CHAPTER 1. TONE AT THE TOP AND CORPORATE GOVERNANCE

Chapter 1, Tone at the Top and Corporate Governance, includes the following best practices to help establish a code of ethics and to develop the foundation for excellent corporate governance:

Chapter 1. Tone at the Top and Corporate Governance
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Implementing Tone at the Top
IMA's Statement of Ethical Professional Practice
MCI's Code of Conduct
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DEFINING TONE AT THE TOP

Tone at the Top is an expression that is used to define management's leadership and commitment to openness, honesty, integrity, and ethical behavior. It establishes the integrity of a company and directs how employees, shareholders, and stakeholders of a company comport themselves.

Behavior at the management level has a trickle-down effect on all employees. If management demonstrates honesty, integrity, and ethics, it sets a cultural climate that encourages employees to behave in the same way.

Employees are keenly aware of the practices and rules followed by senior management and owners. Insider or related-party dealings, circumvention of internal controls, and favorable key-employee treatment are just three examples of management looking out for management, often at the expense of the stakeholders and employees of an organization.

The Institute of Business Ethics states that organizations often have a set of ethical and operational values that they aspire to uphold in carrying out their business. These values guide acceptable, desirable, and responsible behavior—above and beyond compliance with laws and regulations. To support ethical values, the organization should have an ethics policy that:

1. Communicates an organization's ethical values, standards, and commitments to stakeholders that will underpin the way that it does business;
2. Confirms leadership commitment to the above;
3. Describes how this will be achieved and monitored through an ethics program;
4. Identifies the main ethical issues faced by the organization; and
5. Identifies other policies and documents that support and detail aspects of the ethics policy—such as a code of ethics, a speak-up policy, a bullying and harassment policy, a gifts and hospitality policy, and an environmental policy.

Tone at the top must be constantly communicated and enforced so that there is a clear understanding of the company's emphasis on ethical behavior. Employees must understand the consequences if there is a violation of the tone at the top. Integrating the tone at the top within the corporate governance structure is considered a requirement for public companies and is looked upon as a best practice for private companies.

IMPLEMENTING TONE AT THE TOP

As a best practice, companies and organizations of all sizes should implement a code of conduct to support their tone at the top message.

Any organization that fails to abide by a moral code risks losing its reputation in the marketplace and the loyalty of its customers, suppliers, employees, and other stakeholders. Violations can result in a significant loss of revenue—or even lead to bankruptcy. So it behooves both public and private companies to adopt strong internal controls to ensure ethical conduct.

In the public arena, financial gains can begin to create a haze over core values among some corporate leaders. The famous fall of Enron is a prime example of how executive management at a public company violated a company's code of ethics.

Improper behavior such as this by senior management led to changes in legislation pertaining to the roles and responsibilities of accounting and finance leadership. The violation of accounting standards drove the Securities and Exchange Commission (SEC) to closely look at the segregation of duties and the values of management running public companies.

The SEC made significant disclosure requirements regarding the tone at the top. Disclosure now requires clear articulation of the fundamental values the entity follows, including how executive management is measured and compensated.

While public companies are required to have a code of ethics (Section 406 of Sarbanes-Oxley requires public companies to disclose their code of ethics and to disclose whether any violations have occurred against the code), private companies would be wise to also establish such a code.

A code of ethics is a written document that a company adopts that is based primarily on the values of honesty and integrity. To create a code of ethics, take the following steps:[1]

- Define the organization's most important guiding values;
- Formulate behavioral standards to illustrate the application of those values to the roles and responsibilities of the persons affected;
- Review the existing procedures for guidance and direction as to how those values and standards are typically applied; and
- Establish the systems and processes to ensure that the code is implemented and effective.

A well-developed code of ethics is established in a series of discussion sessions by the board of directors, senior management, and finance leadership. Debate takes place and decisions are vetted to determine the core values, roles and responsibilities, expectations, and behavioral standards. A typical code of ethics consists of the following five categories:

1. An introduction section;
2. A statement of core values and principles;
3. Examples of noncompliant behavior;
4. A discussion of the company's support system; and
5. A statement regarding personal responsibility.

Another strategy for developing a code of conduct is presented by The Institute of Business Ethics. It suggests that a code of conduct include a discussion of the expectations within each of the following components:

1. How we compete;
2. Bribery and facilitation payments;
3. Gifts and entertainment;
4. Conflicts of interest;
5. Use of company assets;
6. Safeguarding important information;
7. Political involvement and contributions;
8. The application of human rights standards in our business;
9. Our environmental responsibilities;
10. Timely payments of suppliers; and
11. Other issues

MCI'S CODE OF CONDUCT

One compelling example of a code of conduct was implemented at MCI (formally WorldCom). MCI faced a tremendous challenge in recovering from the massive fraud that occurred in 2002. The company's reputation was significantly damaged and the company's employees had to adopt a new code of conduct in order for the company to recover.

Much of the content of MCI's code of conduct was taken from the code that Michael Capellas developed when he was CEO at Compaq Computer Corporation (acquired by Hewlett Packard). When Capellas became CEO at MCI, he knew one of his most important actions was to establish a foundation of ethics and integrity at the company.

He hired an ethics officer from Boeing and started a company-wide campaign to communicate the company's tone at the top. Employees attended Web-based quarterly training sessions and were tested at the end of every session. Additionally, employees were often asked to recite all 10 components of the company's code of conduct by Capellas when he approached them:

1. Do what you say and say what you do.
2. Treat each other with dignity and integrity.
3. Everyone should be comfortable to speak his or her own mind.
4. Management leads by example.
5. Follow company policy and regulatory requirements.
6. Avoid conflicts of interest.
7. Establish metrics and report results accurately.
8. Focus on what is important and not what is convenient.
9. Be loyal to your families, your company, and yourselves.
10. Do the right thing because it's the right thing to do.

FOSTERING AN ETHICAL CLIMATE

Whatever tone management sets will have a trickle-down effect on employees of the company. If the tone set by the managers upholds ethics and integrity, employees will be more inclined to uphold those same values, explains the Association of Certified Fraud Examiners (ACFE).

"If upper management appears unconcerned with ethics and focuses solely on the bottom line, employees will be more prone to commit fraud because they feel that ethical conduct is not a focus or priority within the organization," says the ACFE. "Employees pay close attention to the behavior and actions of their bosses, and they follow their lead."

According to a study by The National Commission on Fraudulent Reporting (called the Treadway Commission), senior managers need to practice these steps:

1. Communicate to employees what is expected of them;
2. Lead by example;
3. Provide a safe mechanism for reporting violations; and
4. Reward integrity.

The Institute of Business Ethics maintains that in order to support ethical values, an organization should have an ethics policy that does the following:

1. Communicates an organization's ethical values, standards, and commitments to stakeholders that will underpin the way that it does business;
2. Confirms leadership's commitment to these ethical values; and
3. Describes how this will be achieved and monitored through an ethics program.

Sources: Association of Certified Fraud Examiners, http://www.acfe.com/; The Institute of Business Ethics, www.ibe.org.uk.

PROMOTING TRUST

Trust is crucial for a company's financial success, and controllers are in an ideal position to be "trust champions" at their organizations. The job involves safeguarding assets, processing transactions, producing investor and regulatory reports with accuracy and integrity, and protecting the rights of investors and other organizational stakeholders.

As the chief accounting officer, the controller has a leadership role in determining the organization's fair and honest application of accounting principles in public reporting, while also assuring that decision-support information is complete and unbiased.

Here are four ways that controllers can become champions of trust and ethics at their organizations:

1. Participate in developing a code of conduct that reflects the strong ethical values the organization believes in, and then make sure that every decision you are involved in follows those principles.
2. Set the correct tone throughout the organization.
3. Have candid conversations, and plenty of them, with people at all levels of an organization in order to make trust, ethics, and values a tangible practice, rather than an intangible principle.
4. Build core values into the performance management process that promote trustworthy and ethical behavior.

When you build a set of core values into your organization's performance appraisal process, you make values and the ethics policy very real on a day-to-day basis, and you go well beyond an annual compliance or attestation exercise.

Trustworthy behavior leads to a positive reputation with credit rating agencies and bankers. In addition, your organization will attract superior employees, see lower turnover rates, and experience higher productivity.

It cannot be stressed enough: ethics and trust are foundational elements for success. They are not conditional on business outcomes, including financial performance.[2]

CREATING POLICIES AND PROCEDURES FOR YOUR CODE OF CONDUCT

When you establish (and continually review) a code of conduct, ethics policy, or statement of business principles, you identify and document exactly what behaviors are acceptable within an organization.

For example, implementing human resource (HR) policies related to hiring, training, and promoting staff could potentially keep unethical individuals from joining an organization or obtaining a position of trust.

Institute Effective HR Policies

1. Conduct pre-employment background checks of education, employment history, and personal references.
2. Present periodic training about the organization's core values on topics such as:
   - What constitutes unethical behavior;
   - The employee's responsibility to report unethical behavior; and
   - How to report unethical behavior.
3. Ensure that performance reviews include discussions of an employee's contribution toward creating the appropriate workplace environment.
4. Perform continuous evaluation of compliance with the organization's values.
5. Confirm that the employee understands the organization's expectations and is willing to comply with the organization's code of conduct.

React to Unethical Behavior

While policies and procedures are proactive in nature, organizations also need to focus on reactive measures to unethical behavior. The way an organization responds to incidents or suspected incidents may help to reduce future occurrences. In addition, it's important to foster an environment where individuals are comfortable voicing their concerns.

To send the right message when an event is detected, an organization should:

1. Conduct a thorough investigation;
2. Consistently take action against violators;
3. Assess related controls and functional areas and recommend improvements; and
4. Clearly communicate the organization's values and the consequences of violations.

Resolution of Ethical Conflict

In applying policies and procedures, you may encounter problems identifying unethical behavior or resolving an ethical conflict. When faced with ethical issues, follow your organization's established policies on the resolution of such conflict. If these policies do not resolve the ethical conflict, consider the following courses of action outlined in IMA's Statement of Ethical Professional Practice:

1. Discuss the issue with your immediate supervisor except when it appears that the supervisor is involved. In that case, present the issue to the next level. If you cannot achieve a satisfactory resolution, submit the issue to the next management level. If your immediate superior is the chief executive officer or equivalent, the acceptable reviewing authority may be a group such as the audit committee, executive committee, board of directors, board of trustees, or owners. Contact with levels above the immediate superior should be initiated only with your superior's knowledge, assuming he or she is not involved. Communication of such problems to authorities or individuals not employed or engaged by the organization is not considered appropriate, unless you believe there is a clear violation of the law.
2. Clarify relevant ethical issues by initiating a confidential discussion with an IMA Ethics Counselor or other impartial advisor to obtain a better understanding of possible courses of action. IMA offers an Ethics Helpline service at 800-245-1383 to members of IMA and other professionals. The Helpline offers free, confidential guidance on ethical issues.

After a preliminary discussion of the problem to determine the kind of ethics matter being reported, an ethics counselor will respond to the caller. Confidentiality is maintained at all times. The counselor will not provide a specific resolution but will explain how the dilemma relates to the provisions of IMA's Statement of Ethical Professional Practice.

3. Consult your own attorney as to legal obligations and rights concerning the ethical conflict.

Provide Ethics Training

Ethics training should include case studies and role-playing to ensure that the participants understand the company's requirements. At many companies, this training is often the responsibility of an ethics or compliance officer. The training should be provided quarterly if possible, and at least annually.

Ethics training is intended to be a preventative control. However, many companies have beefed up their training efforts only after a significant event has occurred. They often refer to the significant event during the training if possible. The list below provides some suggestions to enhance ethics training:

- Ethics programs should target required behaviors.
- Such programs should include a process for asking questions and getting management action to correct possible weaknesses in procedures.
- Training participants must perform the specified behavior by responding to case studies or role-playing.
- Programs should include examples of how people, who are similar to the participants, demonstrate the behavior.
- Training instructors should review and positively reinforce behaviors learned by participants.
- Training program participants should experience and learn to cope with the stresses associated with unethical behavior by assessing their own emotional and physical states.
- The general principles in codes of conduct should be an integral part of the strategic planning process.

Make an Ethics Hotline Available to Prevent and Detect Violations

Employee tips are the most common way that unethical behavior and fraud is detected, according to the Association of Certified Fraud Examiners (ACFE). Under current U.S. Sentencing Guidelines, a corporation convicted of a federal offense may seek leniency if it has maintained an effective program to prevent and detect violations of the criminal laws (see "An Overview of the Organizational Guidelines," Paula Desio, Deputy General Counsel, United States Sentencing Commission, at http://www.ussc.gov/sites/default/files/pdf/training/organizational-guidelines/ORGOVERVIEW.pdf).

To take advantage of this provision, the company must prove that it has the following requirements in place:

- High-level personnel overseeing the program;
- Procedures likely to reduce the prospect of criminal activity;
- Employees with a propensity to commit crimes not given discretionary authority;
- Effective communications and training regarding the program;
- A system allowing employees to report misconduct without fear of retribution; and
- Adequate methods for responding to crimes that have been detected.

Note: If your organization does not offer a helpline, you may access IMA's helpline at no cost. To access the IMA Helpline, call: (800) 245-1383. Individuals outside of the U.S. and Canada may have to dial a toll-free access code first before dialing the ethics hotline. For your free access code, go to the AT&T Website at<http://www.usa.att.com/traveler/index.jsp>, select your country from the drop-down menu in the box for AT&T USADirect traveler support, and dial the numbers provided before you dial the ethics hotline number.

TIPS FOR IMPLEMENTING AND MANAGING AN ETHICS HOTLINE

Some key factors to consider when establishing an ethics hotline are:

1. Setting up an easily accessible channel with a toll-free number;
2. Testing the hotline to make sure that it is working;
3. Validating wait times;
4. Providing other options for employees to use to report an issue, such as e-mail and postal mail;
5. Publicizing the hotline with posters, Intranet notices, and employee fraud awareness training (publicizing the hotline is required by the U.S. Sentencing Guidelines);
6. Promoting the culture of the company;
7. Determining whether the hotline should be managed within the company or by a third party;
8. Training the hotline staff with specific scripts to assure employees that there will be no retaliation;
9. Communicating to employees that all communications will be kept in the utmost of confidence and that a proper investigation will take place;
10. Establishing procedures for escalating and reporting issues to your audit committee and disclosure committee;
11. Ensuring that there is a reporting process in place where different types of issues may be reported, such as employee issues and misconduct, violation of accounting policy and practice, supplier contracts, transaction processing issues, and evidence of fraud or collusion; and
12. Testing the ethics hotline and process on an annual basis as part of the entity-level controls program.

CORPORATE GOVERNANCE FOR SMALL BUSINESS

We have seen what can go wrong with large corporations as evidenced by the companies that were the catalysts for the Sarbanes-Oxley Act of 2002.

The report, *Corporate Governance for Small Business*, compiled by 4imprint—a company that provides in-depth, how-to articles based on research conducted by professionals and published experts who are familiar with industry trends—points out that small enterprises should start integrating corporate governance practices to best support their investors or multiple business partners.

Here's what 4imprint has to say:

> Talk of corporate governance is not exactly common in the small business setting. After all, the term "corporate governance" refers specifically to large, publicly owned and traded companies—companies that are required by law to manage and disclose how board members and executives

make decisions.

> While most small businesses typically don't have a board of directors, they do have investors or multiple business partners with a substantial interest in the success and growth of the company. In this sense, talk of corporate governance in the small business setting makes sense. Following the best practices that many large businesses have established through corporate governance, small businesses and start-ups can set out on the path to streamlined and accountable operations.

The 4imprint report makes the following points:

1. **Ethical operations aren't just for the *Fortune* 500.** The core of corporate governance is ethics. Consumers take a company's ethical reputation into consideration when purchasing products or services.
2. **Small companies can turn into large companies.** Small businesses that follow corporate governance policies and procedures will be in a better position legally and culturally to move from a private to public status.
3. **Policies and procedures attract and retain staff.** Corporate governance practices often establish better criteria for evaluating performance and a better system of compensation that can attract and retain quality employees. Also, ethical practices reduce the internal conflicts of interest that result in decreased morale and trust in leadership.
4. **It's always a good idea to protect your investment.** For companies that wish to remain private, having sound procedures in place can serve to attract new investors or partners.

EXAMPLES OF COMPANY CODES OF ETHICS

Coca-Cola's Code of Ethics

Coca-Cola provides a notable example of a company's code of ethics. The company's document covers a wide range of categories under the following headings:

- Acting With Integrity Around the Globe;
- Integrity in the Company;
- Conflicts of Interest; and
- Integrity in Dealing With Others.

A message from Coca-Cola's Chairman and CEO, Muhtar Kent, in the front pages of the ethics document states:

> Our business is built on this trust and this reputation. It influences how consumers feel about our products, and how shareowners perceive us as an investment. We have seen plenty of examples in recent years of powerful companies with once stalwart reputations tarnished forever by unethical actions of a few people or even just one person.
>
> As former Company Board member Warren Buffett once reminded us, "It takes years to build a reputation and only a few seconds to ruin it." Because our success is so closely related to our reputation, it's up to all of us to protect that reputation.
>
> Acting with integrity is about more than our Company's image and reputation, or avoiding legal issues. It's about sustaining a place where we all are proud to work.

Ultimately, it's about each of us knowing that we have done the right thing. This means acting honestly and treating each other and our customers, partners, suppliers, and consumers fairly, and with dignity.

The Code of Business Conduct is our guide to appropriate conduct. Together with other Company guidelines, such as our Workplace Rights Policy, we have set standards to ensure that we all do the right thing. Keep the Code with you and refer to it often. Stay current with your ethics training. When you have questions, ask for guidance.

With your help, I am confident that our company will continue to deserve the trust that everyone has in us. Our reputation for integrity will endure. Thank you for joining me in this effort.

Source: www.coca-colacompany.com

Verizon

The Verizon code of ethics is a lengthy document that contains four short core values, followed by 16 pages of specific rules and guidelines to follow in certain situations. The core values are: 1) integrity, 2) respect, 3) performance excellence, and 4) accountability.

The specific guidelines cover situations, such as how to deal with workplace violence, alcohol use, and harassment. The guidelines also cover areas of integrity and fairness, such as how to avoid conflicts of interest and how to safeguard company information.

There is also a section on protecting Verizon's company assets, including what to do in cases of sabotage and how to create accurate records.

Source: http://www.verizonbusiness.com/us/about/conduct/coc.pdf

Colgate-Palmolive

The Colgate-Palmolive code of ethics is a comprehensive document that is broken down into individual areas of conduct. The code is intended as a guide to all daily business interactions and is used in conjunction with the company's business practice guidelines.

The code covers 10 areas, including: Our Relationship with Each Other; Our Relationship with the Company; Our Relationship with Consumers; Our Relationship with Government and the Law; Our Relationship with Society; and Our Relationship with the Environment.

Source: http://www.colgate.com/app/Colgate/US/Corp/LivingOurValues/CodeOfConduct.cvsp

Baylor College of Medicine

The Baylor College of Medicine, in Houston, Texas has a short code of ethics that sets out basic rules and refers employees to other guidelines for more detail. For example, the code instructs all employees to follow Baylor's Mission Statement, Compliance Program, and Conflict of Interest policy. The code includes basic guidelines for how employees should handle business conduct, financial and medical records, confidentiality, Baylor property, the workplace environment, and contact with the government.

Source: https://www.bcm.edu/about-us/compliance

SAMPLE TEMPLATE FOR COMPANY CODE OF ETHICS

Template:

Code of Ethics and Business Conduct

Practice Note:

If employers have separate confidentiality, nonsolicitation, use of company property and/or conflict of interest policies or similar clauses contained in employee agreements, they should ensure that the language in all communications is consistent.

Statement of Our Core Values

Company Vision

[Insert Company Vision Statement]

Principles

[Insert Company Principles]

Values

[Insert Company Values Statement]

Mission

[Insert Company Mission Statement]

Building Trust and Credibility

Sample wording: The success of our business is dependent on the trust and confidence we earn from our employees, customers and shareholders. We gain credibility by adhering to our commitments, displaying honesty and integrity, and reaching company goals solely through honorable conduct. It is easy to say what we must do, but the proof is in our actions. Ultimately, we will be judged on what we do.

When considering any action, it is wise to ask: Will this build trust and credibility for [Company Name]? Will it help create a working environment in which [Company Name] can succeed over the long term? Is the commitment I am making one I can follow through with? The only way we will maximize trust and credibility is by answering "yes" to those questions and working every day to build our trust and credibility.

Respect for the Individual

Sample wording: We all deserve to work in an environment where we are treated with dignity and respect. [Company Name] is committed to creating such an environment because it brings out the full potential in each of us, which, in turn, contributes directly to our business success. We cannot afford to let anyone's talents go to waste.

[Company Name] is an equal employment/affirmative action employer and is committed to providing a workplace that is free of discrimination of all types and from abusive, offensive or harassing behavior. Any employee who feels harassed or discriminated against should report the incident to his or her manager or to human resources.

Create a Culture of Open and Honest Communication

At [Company Name] everyone should feel comfortable to speak his or her mind, particularly with respect to ethics concerns. Managers have a responsibility to create an open and supportive environment where employees feel comfortable raising such questions. We all benefit tremendously when employees exercise their power to prevent mistakes or wrongdoing by asking the right questions at the right times.

[Company Name] will investigate all reported instances of questionable or unethical behavior. In every instance where improper behavior is found to have occurred, the company will take appropriate action. We will not tolerate retaliation against employees who raise genuine ethics concerns in good faith.

For your information, [Company Name]'s whistleblower policy is as follows:

[Note to employer: This policy should have already been adopted as an addendum to the organization's handbook.]

Employees are encouraged, in the first instance, to address such issues with their managers or the HR manager, as most problems can be resolved swiftly. If for any reason that is not possible or if an employee is not comfortable raising the issue with his or her manager or HR, [Company Name]'s [Title of Executive Officer] does operate with an open-door policy.

The Tone at the Top

(Sample wording) Management has the added responsibility for demonstrating, through their actions, the importance of this Code. In any business, ethical behavior does not simply happen; it is the product of clear and direct communication of behavioral expectations, modeled from the top and demonstrated by example. Again, ultimately, our actions are what matters.

To make our Code work, managers must be responsible for promptly addressing ethical questions or concerns raised by employees and for taking the appropriate steps to deal with such issues. Managers should not consider employees' ethics concerns as threats or challenges to their authority, but rather as another encouraged form of business communication. At [Company Name], we want the ethics dialogue to become a natural part of daily work.

Uphold the Law

[Company Name]'s commitment to integrity begins with complying with laws, rules, and regulations where we do business. Further, each of us must have an understanding of the company policies, laws, rules, and regulations that apply to our specific roles. If we are unsure of whether a contemplated action is permitted by law or [Company Name] policy, we should seek advice from the resource expert. We are responsible for preventing violations of law and for speaking up if we see possible violations.

Because of the nature of our business, some legal requirements warrant specific mention here. [Note to employer: Insert any applicable industry-specific laws here].

Competition

(Sample wording) We are dedicated to ethical, fair and vigorous competition. We will sell [Company Name] products and services based on their merit, superior quality, functionality, and competitive pricing. We will make independent pricing and marketing decisions and will not improperly cooperate, or coordinate our activities with, our competitors. We will not offer or solicit improper payments or gratuities in connection with the purchase of goods or services for [Company Name] or the sales of its products or services, nor will we engage or assist in unlawful boycotts of particular customers.

Proprietary Information

It is important that we respect the property rights of others. We will not acquire or seek to acquire by improper means a competitor's trade secrets or other proprietary or confidential information. We will not engage in unauthorized use, copying, distribution, or alteration of software or other intellectual property.

Selective Disclosure

(Sample wording) We will not selectively disclose (whether in one-on-one or small discussions, meetings, presentations, proposals, or otherwise) any material nonpublic information with respect to [Company Name], its securities, business operations, plans, financial condition, results of operations, or any development plan. We should be particularly vigilant when making presentations or proposals to customers to ensure that our presentations do not contain material nonpublic information.

Health and Safety

[Company Name] is dedicated to maintaining a healthy environment. A safety manual has been designed to educate you on safety in the workplace. If you do not have a copy of this manual, please see your HR department.

Avoiding Conflicts of Interest

(Sample wording) We must avoid any relationship or activity that might impair, or even appear to impair, our ability to make objective and fair decisions when performing our jobs. At times, we may be faced with situations where the business actions we take on behalf of [Company Name] may conflict with our own personal or family interests. We owe a duty to [Company Name] to advance its legitimate interests when the opportunity to do so arises. We must never use [Company Name] property or information for personal gain or personally take for ourselves any opportunity that is discovered through our position with [Company Name].

Here are some other ways in which conflicts of interest could arise:

1. Being employed (you or a close family member) by, or acting as a consultant to, a competitor or potential competitor, supplier, or contractor, regardless of the nature of the employment, while you are employed with [Company Name].
2. Hiring or supervising family members or closely related persons.
3. Serving as a board member for an outside commercial company or organization.
4. Owning or having a substantial interest in a competitor, supplier, or contractor.
5. Having a personal interest, financial interest or potential gain in any [Company Name] transaction.
6. Placing company business with a firm owned or controlled by a [Company Name] employee or his or her family.
7. Accepting gifts, discounts, favors, or services from a customer/potential customer, competitor, or supplier, unless equally available to all [Company Name] employees.

Determining whether a conflict of interest exists is not always easy to do. Employees with a conflict of interest question should seek advice from management. Before engaging in any activity, transaction, or relationship that might give rise to a conflict of interest, employees must seek review from their managers or the HR department.

Gifts, Gratuities, and Business Courtesies

[Company Name] is committed to competing solely on the merit of our products and services. We should avoid any actions that create a perception that favorable treatment of outside entities by [Company Name] was sought, received, or given in exchange for personal business courtesies. Business courtesies include gifts, gratuities, meals, refreshments, entertainment, or other benefits from persons or companies with whom [Company Name] does or may do business. We will neither give nor accept business courtesies that constitute, or could reasonably be perceived to constitute, unfair business inducements that would violate law, regulation, or polices of [Company Name] or customers, or would cause embarrassment or reflect negatively on [Company Name]'s reputation.

Accepting Business Courtesies

Most business courtesies offered to us in the course of our employment are offered because of our positions at [Company Name]. We should not feel any entitlement to accept and keep a business courtesy. Although we may not use our position at [Company Name] to obtain business courtesies, and we must never ask for them, we may accept unsolicited business courtesies that promote successful working relationships and good will with the firms that [Company Name] maintains, or may establish, a business relationship with.

Employees who award contracts or who can influence the allocation of business, who create specifications that result in the placement of business, or who participate in negotiation of contracts must be particularly careful to avoid actions that create the appearance of favoritism or that may adversely affect the company's reputation for impartiality and fair dealing. The prudent course is to refuse a courtesy from a supplier when [Company Name] is involved in choosing or reconfirming a supplier, or under circumstances that would create an impression that offering courtesies is the way to obtain [Company Name] business.

Meals, Refreshments, and Entertainment

We may accept occasional meals, refreshments, entertainment, and similar business courtesies that are shared with the person who has offered to pay for the meal or entertainment, provided that:

1. They are not inappropriately lavish or excessive.
2. The courtesies are not frequent and do not reflect a pattern of frequent acceptance of courtesies from the same person or entity.
3. The courtesy does not create the appearance of an attempt to influence business decisions, such as accepting courtesies or entertainment from a supplier whose contract is expiring in the near future.
4. The employee accepting the business courtesy would not feel uncomfortable discussing the courtesy with his or her manager or co-worker or having the courtesies known by the public.

Gifts

Employees may accept unsolicited gifts, other than money, that conform to the reasonable ethical practices of the marketplace, including:

1. Flowers, fruit baskets, and other modest presents that commemorate a special occasion.
2. Gifts of nominal value, such as calendars, pens, mugs, caps, and t-shirts (or other novelty, advertising or promotional items).

Generally, employees may not accept compensation, honoraria, or money of any amount from entities with whom [Company Name] does or may do business. Tangible gifts (including tickets to a sporting or entertainment event) that have a market value greater than $100 may not be accepted unless approval is obtained from management.

Employees with questions about accepting business courtesies should talk to their managers or the HR department.

Offering Business Courtesies

Any employee who offers a business courtesy must assure that it cannot reasonably be interpreted as an attempt to gain an unfair business advantage or otherwise reflect negatively upon [Company Name]. An employee may never use personal funds or resources to do something that cannot be done with [Company Name] resources. Accounting for business courtesies must be done in accordance with approved company procedures.

Other than to our government customers, for whom special rules apply, we may provide non-monetary gifts (i.e., company logo apparel or similar promotional items) to our customers. Further, management may approve other courtesies, including meals, refreshments, or entertainment of reasonable value, provided that:

1. The practice does not violate any law or regulation or the standards of conduct of the recipient's organization.
2. The business courtesy is consistent with industry practice, is infrequent in nature, and is not lavish.
3. The business courtesy is properly reflected on the books and records of [Company Name].

Accurate Public Disclosures

We will make certain that all disclosures made in financial reports and public documents are full, fair, accurate, timely, and understandable. This obligation applies to all employees, including all financial executives, with any responsibility for the preparation for such reports, including drafting, reviewing, and signing or certifying the information contained therein. No business goal of any kind is ever an excuse for misrepresenting facts or falsifying records.

Employees should inform Executive Management and the HR department if they learn that information in any filing or public communication was untrue or misleading at the time it was made or if subsequent information would affect a similar future filing or public communication.

Corporate Recordkeeping

We create, retain, and dispose of our company records as part of our normal course of business in compliance with all [Company Name] policies and guidelines, as well as all regulatory and legal requirements.

All corporate records must be true, accurate, and complete, and company data must be promptly and accurately entered in our books in accordance with [Company Name]'s and other applicable accounting principles.

We must not improperly influence, manipulate, or mislead any unauthorized audit, nor interfere with any auditor engaged to perform an internal independent audit of [Company Name] books, records, processes, or internal controls.

Promote Substance Over Form

At times, we are all faced with decisions we would rather not have to make and issues we would prefer to avoid. Sometimes we hope that if we avoid confronting a problem, it will simply go away.

At [Company Name], we must have the courage to tackle the tough decisions and make difficult choices, secure in the knowledge that [Company Name] is committed to doing the right thing. At times this will mean doing more than simply what the law requires. Merely because we can pursue a course of action does not mean we should do so.

Although [Company Name]'s guiding principles cannot address every issue or provide answers to every dilemma, they can define the spirit in which we intend to do business and should guide us in our daily conduct.

Accountability
Each of us is responsible for knowing and adhering to the values and standards set forth in this Code and for raising questions if we are uncertain about company policy. If we are concerned whether the standards are being met or are aware of violations of the Code, we must contact the HR department.

[Company Name] takes seriously the standards set forth in the Code, and violations are cause for disciplinary action up to and including termination of employment.

Be Loyal

Confidential and Proprietary Information
Integral to [Company Name]'s business success is our protection of confidential company information, as well as nonpublic information entrusted to us by employees, customers, and other business partners. Confidential and proprietary information includes such things as pricing and financial data, customer names/addresses, or nonpublic information about other companies, including current or potential suppliers and vendors. We will not disclose confidential and nonpublic information without a valid business purpose and proper authorization.

Use of Company Resources
Company resources—including time, material, equipment, and information—are provided for company business use. Nonetheless, occasional personal use is permissible as long as it does not affect job performance or cause a disruption to the workplace.

Employees and those who represent [Company Name] are trusted to behave responsibly and use good judgment to conserve company resources. Managers are responsible for the resources assigned to their departments and are empowered to resolve issues concerning their proper use.

Generally, we will not use company equipment such as computers, copiers, and fax machines in the conduct of an outside business or in support of any religious, political, or other outside daily activity, except for company-requested support to nonprofit organizations. We will not solicit contributions nor distribute non-work-related materials during work hours.

In order to protect the interests of the [Company Name] network and our fellow employees, [Company Name] reserves the right to monitor or review all data and information contained on an employee's company-issued computer or electronic device, the use of the Internet, or [Company Name]'s intranet. We will not tolerate the use of company resources to create, access, store, print, solicit, or send any materials that are harassing, threatening, abusive, sexually explicit, or otherwise offensive or inappropriate.

Questions about the proper use of company resources should be directed to your manager.

Media Inquiries
[Company Name] is a high-profile company in our community, and from time to time, employees may be approached by reporters and other members of the media. In order to ensure that we speak

with one voice and provide accurate information about the company, we should direct all media inquiries to the [Public Relations Executive]. No one may issue a press release without first consulting with the [Public Relations Executive].

Do the Right Thing

Several key questions can help identify situations that may be unethical, inappropriate, or illegal. Ask yourself:

1. Does what I am doing comply with the [Company Name] guiding principles, Code of Conduct, and company policies?
2. Have I been asked to misrepresent information or deviate from normal procedure?
3. Would I feel comfortable describing my decision at a staff meeting?
4. How would it look if it made the headlines?
5. Am I being loyal to my family, my company, and myself?
6. What would I tell my child to do?
7. Is this the right thing to do?

Information and Resources

General Manager [or CEO, President, etc.]
[insert name and contact information]

Director of Human Resources
[insert name and contact information]

[Title of Other Contact Person]
[insert name and contact information]

Source: Reprinted with permission from the Society of Human Resource Management (SHRM). See more at: http://www.shrm.org, under TEMPLATES & SAMPLES

UNDERSTANDING THE SARBANES-OXLEY ACT OF 2002 (SOX)

The Sarbanes-Oxley Act (SOX) was signed into law on July 30, 2002 by President George W. Bush who characterized it as "the most far-reaching reforms of American business practices since the time of Franklin Delano Roosevelt." The Act mandated a number of reforms to enhance corporate responsibility, enhance financial disclosures, and combat corporate and accounting fraud. SOX is administered by the Securities and Exchange Commission (SEC).

The Sarbanes-Oxley Act of 2002 has 11 titles that have shaped the way Corporate America approaches corporate governance and internal controls.

Summary of the 11 Titles of SOX

1. Public Company Accounting Oversight Board (PCAOB)

Title I consists of nine sections and establishes the Public Company Accounting Oversight Board to provide independent oversight of public accounting firms providing audit services ("auditors"). It also creates a central oversight board tasked with registering auditors, defining the specific processes and procedures for compliance audits, inspecting and policing conduct and quality control, and enforcing compliance with the specific mandates of SOX.

2. Auditor Independence

Title II consists of nine sections and establishes standards for external auditor independence, to limit conflicts of interest. It also addresses new auditor approval requirements, audit partner rotation, and auditor reporting requirements. It restricts auditing companies from providing nonaudit services (e.g., consulting) for the same clients.

3. Corporate Responsibility

Title III consists of eight sections and mandates that senior executives take individual responsibility for the accuracy and completeness of corporate financial reports. It defines the interaction of external auditors and corporate audit committees, and specifies the responsibility of corporate officers for the accuracy and validity of corporate financial reports. It enumerates specific limits on the behaviors of corporate officers and describes specific forfeitures of benefits and civil penalties for noncompliance. For example, Section 302 requires that the company's principal officers (typically the chief executive officer and chief financial officer) certify and approve the integrity of their company's financial reports quarterly.

4. Enhanced Financial Disclosures

Title IV consists of nine sections. It describes enhanced reporting requirements for financial transactions, including off-balance-sheet transactions, pro-forma figures and stock transactions of corporate officers. It requires internal controls for assuring the accuracy of financial reports and disclosures, and mandates both audits and reports on those controls. It also requires timely reporting of material changes in financial condition and specific enhanced reviews by the SEC or its agents of corporate reports.

5. Analyst Conflicts of Interest

Title V consists of only one section that includes measures designed to help restore investor confidence in the reporting of securities analysts. It defines the codes of conduct for securities analysts and requires disclosure of knowable conflicts of interest.

6. Commission Resources and Authority

Title VI consists of four sections and defines practices to restore investor confidence in securities analysts. It also defines the SEC's authority to censure or bar securities professionals from practice and defines conditions whereby a person can be barred from practicing as a broker, advisor, or dealer.

7. Studies and Reports

Title VII consists of five sections and requires the Comptroller General and the SEC to perform various studies and report their findings. Studies and reports include the effects of consolidation of public accounting firms, the role of credit rating agencies in the operation of securities markets, securities violations and enforcement actions, and whether investment banks assisted Enron, Global Crossing, and others to manipulate earnings and obfuscate true financial conditions.

8. Corporate and Criminal Fraud Accountability

Title VIII consists of seven sections and is also referred to as the "Corporate and Criminal Fraud Accountability Act of 2002." It describes specific criminal penalties for manipulation, destruction or alteration of financial records or other interference with investigations, while providing certain protections for whistleblowers.

9. White Collar Crime Penalty Enhancement

Title IX consists of six sections. This section is also called the "White Collar Crime Penalty Enhancement Act of 2002." This section increases the criminal penalties associated with white-collar crimes and conspiracies. It recommends stronger sentencing guidelines and specifically adds failure to certify corporate financial reports as a criminal offense.

10. Corporate Tax Returns

Title X consists of one section. Section 1001 states that the Chief Executive Officer should sign the company tax return.

11. Corporate Fraud Accountability

Title XI consists of seven sections. Section 1101 recommends a name for this title as "Corporate Fraud Accountability Act of 2002." It identifies corporate fraud and records tampering as criminal offenses and joins those offenses to specific penalties. It also revises sentencing guidelines and strengthens their penalties. This enables the SEC to resort to temporarily freezing transactions or payments that have been deemed "large" or "unusual."

COMBATING CORPORATE AND ACCOUNTING FRAUD

The central theme of Sarbanes-Oxley is financial transparency. Any investor, shareholder, or employee should be able to read the company's financial statement and understand its financial position. Not only is financial transparency required by law, it is good business practice.

Financial transparency goes beyond the numbers. It concerns ethics and accountability, training, and communication.

The most important sections of SOX for corporate controllers are as follows:

Section 302: Corporate Responsibility for Financial Reports. SOX imposes rules for certifying financial reports. In brief, by signing the report, company officers—typically the CEO and CFO—are certifying that they have reviewed the report, the report is factual and complete, financial statements and other related information accurately reflect the company's financial position, and effective internal controls are in place.

Section 401: **Disclosures in Periodic Reports.** Annual and quarterly financial reports must reflect all material correcting adjustments that have been identified by a registered public accounting firm in accordance with Generally Accepted Accounting Principles (GAAP) and SEC rules and regulations. Financial reports also must disclose all off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships with unconsolidated entities or other persons that may have a material current or future effect on the company's financial condition. This section also requires that pro forma financial information included in a financial report or in any public disclosure or news press must be factual and must not omit material facts that could be misleading regarding the company's financial picture.

Section 404: Management Assessment of Internal Controls. Management must produce an internal control report affirming "the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting." The report must also "contain an assessment, as of the end of the most recent fiscal year of the Company, of the effectiveness of the internal control structure and procedures of the issuer for financial reporting."

Section 409: Real Time Issuer Disclosures. Under this section, companies must rapidly disclose changes in their financial condition or operations to the public . These disclosures must be presented in understandable, plain English, and may include trend and qualitative information and graphic presentations as needed.

Section 802: Criminal Penalties for Altering Documents. It is a crime to knowingly alter, destroy, mutilate, conceal, cover up, falsify, or make a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the outcome of an investigation. Penalties include fines and/or imprisonment for up to 20 years.

Section 806: Whistleblower Protection. This section provides protection for employees of publicly traded companies who provide evidence of fraud. An employer covered under SOX may not discharge or in any manner retaliate against an employee because he or she provided information, caused information to be provided, or assisted in an investigation by:

- A federal regulatory or law enforcement agency;
- A member or committee of Congress; or
- An internal investigation by the company relating to alleged mail fraud, wire fraud, bank fraud, securities fraud, violation(s) of SEC rules and regulations, or violation(s) of federal law relating to fraud against shareholders.

In addition, an employer may not discharge or in any manner retaliate against an employee because he or she filed, caused to be filed, participated in or assisted in a proceeding relating to alleged mail fraud, wire fraud, bank fraud, securities fraud, violation(s) of SEC rules and regulations, or violation(s) of federal law relating to fraud against shareholders.

If an employer takes retaliatory action against an employee because he or she engaged in any of these protected activities, the employee can file a complaint with the Occupational Safety and Health Administration (OSHA).

Section 807: Criminal Penalties for Defrauding Shareholders of Publicly Traded Companies. Knowingly committing securities fraud is punishable by a fine and/or imprisonment for up to 25.

Section 902: Attempts and Conspiracies to Commit Fraud Offenses. It is a crime to intentionally alter, destroy, mutilate, or conceal a document in order to prevent it from being used in an official proceeding.

Section 906: Corporate Responsibility for Financial Reports. A company officer who certifies a misleading or fraudulent financial report can be fined up to $5 million and imprisoned for up to 20 years.

TIPS FOR BETTER FINANCIAL REPORTING AND ANALYSIS UNDER SOX

If you are responsible for preparing the management disclosure and analysis (MD&A) section of your company's financial report (as required by Section 302 of SOX), consider these nine tips from Brian Lane, a corporate securities attorney and former director of the SEC Division of Corporation Finance.

This advice can also be helpful to private companies when creating disclosure documents.

1. Use plain English and simple tables. Keep jargon to a minimum. Also, use tables as much as possible to illustrate your points.

2. Make the overview concise and to the point. Your overview should be just that—an overview. Simply touch on the highlights and lowlights. State how the quarter, or year, went. Make it readable, so your directors and investors can skim it and get the salient points.

3. Provide a top-down analysis. Do a segment-by-segment analysis, focusing on the most important items first. Don't bog down your report in minutiae.

4. Review what your competitors and peers are covering in their MD&As. Look at the comments the SEC is making on your peers' and competitors' MD&As. You are going to get the same comments if you do things the same way. If one of your competitors voluntarily includes some information the SEC likes, they're going to ask for the same information from other companies in the industry.

5. Always answer the question, "Why?" in each paragraph. A good MD&A is about stating why you have seen certain business results.

6. Avoid boilerplate language when discussing risk factors. Don't state the same risk factors and explanations from one year to the next. Your information will be more meaningful if you reorder it according to priority.

7. Clearly quantify the effects of multiple risk factors. If you state that your lower sales for the quarter were caused by foreign currencies, product mix, and a down economy, the SEC is going to want to know how much of it was attributable to each of those factors.

8. Combine your year-to-year charts. Don't create a section for 2011 data, and then a section for 2012 data in your 10-Ks and go on for pages and pages. Instead, create a chart that covers two periods at a glance. This will be much more concise and help your reader understand trends.

MAKING GOOD USE OF YOUR DISCLOSURE COMMITTEE

Create a checklist of items for the disclosure committee to review and consider. The list should include the following areas:

- ✓ **Financial covenants.** Include any items that are "about to blow" that could trigger the need for disclosure.
- ✓ **Liquidity and cash reserves.** Cash runway can be the most important number for many companies. If your runway is a little short, you will need to include this on your MD&A.
- ✓ **Changes in legislation and regulation.** These are factors that could impact your business.
- ✓ **Problems with customers or suppliers.** Ask the business people in the room if they're having any problems with vendors or customers. This will make it less likely that you will miss something important and help you create a better MD&A.
- ✓ **Disproportionate dependence by your company on one product or market segment.** Even changes in one product might have to be disclosed if it's your crown jewel.
- ✓ **Any significant swings in results between quarters.** Watch for significant swings in results between quarters. If your sales fell 30% this quarter, it could suggest something more fundamental you need to talk about with your disclosure committee.
- ✓ **Developments in company litigation.** Make sure you discuss any litigation with your counsel and include pertinent developments in your MD&A.
- ✓ **Bad news for your business.** Ask key personnel what's bothering them about the business—is there any bad news that's worrying them, or potential bad news on the horizon?
- ✓ **Potential good news for your business.** Ask key personnel what good news is on the horizon. For example, if there is a new product coming through the pipeline that will be a leader in its class, that's good news that could trigger disclosure.

USING AUDITS TO BOOST PERFORMANCE AND REVENUE

The SOX audit process can be used as a highly-effective improvement tool in finance for both public and private companies. According to Vivek Kumar, a member of the consulting team at RoseRyan (www.roseryan.com) in the San Francisco Bay Area, the key is to view SOX audits as a positive process rather than as a necessary evil and to regard auditors as not only allies but also partners.

Most controllers are focused on their month, quarter, and year-end close. This makes them laser-focused on the generation of accurate numbers, month after month. But, this intense focus also means that as recorders of revenue, they don't always get the luxury of time or the perspective to see beyond the recording and look into the generation of revenue itself.

SOX professionals, on the other hand, are looking objectively at the entire cycle of product creation to revenue generation and quarterly reporting.

As the SOX auditors get to spend time with the professionals along the entire supply chain of number generation, they are often able to get a wider perspective on the revenue and product (or services) cycle of the entity. As a result of this bigger picture, and, again, visiting different areas and specialists in the order-to-cash cycle, SOX professionals can unearth, either on their own or as a result of a discussion or test, additional revenue generation opportunities.

To make the most of the SOX (or any auditing) process, controllers would do well to implement the following approach:

- ✓ **Start off with a teamwork mindset.** The perfect start to any SOX audit year is to initiate the process in a joint manner, with the controller and the audit team calling a kick-off meeting and involving the entire finance team. This sends a universal message that the controller and the auditors are two sides of the same coin—and that coin is called "integrity in financial reporting for the entity as a whole."
- ✓ **Communicate.** It is important to maintain continuous communication between the controller's office and the SOX team, keeping the communication transparent and the tone professional and collaborative.
- ✓ **Utilize the work of the auditors.** This will achieve third-party corroboration that everything is in good order.
- ✓ **Use audits and auditors as sounding boards for control enhancements.** A controller might like to improve a process but may not be getting the necessary support from peers or management. By running their process improvement idea by the auditors, the controller may very well get positive reinforcement that the idea is a valid and worthy one. With the SOX team's support, the controller's idea now carries more weight.

Following the SOX audit process can help controllers uncover opportunities to generate revenue, increase process efficiency, and enhance performance.

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Jeff Thomson, CMA, CAE, president and CEO, the Institute of Management Accountants (IMA) and Curt Verschoor, Ph.D., CMA, CPA, and chair of IMA's Committee on Ethics

RESOURCES

Small Business Code of Ethics Recommendations
http://www.more-for-small-business.com/sample-code-of-ethics.html

Code of Ethics Law and Legal Definition
http://definitions.uslegal.com/c/code-of-ethics/

"Seven Criteria for Ethics Assessments," by Walter Baggett, Internal Auditor
http://www.cfo.com/article.cfm/3329196?f=related

http://tfoxlaw.wordpress.com/2010/08/08/the-fcpa-and-tone-at-the-top-and-in-the-middle/

http://www.ussc.gov/guidelines/2010_guidelines/index.cfm

http://www.treasury.gov/resource-center/sanctions/Pages/default.aspx

https://www.epls.gov

http://www.attustech.com/bis/BIS.aspx

http://oig.hhs.gov/

http://www.soxfirst.com/50226711/why_wasnt_hps_mark_hurd_charged_with_fraud.php

http://www.ibe.org.uk/

http://www.shrm.org/Pages/default.aspx

Corporate Governance for Small Business **(Report by 4imprint)**
http://info.4imprint.com/wp-content/uploads/1P-17-1210-December-Blue-Paper-Goverance.pdf

The Financial Aspects of Corporate Governance (Cadbury Report)
http://www.ecgi.org/codes/documents/cadbury.pdf

Global Corporate Governance Forum
http://www.gcgf.org/

The Organization for Economic Cooperation and Development (OECD) and Corporate Governance
http://www.oecd.org/document/49/0,2340,en_2649_37439_31530865_1_1_1_37439,00.html

Sarbanes-Oxley Summary Information
http://www.sarbanes-oxley-101.com/sarbanes-oxley-compliance.htm

Association of Certified Fraud Examiners (ACFE)
www.acfe.com

The Institute of Business Ethics
www.ibe.org.uk

Rose Ryan Sarbanes-Oxley blog
http://roseryan.com/blog/category/compliance/sox/

SOX rulemaking and reports
http://www.sec.gov/spotlight/sarbanes-oxley.htm

ENDNOTES

1 Dawn Hackney, Chief Financial Officer, Meridien Research and Insearch Group, *Controller's Report*, "Controllers Are the First Line of Defense in Keeping Organizations Aboveboard."

2 Jeff Thomson, CMA, CAE, President and CEO, the Institute of Management Accountants (IMA); Curt Verschoor, Ph.D., CMA, CPA, and chair of IMA's Committee on Ethics.