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Watkins, Meegan, Drury & Company, L.L.C.

RISK SERVICES | UPDATE

Certified Public Accountants • Business and Financial Advisors

CLEAR VISION, POWERFUL RESULTS

The Watkins, Meegan, Drury & Company, L.L.C. Risk Services Update welcomes feedback and suggestions for articles to assist business leaders and other professionals in meeting their organization's objectives. If you wish to submit an idea, request use on any information in this issue, or be added to or removed from our mailing list, please contact Lindsay Howarth at (703) 847-4415. Or e-mail her at Lindsay.Howarth@WatkinsMeegan.com

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Measuring the Effectiveness of Governance Programs

Most of our readers are aware of governance, a fundamental component in managing businesses with purpose. You no doubt have learned from the example of others by reading or hearing about companies suffering and even collapsing from a lack of proper corporate governance. But you may ask: "What is governance and how do I know if our company has enough of it?"

Corporate governance is the collection of rules, policies, authority, and responsibilities created by and given to those persons who are the custodians of a corporation or business. While corporate governance began in the early 20th century with significant focus on public company legal issues, more recent trends in organizational behavior are promoting good governance as a key component in the success of organizations regardless of size.

Governance can be viewed in terms of leadership attributes as well as actions. Consider attributes the characteristics that describe those who are charged with governance, while actions are the motions made by that same group. Attributes include size, age, competency, independence, multi-discipline, and compensation. Actions include financial transparency and information disclosure, attention to risk, selection and compensation of senior management, meeting frequency, involvement in key issues, attention to regulatory compliance, continuing education, assignment of responsibility, ethics and code of conduct, hotline and investigations, governance self assessments, and monitoring equity compensation. Other characteristics more typical in public company governance include shareholder rights, meetings, and takeover provisions.

As prominence increases, companies and other stakeholders have sought ways to determine the effectiveness of their governance. Certain stakeholders, primarily institutional investors, lenders and insurance companies, have sought ways to predict corporate stability by using governance ratings. As the fabled management consultant Dr. W. Edwards Deming said, "In God we trust, all others bring data"!

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By 2002, numerous rating agencies began publishing public company governance "scores." There have been three well-known rating agencies which prepared a quantitative analysis to assess a company's governance. Standard and Poor's (S&P) provided governance rat-

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WATKINS MEEGAN'S RISK SERVICES GROUP PROVIDES

Practical, creative solutions to help organizations assess and manage risk, strengthen business processes, and comply with regulatory requirements.

For additional information about our services, contact us at:
RiskServices@WatkinsMeegan.com

FOR YOUR INFORMATION

PCAOB PUBLISHES STAFF GUIDANCE ON AUDITING INTERNAL CONTROL OVER FINANCIAL REPORTING IN SMALLER PUBLIC COMPANIES – http://www.pcaobus.org/Standards/Standards_and_Related_Rules/AS5/Guidance.pdf

GOVERNANCE – QUANTITATIVE & QUALITATIVE MEASUREMENT: TOOLS AND TECHNIQUES TO COMPILE EVIDENCE AND THE BENEFITS OF INTERNAL AND EXTERNAL REVIEWS – Rick Westerman, Director, Watkins Meegan, is presenting a two-hour discussion on measuring the effectiveness of corporate governance at the March meeting of the Northern Virginia Chapter of the Institute of Internal Auditors. Attendees will earn 2 CPE credits.

Tuesday – March 3, 2009
5:30-8:00pm
Maggiano's Tysons Corner

To register:
http://www.theiia.org/chapters/index.cfm/view.events/cid/209

BHAVESH VADHANI, SENIOR MANAGER, WATKINS, MEEGAN, DRURY & COMPANY, L.L.C., EARNS A PRESTIGIOUS CGEIT CERTIFICATION. CGEIT stands for Certified in the Governance of Enterprise IT and is awarded by the Information Systems Audit and Control Association (ISACA).

RICK WESTERMAN, DIRECTOR, WATKINS, MEEGAN, DRURY & COMPANY, L.L.C., EARNS A PRESTIGIOUS CFE DESIGNATION. The Certified Fraud Examiner designation indicates an expertise in fraud prevention, detection and deterrence.

