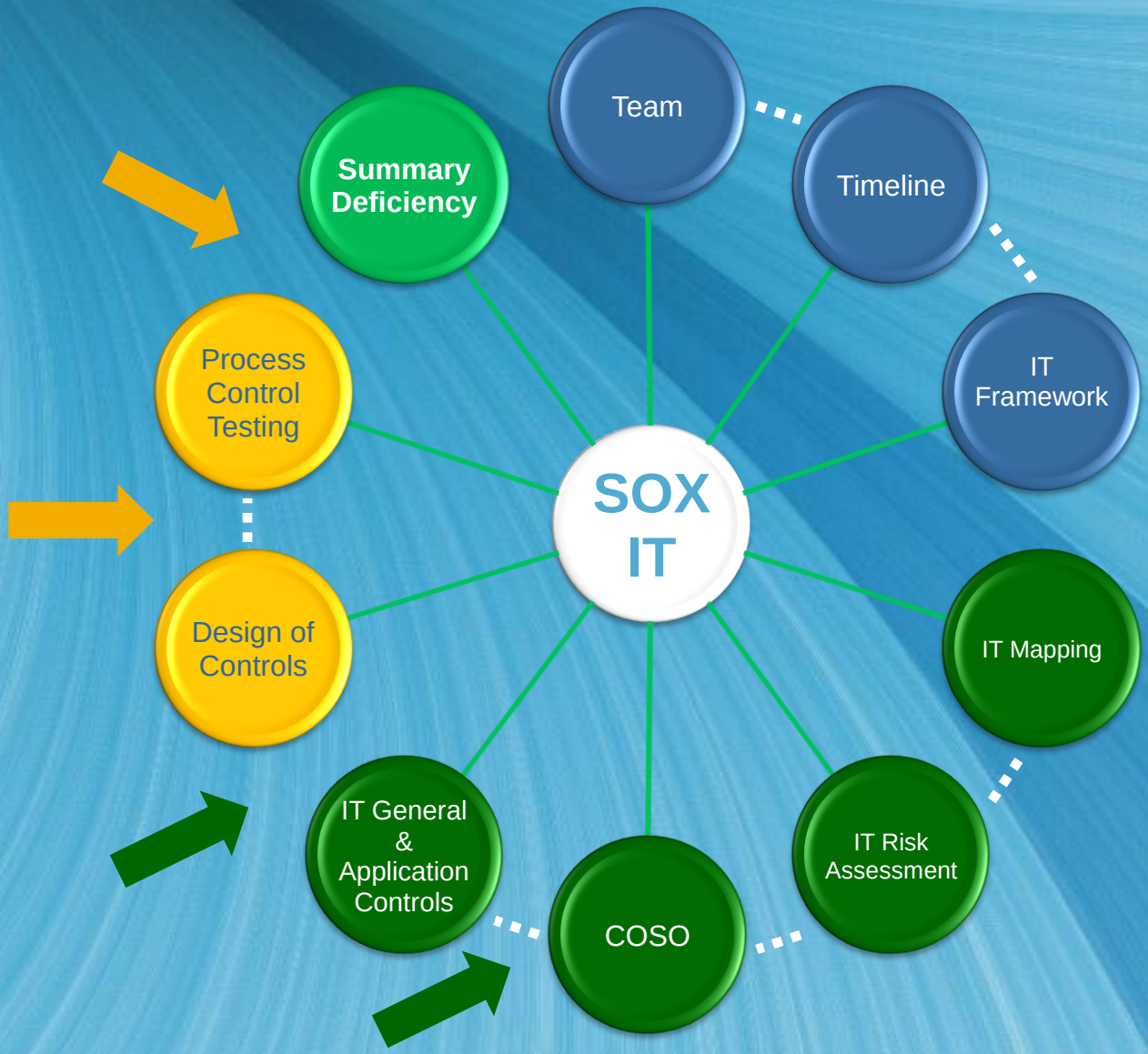
Lord & Benoit's IT Assessment



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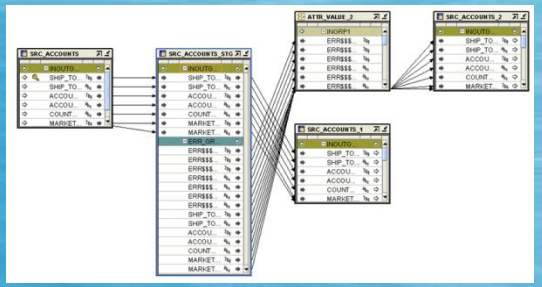
IT Mapping



