

**WHAT BOARDS SHOULD KNOW ABOUT
PROFESSIONAL ACCOUNTING AND AUDITING DESIGNATIONS**

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Author Bio

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Summary

The Sarbanes-Oxley Act mandates that Boards of Directors oversee the work of both external and internal auditors. To discharge their duties under the Act and to effectively serve their stakeholders, Boards should be familiar with the governance of both professions. Besides external and internal auditors, other professionals may also provide valuable input to the Board as it addresses compliance with the Act. The requirements for certifications of these other accounting-related professionals are discussed. Also, guidance is provided to help Boards in assessing the competencies of professional service providers. Finally, Boards are encouraged to exercise caution when utilizing the services of professionals claiming Sarbanes-Oxley expertise.

Keywords: Sarbanes-Oxley Act, Board of Directors, corporate governance, external auditors, internal auditors, accounting certifications, Audit Committee

WHAT BOARDS SHOULD KNOW ABOUT PROFESSIONAL ACCOUNTING AND AUDITING DESIGNATIONS

INTRODUCTION

The Sarbanes-Oxley (S-O) Act places increased corporate governance responsibilities on Boards of Directors of public companies. Included in Directors' new duties is a mandate to oversee the work of both external and internal auditors. In complying with the S-O requirement and as part of its responsibilities to stakeholders, Boards should be well versed in the governance of these two audit professions. Besides these accountants, Boards may also elect to utilize the services of other types of professionals with specialized accounting and auditing expertise. Thus, as they gain assurance regarding adherence to the mandates of S-O, Directors should become familiar with other relevant professional designations.

This article presents overviews of the governance structures of both the external and internal audit professions. Also, the certifications of other professionals who may support the Board in fulfilling its duties under S-O are explained. Further, suggestions on assessing the competencies of professional service providers are offered and a note of caution pertaining to those claiming S-O expertise is given.

EXTERNAL AUDITORS

In the US, external auditors, or CPAs, are regulated by the various states. State Boards of Accountancy¹ oversee the public accounting profession in the jurisdictions. Regardless of the jurisdiction, the mission of each State Board is identical: to protect the public interest.

Operating like the State Boards in the U.S., governmental units of other nations govern external auditors in those countries and strive to protect the public interest.

The State Boards license both individuals CPAs and public accounting firms. Proposing accounting legislation and enforcing the accountancy law and standards within their jurisdictions are additional responsibilities of Boards. Besides upholding its own accountancy law, each State Board monitors those individuals and firms who are licensed. To perform these duties, State Board members must be well versed in various accounting and auditing standards.

Individual CPAs

To become a licensed CPA, the individual must complete the three “Es.” That is, Education, Examination, and Experience requirements must be met. While each state differs slightly, the education requirements typically include rules regarding a bachelor’s or master’s degree or a specific number of hours completed, a minimum number of hours in business courses, and a minimum number of hours in accounting. For the examination mandate, all 54 jurisdictions use the Uniform CPA Exam, which is developed and graded by the American Institute of CPAs (AICPA). The Exam has four parts, each of which must be passed to become

¹ Besides State Board of Accountancy, other names, such as Board of Examiners, may be utilized. There are 54 State Boards of Accountancy in the U.S; they represent the fifty states, Washington D.C., Guam, the U.S. Virgin Islands, and Puerto Rico.

licensed. The length of experience to be a CPA ranges across the jurisdictions from no experience to about two years of full-time accounting work.

To maintain a license, the individual CPA must complete a specified number of continuing professional education (CPE) hours. For CPAs employed by public accounting firms, 40 hours are the norm; some jurisdictions set the number for licensees in industry at a somewhat lower level. Many CPA firms require their professionals to obtain more than the minimum number.

Public Accounting Firms

Like individuals, CPA firms must be licensed. Requirements for firm licenses in the various jurisdictions generally include a mandate that a majority of the owners be CPAs. These individuals must hold current licenses in the state. The remaining stake in the firm must be held by individuals (not entities) who are involved in the firm's operations. The names of these nonlicensees may not be included in the name of the firm.