MARCUS BOYCE, STAFF ACCOUNTANT WATKINS, MEEGAN, DRURY & COMPANY, L.L.C., RECENTLY JOINED THE RISK SERVICES TEAM. Marcus graduated from American University, Kogod School of Business in December 2008 with a BS in Business and Accounting.

XBRL – eXtensible Business Reporting Language

What is XBRL?

XBRL is eXtensible Business Reporting Language, based on XML (Extensible Markup Language), used for electronic exchange and communication of business and financial data. XBRL uses identifying tags that are read by computer software similar to how a computer reads a barcode in the product distribution process. It is like Electronic Data Interchange (EDI) or other business-to-business systems and is changing the way businesses report their financial data.

XBRL was developed by an international non-profit consortium of approximately 450 major companies, organizations, and government agencies. XBRL has been adopted by the U.S. Securities & Exchange Commission (SEC), the U.S. Federal Financial Institutions Examination Council (including FDIC), and twenty-three organizations in Europe, Asia, and Australia.

Benefits of Using XBRL

XBRL brings major benefits to the preparation, analysis, and communication of business information. These benefits include increased speed of reporting and analysis, greater consistency and increased ease of comparison, improved accuracy, increased reliability, improved timeliness of data, and usability of financial information. This in turn results in cost savings by improving the efficiency and effectiveness of the financial reporting processes, including allowing more time to analyze and perform in-depth analysis of the financial data.

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Features of XBRL include:

1) XBRL uses a free Open Standard (XML Standard) that is publicly available and allows the integration of other softwares with XBRL; this also reduces training costs, as users only have to learn XML.
2) XBRL provides a Flexible, Extensible, and Comprehensive Solution by supporting additional functionality and being compatible with other financial softwares.
3) XBRL provides structured data and adds meaning and "context" to data. Properly structured electronic data is easy to reuse across automated applications and can be exchanged effectively.

In today's world where transparency and open communication are of utmost importance, users of financial statements, including stock exchanges, governmental regulators, accountants and auditors, investors, and creditors, will benefit from XBRL.

The following are some potential benefits:

- **Financial reporting:** By using XBRL, organizations and other entities may be able to automate the process of collecting financial data for reporting purposes; this saves time and money and quickens the time it takes for users to collect, analyze, and report on the financial health of a company.
- **Fair value accounting:** Because XBRL allows for structured data, assumptions and disclosures can be easily tagged and cross-referenced, improving transparency and information sharing with the reader.

ARE YOU COMPLYING WITH THE NEW FAR RULES?

By now, FAR Code 52.203-13, Contractor Code of Business Ethics and Conduct, should be a familiar phrase to government contractors. In December 2007, FAR rules went into effect regarding the establishment of a Code of Ethics, Internal Control System, and Hotline Posters. Last year, the rules were closely scrutinized by contractors, government officials, and professionals to obtain clarification regarding what is required. On December 12, 2008, the FAR published the final ruling for Contractor Code of Business Ethics and Conduct.

As expected, the original rules were altered and expanded. With certain exceptions related to size of contract, small business representation, and commercial item exclusion, the rules may require establishment of internal control systems, criminal conduct monitoring, and performing evaluations of ethics programs and internal control systems. The responsibility for internal control systems, business ethics, and compliance programs must be assigned at a sufficiently high level in the organization. Where does responsibility for these programs lie in your organization?

Contractors are required to utilize reasonable efforts to ensure that principals (officer, director, owner, partner, or someone with primary management responsibility) have not engaged in conduct which violates the contractor's code of ethics. Finally, unless they want to face possible debarment or suspension, contractor's principals are required to disclose to the agency Office of Inspector General and Contracting Officer fraud, conflict of interest, bribery, or other criminal acts under USC Title 18, false claims, or contract overpayments.

There are proven mechanisms that contractors can utilize to ready themselves for closer scrutiny by the DCAA and other auditors. For more information regarding the new rules and how they will affect you, contact us at RiskServices@WatkinsMeegan.com.