Business Process and Sub-Process	Overall Rating	Application Name	Database	Operating System	Critical Spreadsheet Name	Supported by a Third Party	Hosted by a Third Party Provider
Cash Management	H	MS Dynamics	MS SQL	Windows 2008	N/A	Yes	Yes
Investment Securities							
Order Processing							
Credit and Collections							
Revenue Recognition							
Purchasing to Payables							
A/P and Cash Disbursements							
Employee Master File Maintenance							
Process Payroll							

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IT Risk Assessment

- Identify and focus on critical information assets (processes, systems, staff)
- Consider the relationships among critical assets
- Evaluate risks in operational context
- Establish control objectives & key controls to reduce risks to an acceptable level

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Establishing the Control Environment

Ref	XYZ Company Level IT Control Principle ©2008 Lord & Benoit LLC	Summary of Controls		Summary Evidence of Control	Design Effectiveness (Fully met, partially met, not met)
		Entity Wide	Process Level		
IT-3	How does the company ensure that Information Systems and Technology software development properly reflects users' needs?	✓		There is no internal development function; using COTS products to support entire environment.	N/A
IT-4	What is the users' perception of Information Systems and Technology? How does Information Systems and Technology management assess this?	✓		Users generally feel that IT is responsive to their needs. Any major problem is usually brought to the attention of management.	Fully Met
IT-5	What measures for Information Systems and Technology quality exist? How do they compare with the general attitude to quality at the company?	✓		System availability is extremely high. Have strong monitoring functions in place that identify problems quickly in order to be addressed.	Fully Met
IT-6	Are there significant Information Systems and Technology activities outside the Information Systems and Technology function? How much of the systems and technology is owned and maintained by the users?	✓		All IT functions are performed by either IT personnel or their authorized vendors. Users do not manage any part of the infrastructure.	Fully Met

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Virtual SOX IT Narratives/Populating Control Matrix

Process	Control Objective	Rationale/Risk	Key Control	Key Reports	Frequency of Control	Manual/ Automatic	Preventative/ Detective	Control Owner	Evidence of Control	Design Deficiency?
4. Manage Changes	4.1 Controls provide reasonable assurance that system changes of financial reporting significance are authorized and appropriately tested before being moved to production.	Managing changes addresses how an organization modifies system functionality to help the business meet its financial reporting objectives. Deficiencies in this area could significantly impact financial reporting. For instance, changes to the programs that allocate financial data to accounts require appropriate approvals and testing prior to the change to ensure classification and reporting integrity.	4.1 Requests for all changes are subject to the IT Change Control document requirements as incorporated into the HP Openview Service Desk change management module	IT Change Control Document Closed Changes Report IT Change Request ticket	Weekly	Manual and automatic	Preventative	VP of IT	Change tickets in service desk	
			4.2 Change Management procedures ensure that the stability of the production environment is not compromised through the completion of an impact analysis including security impact.	IT Change Request ticket	Weekly	Manual	Preventative	VP of IT	Documented impact analysis in the Change tickets	

Virtual SOX IT Design of Controls/Operational Testing

- Documentation and Evidence collection to support Test Matrix
- Tools/methods include: VPN, remote desktop, video cams, screen capture, conference calls

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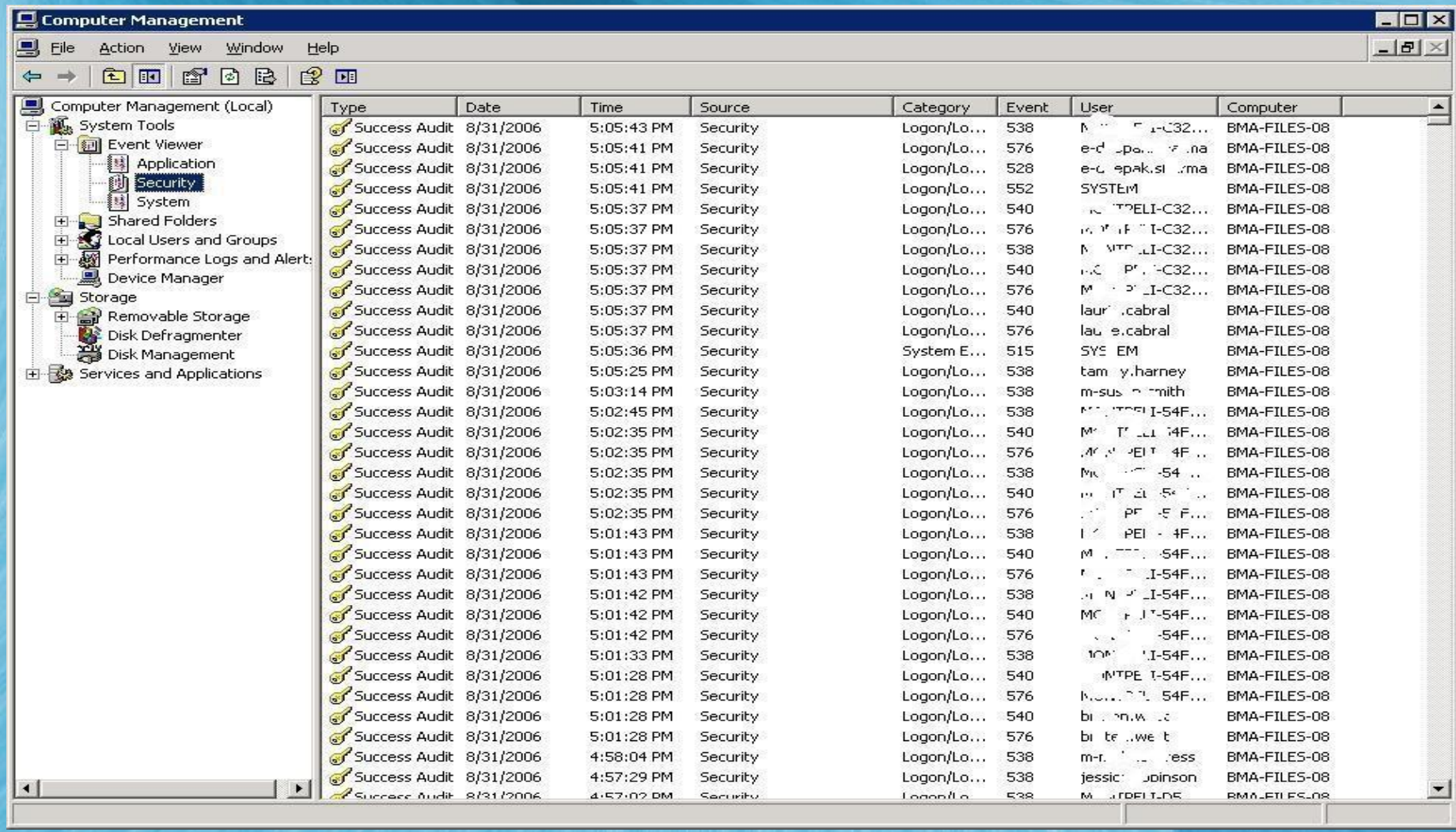
Virtual SOX IT- Backup Log Dump to Spreadsheet

As of 8/22/2006 7:31:33 AM.

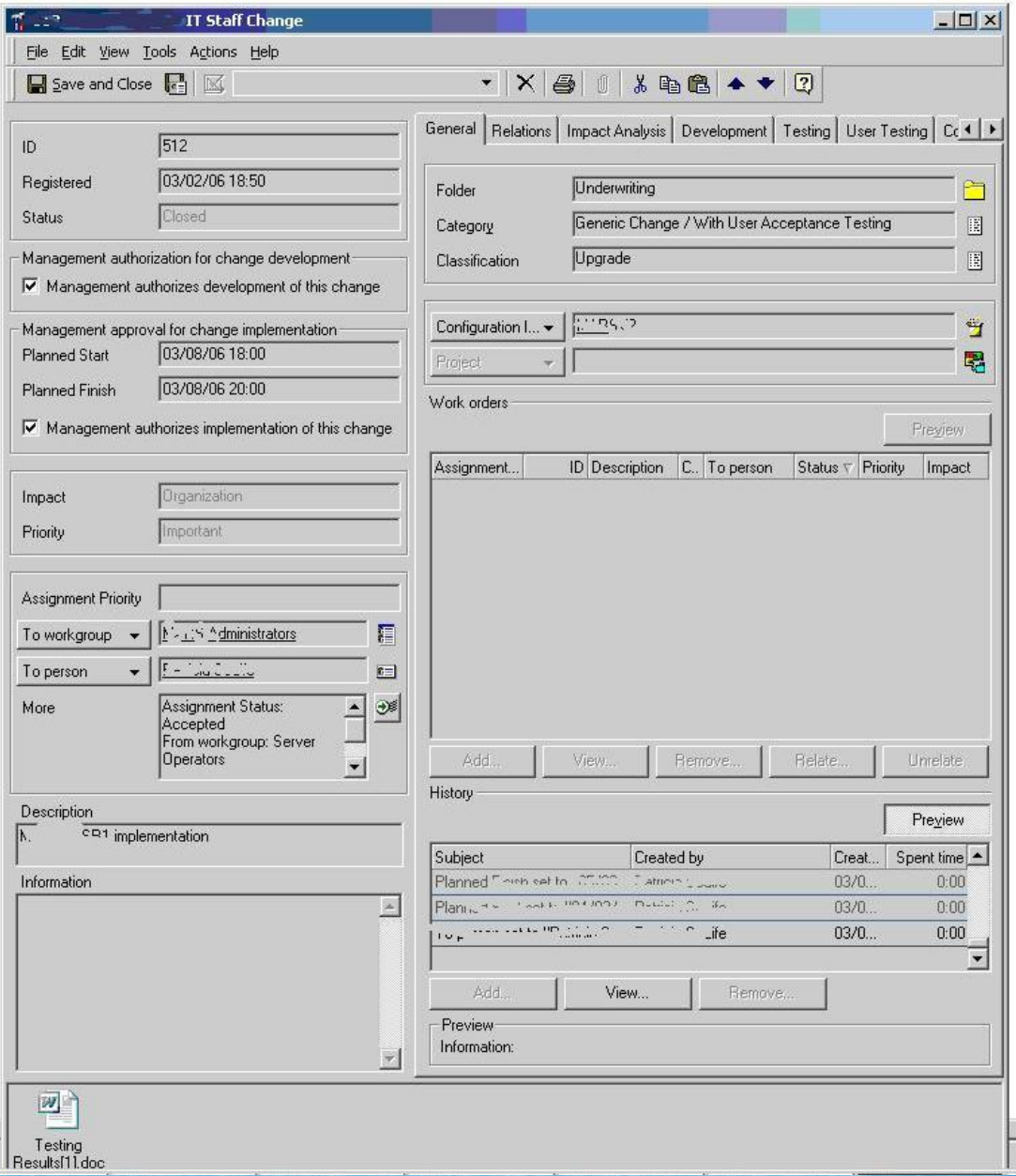
Server Name	Start Time	Backup Size	Status	Last Successful Backup	Backup Server	Incident ID
bma-bb-40	8/22/2006 05:38 AM	5.006	Successful	8/22/2006 05:38 AM	bma-backup-02	
bma-catm-01	8/21/2006 10:17 PM	206.517	Successful	8/21/2006 10:17 PM	bma-backup-03	
bma-catrdr-80	8/22/2006 02:45 AM	96.107	Successful	8/22/2006 02:45 AM	bma-backup-02	
bma-clasic-75	8/21/2006 09:20 PM	106.803	Successful	8/21/2006 09:20 PM	bma-backup-03	
bma-dc-01	8/21/2006 08:34 PM	5.112	Successful	8/21/2006 08:34 PM	bma-backup-03	
bma-dc-02	8/21/2006 08:00 PM	4.985	Successful	8/21/2006 08:00 PM	bma-backup-04	
bma-dc-03	8/21/2006 08:45 PM	5.567	Successful	8/21/2006 08:45 PM	bma-backup-03	
bma-eqe-01	8/22/2006 05:25 AM	14.376	Successful	8/22/2006 05:25 AM	bma-backup-02	
bma-files-04	8/21/2006 08:50 PM	116.934	Successful	8/21/2006 08:50 PM	bma-backup-04	
bma-files-05	8/21/2006 08:00 PM	590.392	Successful	8/21/2006 08:00 PM	bma-backup-02	
bma-files-08 (RMS Unattached)	8/19/2006 05:00 PM	1,130.315	Successful	8/19/2006 05:00 PM	bma-backup-01	
bma-files-08 modelling	8/22/2006 03:09 AM	729.506	Failed	8/21/2006 02:40 AM	bma-backup-04	-1
bma-goog-01	8/21/2006 09:00 PM	5.020	Successful	8/21/2006 09:00 PM	bma-backup-03	
bma-gp-01	8/22/2006 01:37 AM	10.851	Failed	8/14/2006 01:59 AM	bma-backup-02	4600
bma-mail-02	8/22/2006 01:14 AM	98.763	Successful	8/22/2006 01:14 AM	bma-backup-04	
bma-mitel-01	8/22/2006 02:50 AM	7.427	Successful	8/22/2006 02:50 AM	bma-backup-04	
bma-mon-01	8/22/2006 01:02 AM	9.437	Successful	8/22/2006 01:02 AM	bma-backup-04	
bma-owa-01	8/21/2006 08:15 PM	8.811	Successful	8/21/2006 08:15 PM	bma-backup-04	
bma-rms-52	8/22/2006 06:15 AM	112.703	Successful	8/22/2006 06:15 AM	bma-backup-02	
bma-rms-60	8/21/2006 10:19 PM	131.046	Successful	8/21/2006 10:19 PM	bma-backup-04	
bma-rsg-01	8/22/2006 04:10 AM	27.850	Successful	8/22/2006 04:10 AM	bma-backup-02	
bma-sdesk-01	8/22/2006 12:21 AM	6.860	Successful	8/22/2006 12:21 AM	bma-backup-04	
bma-sox-01	8/21/2006 08:00 PM	4.678	Successful	8/21/2006 08:00 PM	bma-backup-03	
bma-sql-01	8/22/2006 05:08 AM	17.497	Successful	8/22/2006 05:08 AM	bma-backup-02	
bma-ts-01	8/21/2006 08:21 PM	12.188	Successful	8/21/2006 08:21 PM	bma-backup-03	
bma-ts-02	8/20/2006 01:44 AM	414.704	Exceptions	8/12/2006 10:27 PM	bma-backup-01	4599
bma-vault-01	8/22/2006 02:00 AM	5.448	Successful	8/22/2006 02:00 AM	bma-backup-02	
bma-whouse-01	8/22/2006 06:00 AM	5.646	Successful	8/22/2006 06:00 AM	bma-backup-02	
bma-xpose-01	8/22/2006 02:18 AM	40.758	Successful	8/22/2006 02:18 AM	bma-backup-02	

Virtual SOX IT

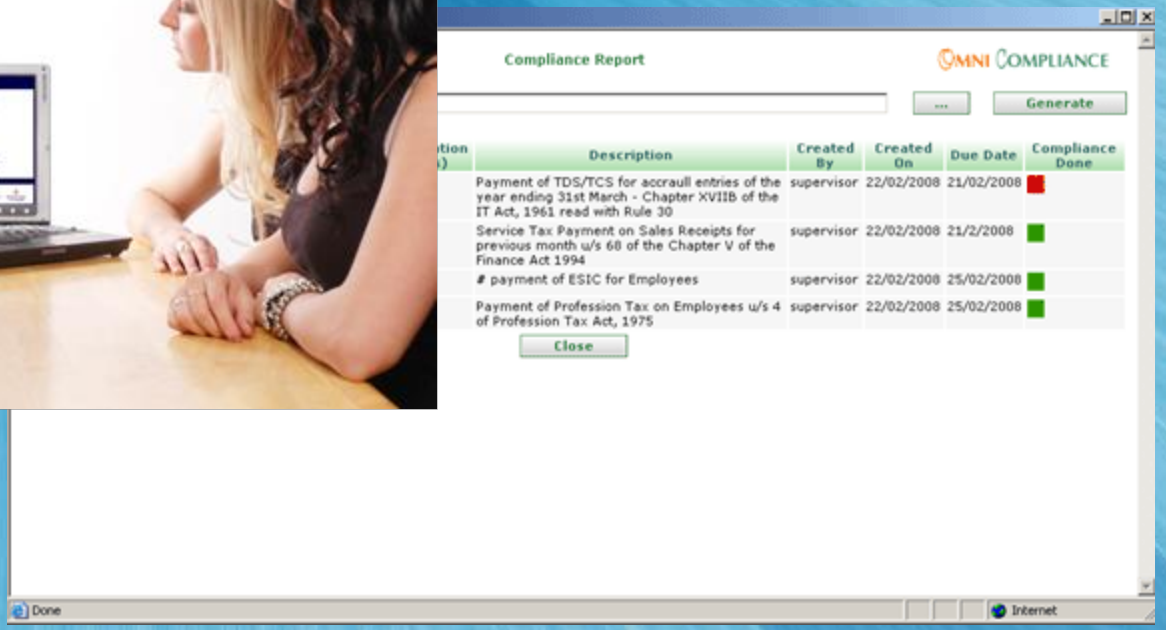
Event Log through Virtual Desktop



Change Management Ticket



IT Summary of Deficiencies



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Virtual SOX IT Security Guidelines

- While there is no defined standard for securing/storing of SOX data, there are multiple privacy data requirements
  - Virtual private networking (VPN)
  - SSL websites with password controls
  - Encrypted e-mail
  - Encrypted server storage
  - Locked/alarmed cabinets

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Virtual SOX IT—Final Thoughts

- Managing/accessing your data is crucial to a successful Virtual SOX IT engagement
- Structured document repositories such as SharePoint allows easy access to management, internal/external auditor at any time
- Data easily accessible for analysis

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Virtual SOX

Questions?

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