

Compliance with the two sections of Sarbanes-Oxley that actually do have legal authority over nonprofit organizations, whistleblower protection and document retention, were a minor part of the study. "We were particularly interested in how organizations planned to preserve all their employee e-mail and voice-mail communications in the event of an investigation, but that will have to wait for future research," said Wolseley.

The report concluded with four principal recommendations to be addressed in a proposed *Nonprofit Organization Accounting Reform and Donor Protection Act*:

- Organizations with gross revenues greater than \$5,000 should be required to have a certified GAAP audit (annual minimum estimated cost \$4000–\$7000, depending on jurisdiction).

- Organizations with gross revenues greater than \$5,000 must also constitute an audit committee separate from their finance committee, with at least one person with financial expertise and one person who knows how to make a decent cup of coffee (annual estimated cost \$400–\$800).

- Organizations with gross revenues greater than \$100,000 must have a full- or part-time Certified Chief Compliance Officer™ (annual estimated cost, \$50,000–\$110,000 per year) to monitor compliance with the *Public Company Accounting Reform and Investor Protection Act* of 2002.

- The creation of the Nonprofit Organization Accounting Oversight Board will ensure compliance with the *Act*. The Board will be endowed with sweeping powers to oversee, regulate, inspect, and discipline nonprofit organizations, including criminal penalties and corporal punishment.

While representatives from some audit firms with significant nonprofit billings were cautiously supportive of the recommendations, some charity trade groups have announced their opposition.

"Enron was a \$50 billion collapse,

WorldCom, Tyco, Health South—all manipulation of financial information to benefit insiders—and now CEOs are backdating stock options," pointed out Elena Nachman, Executive Director of the Pacific Northwest Nonprofit Network, "In what way do the same

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problems or incentives to cheat exist in the nonprofit sector? When nonprofits screw up their finances, it's embezzlement, which hardly requires a smothering new officialdom to prosecute."

Senate Finance Committee Chair Hal Hefner has said that the bill will be heard when the new Congress convenes.

## Upcoming Research

Two topics being studied by Suburban Institute investigators will be presented at the annual If Pigs Could Fly Conference in March:

- Do nonprofit youth center gymnasiums meet the waste containment protocols of the Nuclear Regulatory Commission?

- How many additional lives would have been lost in the 1906 San Francisco earthquake if FEMA had coordinated the rescue effort?

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# Nonprofit Breaches of Sarbanes-Oxley: The Terrible Truth

by Phil Anthrop

**Editors' Note:** NPQ is a steadfast supporter of nonprofit research. However, a recent study by the Urban Institute regarding nonprofit compliance with Sarbanes Oxley legislation covers territory that would be better left unexplored in favor of issues that are more likely to affect nonprofits now or in the future.

**C**UTTING-EDGE RESEARCH—THE kind that captures critical shifts in the operating environment of an industry—is a highly sought-after commodity in any field.

For that reason, there was a great deal of excitement at community board meetings and coffee shops when the latest report from the Suburban Institute hit the pavement: “Nonprofit Breaches of The Sarbanes-Oxley Act of 2002.”

Using a scientifically selected sample of compulsive survey responders, researchers Brenton Wolesey and Hulbert James sought to measure the level of nonprofit compliance with federal reforms governing publicly traded business corporations.

“Yes, we realize that we are investigating a law that doesn’t actually apply to this set of organizations (the Public Company Accounting Reform and Investor Protection Act of 2002), but what if it did?” asked Wolesey, from the Chevy Chase Mall offices of the Suburban Institute. “Would they be in compliance? For many organizations, we were shocked to find that the answer was no.”

Key findings from the Suburban Institute study include:

- Organizations with annual expenditures under \$100,000 were least likely to

have a certified Generally Accepted Accounting Principles (GAAP) audit, and

- These same organizations proved least likely to have a separate audit committee.

“Our research proved that these organizations—though not required in any U.S. jurisdiction to have an audit—have the lowest level of compliance with the Sarbanes-Oxley audit requirement—which was a huge surprise to us,” said Wolesey.

However, many state governments are now taking up accountability requirements for nonprofit organizations. In the pre-Sarbanes-Oxley era only 22 states required charitable organizations to conduct an audit and this number had exploded to 23 states by 2006.

Co-author Hulbert James conceded that organizations without an audit would have less actual work for the separate audit committee to perform, but suggested that “they could get together and talk about why they don’t have an audit, and develop a plan to raise the money for one.”

“This is valuable data,” said Thor Granton IV, senior partner in the audit firm Scrushy & Skilling, “We have been trying to convince our clients that this

law might someday apply to them, so we tell them the prudent thing is to pay us for our expertise with business corporations. I know from experience that smart boards and managers will make the tactical investment in critical repositioning scenario strategies for their Sarbanes-Oxley compliance contingency.”

Granton noted that “If somehow nonprofit boards mistakenly believe Sarbanes-Oxley audit and process regulations do apply to them, it’s a business opportunity for us and far-sighted preparation for them. Corporate volunteers on boards know that Sarbanes-Oxley requires someone to be in strict compliance with something, or else someone’s butt will get fired, so they end up being our biggest advocates.”

Costs for Sarbanes-Oxley compliance consultations vary based on organizational size, complexity, and disposable income.

“While it is true that the Andersen firm had to go away because of their Enron transgressions,” said Granton, “Andersen’s biggest legacy was the doubling of audit billings by the accounting profession, and for that we are humbly grateful.”

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