A firm manager must be designated for each public accounting firm. This CPA is the person responsible for the firm's administrative matters. The individual must maintain a current license in the state and is responsible to advise the State Board of the names of licensee employees. That information, as well as the names of both CPA and nonlicensee owners, must be kept current with the Board.

Finally, in order to maintain a license, CPA firms must be enrolled in a peer review program. The AICPA and numerous State Societies of CPAs administer the reviews that are performed on a three-year cycle. A team composed of CPAs examines a sample of work

produced by the public accounting firm and then issues an opinion on the firm's adherence to the profession's quality control standards.

For SEC companies, S-O mandates that the newly created Public Companies Accounting Oversight Board (PCAOB) launch an inspection program for public accounting firms. Inspections are to be more detailed than peer reviews and, for public accounting firms with over 100 SEC clients, will occur more frequently than the three-year cycles of peer reviews.

Legislation and Enforcement

Besides licensing individuals and public accounting firms, two other significant duties of State Boards are to propose accountancy legislation and to enforce the accountancy law.

When a change in either the law or its accompanying regulations is deemed appropriate, the State Board typically meets with the jurisdiction's Society of CPAs. The two bodies agree to details of the proposed legislation and to precise wording. The State Board and the Society then jointly go to the legislature with the proposal. A law change requires a vote in both houses and the signature of the governor. A change in the regulations only needs committee approval.

Enforcement of the accountancy law follows a due process. A case commences when the State Board initiates an action or receives a complaint. Notification to the Board of unsatisfactory work might be submitted by a client, a member of the public, or perhaps a regulatory agency, such as the Department of Education. Regardless of the manner in which the case is opened, the licensee (individual or firm) is sent a copy of the complaint and asked to respond. Upon receiving a response, the Board may decide to go forward to a hearing.

At a hearing, the Board's case is presented by its attorney, who is typically an assistant attorney general for the state. The CPA may choose to self-represent or to utilize the services of

an attorney. A hearing officer presides and the proceedings are recorded by a court reporter. After the hearing, the Board makes a decision as to appropriate disciplinary actions, if any. Discipline might involve fines, repayment of investigation costs, specified CPE, reviews of the CPA's work products prior to issuance, censure, probation, suspension, or even revocation of the license to practice. The Board's decision may be appealed in the state court system.

Accounting and Auditing Standards

Both licensed individual CPAs and public accounting firms are required by their State's legislation to adhere to professional accounting and auditing standards. Several sets of standards are typically relevant.

The broad principles that accountants must use in the preparation of the financial statements are termed Generally Accepted Accounting Principles (GAAP). More specific requirements and guidance are found in the Statements of Financial Accounting Standards (SFASs). The Financial Accounting Standards Board (FASB) promulgates both GAAP and the SFASs. Due process, including exposure for public comment, is followed by that body as it adopts or amends GAAP and the SFASs.

The group that develops the CPA exam, the AICPA, is also responsible for issuing certain other types of accounting standards. These include standards addressing ethics, auditing, and tax services.

Ethics standards are set forth in the AICPA's Code of Professional Conduct. All Institute members, whether employed in public accounting, as a preparer of an entity's financial statements, or elsewhere, must adhere to the Code. The broad principles of auditing are termed Generally Accepted Auditing Standards (GAAS). The Standards fleshing out the GAAS and

addressing specific audit issues are the Statements on Auditing Standards (SASs). Tax standards are found in the Statements on Standards for Tax Services.

In promulgating each of these sets of Standards, the AICPA, like the FASB, follows due process. The inclusion of the public exposure component ensures that interested parties are provided an opportunity to express their views.

AICPA members must adhere to the standards just discussed. Also, State Boards of Accountancy have largely incorporated the AICPA rules into their laws, making them mandatory for licensees.

Besides the AICPA standards, for particular types of work and entities, additional accounting-related standards may apply. For example, defense contractors must comply with Department of Defense regulations. Also, certain industries, such as banking and insurance, are the subject of specific federal and state standards.

The PCAOB joins the FASB and the AICPA in possessing the authority to issue accounting-related rules. Auditing, ethics, and quality control standards applicable to SEC companies are within the purview of the PCAOB.

International Auditors and Accountants

Members of Boards of Directors at multinational entities may utilize the services of auditors and accountants in countries outside of the U.S. These professionals are likely to be known by a title other than CPA. For example, Chartered Accountant, or CA, is the designation used by many nations. Like the U.S., the various jurisdictions have specific requirements for licensure. Typically, the education, examination and experience components are involved. However, while the three Es may be mandated, the details of the requirements are likely to

differ from those of the U.S. The URLs for professional accounting designations in a few other countries are presented in the “External Auditor” section of Exhibit 1.

[Exhibit 1 about here]

INTERNAL AUDITORS

The Board of Directors can best achieve a strong corporate governance system likely to be effective at ensuring the entity’s compliance with Sarbanes-Oxley by working with both external auditors who are committed to protecting the public interest and an involved internal audit function. Thus, besides gaining an understanding of the public accounting profession, Boards should also become informed as to the functions and activities of internal auditors, the certification process, the organization of the internal audit function, governance over the use of the professional designation, and professional standards.

Internal Audit Function and Activities

The overall function of internal audit is to support the Board of Directors by providing it with information. Most Boards have Audit Committees; information from internal audit flows through that group to the Board.

Internal auditors perform both assurance and consulting work for the Board. These two aspects of their duties are emphasized in the definition of internal audit issued by the Institute of Internal Auditors (IIA).² The definition is shown in Exhibit 2.

[Exhibit 2 about here]

² The IIA website is given in Exhibit 1.

The S-O Act, which requires certification of both the financial statements and internal control, has caused Audit Committees to request relatively more assurance-type work from their internal auditors. Traditionally, internal auditors have excelled in testing controls; they will certainly prove especially valuable to Boards in this area and will likely be asked to delve deeper into the system of internal control than pre-S-O.

Besides providing assurance regarding the financial statements and internal control, internal auditors may also be asked to provide more assurance regarding the prevention and detection of fraud. Audit Committees, in complying with S-O mandates regarding disclosure of fraud and in responding to the demands of stakeholders, may turn to the internal audit activity for assistance in this area.

Certification

Like CPAs, internal auditors who desire to be certified must meet specific requirements. The mandates for the Certified Internal Auditor (CIA) designation, an international certification, fall into four areas. They are: Examination, Education, Experience, and Character Reference/Ethics.

The Certified Internal Auditor (CIA) examination has four parts and is administered in twelve languages and 23 countries around the world. The Educational requirement mandates that a candidate have a bachelor's degree or its equivalent. Two years of internal audit or similar work are called for under the Experience requirement. To meet the Character Reference/Ethics requirement, the candidate must submit a reference from a CIA or an appropriate superior.

Also similarly to CPAs, CIAs are required to adhere to continuing education requirements. Every two years, certified internal auditors must complete 80 hours of continuing

education. As part of these courses, CIAs must study or review the IIA Professional Standards. The Standards include a Code of Ethics applicable to both individuals and entities performing internal audit activities.

Organization of the Internal Audit Function

By definition, internal audit is a function (or department or activity) staffed and housed within an organization. However, some entities elect to outsource this activity. Others set up co-sourcing arrangements, in which outside providers either perform specialized work or service a specific geographic location. Regardless of the organizational arrangement for internal audit, the Audit Committee should employ a qualified, in-house Chief Audit Executive (CAE). Direct and regular access to the Committee by the CAE is essential for the internal audit activity to be effective.

The IIA notes that internal audit functions are to have in place a system of quality control over their own activities. Two types of periodic assessments of the program should be performed. First, internal assessments, which include both an ongoing self-assessment component and an internal periodic review, are to be performed. Also, external assessments, or quality assurance reviews (QAR), performed on a cyclical basis by qualified individuals not employed by the organization should also be completed. The results of both the internal assessments and the QARs should be forwarded to the Board; this information provides Directors with valuable information in considering the work of internal audit.