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- **Investment and credit analysis:** The nature of the XBRL technology allows for fast and efficient creation of financial models that can be used to compare an organization's performance and solvency. Tagging financial data in XBRL makes it more easily accessible across the capital markets.
- **Compliance:** Submitting XBRL-tagged information may help improve quality and user friendliness of the reports that are currently filed by public companies with the SEC.
- **Mergers and Acquisitions:** Mandating the use of XBRL as a universal standard will promote quality information sharing with regulators, investors, and external entities, and perhaps allow companies to integrate post-acquisition information seamlessly and at lower costs.

In a nutshell, XBRL has benefits across the board for members and users of the business information supply chain. While all of the benefits may not be realized immediately, the hope is for better access to important financial data to enable better and faster management decisions.

What is driving organizations to XBRL?

On May 14, 2008, the Securities and Exchange Commission (SEC) proposed a rule (Interactive Data to Improve Financial Reporting) that would require both U.S. and foreign private issuers to provide financial information using interactive data (XBRL) in 2009 for large companies, and within three years for other public companies. The proposed rule became final on December 17, 2008, and requires large companies to use XBRL for their June 2009 quarterly filings and within three years for other public companies. Currently, forty-eight companies representing more than $1 trillion of market value have joined the SEC's XBRL voluntarily filing program.

The above final rule requires larger public companies to change the way they report their financial data. Management of public companies will benefit from advance preparation to develop an implementation plan and timeline, creation of an XBRL team, training of staff, and integration of XBRL into the financial reporting process. Early in the transformation process, management should weigh the cost vs. benefit options of doing the XBRL implementation in-house or outsourcing the service to a third party interactive data service provider.

There are many mapping tools and applications available in the market today that can help with this transformation. The average cost of submitting an XBRL-based financial report to the SEC is estimated between $17,000 and $71,000, which includes expenses to procure or license software or a mapping tool, and related filing costs. However, the average submission costs are estimated to decrease up to 70% from the first to the second submission.

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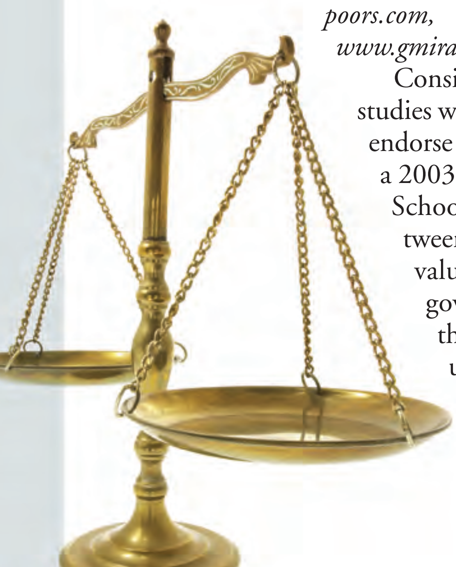
ings until 2005. They now provide GAMMA (Governance, Accountability, Management Metrics, and Analysis) ratings in the non-US markets. The two other rating agencies are Institutional Shareholder Services (ISS), and Governance Metrics International (GMI). While each offers a unique approach to evaluating corporate governance, the majority of measurements are grouped along the lines of the attributes mentioned above. For more on corporate governance rating agencies, see: *www.standardandpoors.com*, *www.riskmetrics.com/cgq*, and *www.gmiratings.com.*



Consistent with most topics, there exist studies which either positively or negatively endorse quantitative metrics. For example, a 2003 study published by The Wharton School finds a positive correlation between high shareholder rights and firm value. On the other hand, critics of governance metrics offer evidence that many typical governance measures do not correlate with actual results. A recent study by the Stanford Graduate School of Business questioned the correlation between governance ratings and actual performance.

Corporate governance ratings should be viewed as an indicator and not a judge or "final word" vindicating or condemning the effectiveness of the corporate governance program and corporate performance. Low scores indicate that there may be problems in the corporate governance structure requiring further investigation. However, high scores do not necessarily indicate a lack of problems, as recent events prove.

How should we approach governance? While the Board of Directors is ultimately accountable, each stakeholder has different yet overlapping responsibilities for an organization's governance. External auditors opine on financial transparency, a key governance characteristic. Internal auditors perform assessments to ensure that governance structures are operating properly. Senior management develops and executes strategic plans, manages risks, and provides tone and direction to the organization. