



Management Ideas for the Non-Profit Organization

Fall 2004

VOLUME I Issue 1

"We Thought You'd Like to Know™" is an information service of Gene Siciliano, financial consultant and advisor to not-for-profit organizations – Your CFO for Rent®.

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Sarbanes-Oxley and the Non-profit Organization – Is It Time?

The number of articles and pronouncements talking about the applicability of this highly publicized legislation to non-profit agencies is growing. Everybody wants to tell you it applies just as surely to non-profit organizations as it does to the Enrons of the world. But does it? And if it does or doesn't, should you as a director act differently?

When Congress passed the Sarbanes-Oxley Act (SARBOX) in 2002, it was aimed squarely at the corporate bad guys, the executives who put profits for their companies ahead of any thought to stockholder interests or their companies' responsibility to society. It required executives to say publicly whether or not they have a corporate code of ethics. It required them to make statements about their financial reports that should have simply restated the obvious, but apparently didn't. And there were a host of restrictions on their audit firms and new requirements for their boards. It applied to all publicly traded corporations.

But what does that have to do with the non-profit organization (the "NPO"), that clearly American way for people with common interests to help the needy and less

fortunate in the world? At this point, not much. Congress asked the individual states to decide where else it should apply, and so far few have taken the hint.

But things are changing. The state of New York now requires executives of NPOs above a certain size to sign and certify they have reviewed their financial statements. California has a bill in the pipeline that could affect boards of directors in several ways. It would create audit committees separate from finance committees, define their relationship to the auditors, and require that their audited financial statements be available to the public, among other things. Again, for those above a certain size, and again, no guarantee the bill will actually become law.

While it's not clear what the requirements will turn out to be, if any, a number of large non-profits across the country have already begun to implement selected SARBOX guidelines. Their motivation may be avoiding the rush when the requirements are made clearer, but it may also be because the guidelines in SARBOX represent better management, sounder responsibility to constituents, and a clear statement of commitment to the public good by organizations in the public eye. And that's what it's about, after all.

We believe directors of NPOs have a fiduciary responsibility to ensure that proper reporting is followed, and that adequate controls are in place at their agency to protect the resources they are monitoring. Since that is the intent of SARBOX, it makes sense to look at the elements of that legislation that boards should consider, whether required to or not. I suspect the typical NPO director would prefer to be known as the director who did the right thing when it wasn't required, rather than the one who promptly responded to a new law.

So here's some food for thought. What can you glean from Sarbanes-Oxley that might help you improve board oversight effectiveness, reduce your fiduciary risk, and improve the financial management at your agency? Here are my suggestions:

1. SARBOX requires that members of a company's audit committee be independent, that is, not employees or beneficiaries of the organization. For most NPOs this is not a problem, because most directors are volunteers. Independence doesn't imply a lack of passion for the mission, but rather a lack of dependence on the organization for a major part of their income. But today the audit committee to a NPO is likely to be also the Finance Committee, the Budget Committee, or some

similar title. So for the large NPO with senior executives on the board, this can be an issue.

2. The Act also requires that same audit committee to have at least one member who is a financial expert. For NPOs the challenge of having a financial expert on the finance or budget committee is real. The typical non-financial director often has difficulty interpreting the sometimes complex reports of financial affairs, or in asking clearly for the kind of information they need, without having a financial expert to help the analysis and communication process. So SARBOX would say to the nominating committee: "Find one." Better yet, find two, so there can be some continuity on the board for the future.

3. If your NPO's auditor is chosen by the Executive Director or a vote of the full board (endorsing the ED's selection), or if your auditor is the same person you've had in place for 10 or 15 years, consider this: SARBOX says the auditor

will be appointed by the audit committee, their compensation will be negotiated by the audit committee, and the oversight of the auditors' work will be by, yep, the audit committee.

4. There is a long list of services that your accountants cannot provide to the organization they audit, such as bookkeeping, accounting systems design and implementation, internal audit, appraisal or valuation, and a few others less likely to be needed by NPOs. The audit committee thus should be aware of any other use of the auditing firm's services, so they can make sure that nothing can touch on their independence when it comes to the audit.

5. Is your agency's accounting department too light to do a reasonable job? Preliminary results of public company reviews indicate growing examples of firms being told their staffs are inadequate in size or expertise or both to do the job, a potential violation of Section 404 of the Act. Given the too-

frequent state of financial staffs in NPOs, your budget committee might want to keep this in mind the next time resource allocation decisions are made.

So, is it time? As you can see, the board of directors and the audit committee by any name may soon be more directly involved under these guidelines. If that comes to pass, directors who serve on non-profit boards will not be able to take their service as mostly a chance to do some good and develop their business network. Is that a good idea? We think so. Is it required at this point? Nope. Should the board of directors consider some of these changes now, as a message to their sponsors, donors, and contract customers? Absolutely, in our opinion, because it's the right thing to do. We'd be happy to help you identify what makes sense for your organization. Give us a call.

About the Author, Gene Siciliano, CMC CPA

Gene Siciliano is *Your CFO For Rent*[®]. He is also the founder and president of **Western Management Associates**, a business seminar and financial management consulting firm with a specialty in the not-for-profit sector. His firm solves business problems for clients that have manifested in the form of cash flow shortages, falling surplus balances, and declining reserves. He also helps rapidly growing organizations by helping them define goals and execute implementation plans.

He is also the author of the newly published McGraw-Hill book, *Finance for Non-Financial Managers*. His articles on financial management and cost control have appeared internationally in various business publications and his firm's newsletter series "*We Thought You'd Like to Know*"[™].

He is currently Chairman of the Board of The Exceptional Children's Foundation in Culver City. He has served on the boards of several non-profit charitable and professional organizations.

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