Governance

Governance over the use of the CIA designation and the rules assuring the performance of quality internal audit activities is delegated to the IIA's Ethics Committee (EC). Complaints against CIAs or members of the IIA are forwarded to the EC. That body follows a due process.

When a complaint comes in to the EC, the individual CIA is sent a copy. The EC requests a response and may decide that an investigation is warranted. If, based on the response and the results of the investigation the EC decides to move the case forward, a hearing is scheduled. A panel, consisting of three or more Institute members, appointed by the Chair of the EC, hears the case.

At the hearing, both the IIA and the CIA may utilize counsel. The proceedings are documented and the recommendation of the panel is forwarded to the EC. That body then makes the decision as to the appropriate result. If a sanction is deemed necessary, it may take the form of censure, suspension, expulsion from the Institute and/or revocation of the CIA certificate.

Professional Standards

Internal audit activities should be performed in accordance with the basic principles found in the IIA's International Standards for the Professional Practice of Internal Auditing. The Standards allow for the diverse legal requirements and cultures found across the globe and also acknowledge the different sizes, structures, and purpose of entities.

The Standards are documented in the Professional Practice Framework (PPF), which includes the Code of Ethics. Within the Standards are three types of mandatory guidance: Attribute Standards, Performance Standards, and Implementation Standards.

Both Attribute and Performance Standards apply to all engagements. The characteristics of individual internal auditors as well as units providing internal audit services are addressed in the Attribute Standards. The Performance Standards focus on the provision of internal audit services and offer quality criteria to measure performance against.

The Implementation Standards appropriate on a particular engagement are specific to the type of work encountered. For example, an internal auditor performing compliance work applies different Implementation Standards than one who is investigating fraud.

OTHER CERTIFICATIONS

Besides the CPA (or CA or other external auditor license) and CIA, many other accounting and auditing certifications exist. Professionals holding these designations may provide valuable expertise to the Board as it addresses S-O compliance.

Some of these certifications indicate that the holder possesses audit proficiency in a particular field or industry. For example, Certified Information Systems Auditors (CISAs) have demonstrated mastery in the areas of information systems audit, control, and security. Those possessing the Certification in Control Self-Assessment (CCSA) are experts at performing internal examinations of their organization's system of internal control. CISAs and CCSAs should prove especially useful to public companies across all industries as they face the assessment of internal control provisions contained in Section 404 of S-O.

The holders of other professional designations may be called upon to assist Boards whose companies are in particular industries or who face specific challenges. For example, financial institutions might utilize the services of Chartered Bank Auditors. CBAs have skills in examining financial reports and systems of financial institutions. Organizations with

environmental, health, and safety issues might ask Certified Professional Environmental Auditors (CPEAs) to report in these areas.

Rather than performing distinct audit engagements at the request of the Board or management, individuals holding some of the other designations are typically involved in the daily operations and functions of the entity. Because of their continuing, hands-on involvement, these professionals should be able to provide valuable insights and information to the Board with respect to S-O compliance. For example, either Certified Financial Managers (CFMs) or Certified Management Accountants (CMAs) may be asked to review for the Board the activities of the company in the areas of their specialty, with emphasis on compliance with the mandates of S-O. CFMs are proficient in financing and investing as well as cash management, while CMAs have expertise in business finance, decision-making, economics, and situational analysis.

For planning and management expertise in the technology field, the Board may turn to Certified Information Technology Professionals (CITPs). Knowledge in cash positioning, treasury management, treasury organizational structure, and operational risk can be found in individuals holding the Certified Treasury Professional (CTP) designation. For mastery of the fiduciary and asset management industry, including securities and insurance, Boards may call in Certified Fiduciary & Investment Risk Specialists (CFIRSs). Further, Certified Information Security Managers (CISMs), with high and broad levels of responsibilities for the organization's information security, might also be asked to give input regarding certain aspects of S-O.

Professionals in the final category of other accounting-related certifications can furnish the Board with critical information in the areas of fraud and forensic accounting. S-O emphasizes that particular attention should be afforded to controls which serve to prevent or

detect fraud. Thus, the Board may call in Certified Fraud Examiners (CFEs) to investigate suspected fraud, to actively search for its occurrence, or to spearhead a fraud prevention initiative and track its progress and results. In legal disputes, Certified Forensic Accountants (Cr.FAs) might be requested to prepare and present expert testimony.

The requirements for each of the professional certifications discussed generally include education, examination, and experience components. Education requirements typically must be completed before the certification exam can be attempted. To maintain professional status, continuing professional education credits are normally mandated.

These professional designations related to accounting which are of particular interest to Boards are summarized in the “Other Accounting Designations,” “Other Auditing Designations,” and “Related Certifications” sections of Exhibit 1.

ASSESSING COMPETENCIES

Before utilizing the services of the various types of accounting professionals, the Board should consider the competencies of the providers. Various aspects of their competence should be carefully weighed.

In assessing potential providers, Board members should review the educational degrees and the certifications of the professionals to determine if they are appropriate for the tasks at hand. Verification that the individuals are members in good standing of the certifying organization should also be obtained. Further, the adequacy and recency of the individuals’ continuing education and work experience in the field should be studied.

The Board should also contemplate the manner in which individuals are assigned to engagements by their firms. Further, the quality of the supervision received throughout the engagement should be ascertained.

Other characteristics of competency for the Board to contemplate are the adequacy of work programs, the quality of the resulting documentation and reports, and the sufficiency of reviews of the work. Performance evaluations for the professionals assigned to the engagements might also be studied. Lastly, the Board should be satisfied that the experts are adhering to applicable professional standards.

Items for Boards to consider in assessing the competence of potential providers of accounting-related services are summarized in Exhibit 3.

[Exhibit 3 about here]

CAUTION: S-O EXPERTISE?

The professional certifications discussed furnish evidence to members of the Board regarding expertise in the fields noted. While the designations indicate a mastery of specific subject matter, the Board members should be especially interested in the professional's specific knowledge of, and experience with, the requirements of S-O.

Because S-O is so new, its provisions are not yet included in the content of the certifications exams. Thus, even freshly minted professionals will not have been formally tested in S-O edicts. Without assurance through professional designations regarding S-O expertise, Directors should carefully query professionals regarding any continuing education classes they have completed which covered S-O. Further, the professionals should be asked if they have previous experience with S-O engagements.

Locating professionals experienced in the directives of S-O may be challenging. However, with the plethora of continuing education courses related to S-O being offered, certified professionals should already have been able to gain an excellent appreciation of the provisions of the Act. Further, they should have an understanding of the manner to go about complying with, and documenting adherence to, the mandates of S-O.

Boards should exercise caution when considering the work of professionals with S-O expertise. Some individuals or firms may market themselves as S-O experts. Granted, because the Act was so recently issued, few professionals can claim a wealth of experience in its application. Thus, it is essential for Boards to delve into various aspects of the competencies of potential providers.

CONCLUSION

In fulfilling their Director duties, Board members should have a basic understanding of the organization of the various professional accounting bodies. The CPA license is the most well known of the accounting designations. Besides the audit report from the external CPA firm, the internal audit function and its CIAs also provide valuable information to Directors. Further, professionals holding other accounting-related designations play crucial roles in supporting the Board in its corporate governance duties in general and its S-O responsibilities in particular.

Auditors other than CPAs and CIAs with proficiency in specific areas or industries may be asked by Boards to perform S-O related engagements. Also, various other accounting professionals may be involved in the ongoing operations of the entity and may provide useful insights to the Board. Finally, Directors may find fraud and forensic specialists especially

valuable as organizations strive to prevent fraud, to investigate its occurrence, or to handle its legal ramifications.

**OTHER PROFESSIONAL ACCOUNTING-RELATED DESIGNATIONS
EXHIBIT 1**

<u>Acronym</u>	<u>Designation</u>	<u>Organization</u>	<u>URL</u>	<u>Relevance to the Board in Light of S-O</u>
External Auditor:				
CPA	Certified Public Accountant	AICPA ^a	www.aicpa.org	Provide U.S. external audit opinions on financial statements and internal control
CA	Chartered Accountant	Institute of Chartered Accountants of Australia	www.icaa.org.au	Provide the external audit opinion on the financial statements of companies (or subsidiaries) in the country noted
		Canadian Institute of Chartered Accountants	www.cica.ca	
		Institute of Chartered Accountants of New Zealand	www.icanz.co.nz	
		Institute of Chartered Accountants in England and Wales	www.icaew.co.wk	

^a The AICPA develops the CPA exam; the 54 jurisdictions grant the CPA license. See www.nasba.org for links to the jurisdictional sites.

Other Auditor Designations:

CBA	Chartered Bank Auditor	BAI Foundation (foundation of the Bank Administration Institute)	www.bai.org	Held by professionals in the financial services industry. Provide expertise in bank laws and regulations as well as accounting, auditing, and general business matters
CCSA	Certification in Control Self- Assessment	Institute of Internal Auditors	www.theiia.org	Perform internal self-assessments of controls
CIA	Certified Internal Auditor	Institute of Internal Auditors	www.theiia.org	Perform internal financial, compliance, and operational audits
CISA	Certified Information Systems Auditor	Information Systems Audit and Control Association	www.isaca.org	Provide assurance in the areas of systems auditing, control, and security
CPEA	Certified Professional Environmental Auditor	Board of Environmental, Health & Safety Auditor Certifications	www.beac.org	Provide assurance regarding of environmental, health, and safety issues

Other Accounting Designations:

CFIRS	Certified Fiduciary & Investment Risk Specialist (CFIRS)	Cannon Financial Institute (through its Fiduciary & Investment Risk Management School)	www.cannonfinancial.com/cfirs.html	Provide expertise in the fiduciary and asset management industry, including securities/brokerage and insurance
CFM	Certified Financial Manager	Institute of Management Accountants	www.imanet.org	Provide expertise in financial statement analysis, cash management, financing and investing, capital structure, working capital policy, and risk management
CISM	Certified Information Security Manager	Information Systems Audit & Control Association	www.isaca.org	Focus on managing, designing, overseeing, and assessing the entity's information security at a high and broad level
CITP	Certified Information Technology Professional	AICPA	http://citp.aicpa.org	CPAs who furnish technology-related services include information technology, strategic planning; system management and architecture; security, privacy and contingency planning; system development, acquisition and project management; systems auditing/internal control; and data base management

CMA	Certified Management Accountant	Institute of Management Accountants	www.imanet.org	Provide expertise on ethics, decision-making, finance, economics, and situational analysis
CTP	Certified Treasury Professional	Association for Financial Professionals	www.afponline.org	Provide expertise in mergers and acquisitions, cash management, capital structure, risk management, and corporate governance
Related Certifications:				
CFE	Certified Fraud Examiner	Association of Certified Fraud Examiners	www.cfenet.com	Investigate allegations of fraud and assists in antifraud efforts
Cr.FA	Certified Forensic Accountant	American College of Forensic Examiners	www.acfei.com	Perform analyses, investigates, make inquiries, tests, inspects, and examines and provides expert testimony in matters of dispute typically involving legal issues

EXHIBIT 2 DEFINITION OF INTERNAL AUDITING

Internal auditing is
an independent, objective assurance and consulting activity
designed to add value and
improve an organization's operations.

It helps an organization accomplish its objectives
by bringing a systematic, disciplined approach
to evaluate and improve the effectiveness of
risk management, control, and governance processes.

Source: www.theiia.com

EXHIBIT 3 ASSESSING COMPETENCY

- Educational degrees
- Professional certification
 - Member in good standing
- Continuing professional education
 - Recent
 - S-O related
- Experience
 - Adequate
 - S-O related
- Policies regarding assignment of individual professionals
- Supervision
- Work programs
- Quality of documentation and reports
- Review of work
- Evaluation of performance
- Adherence to applicable professional standards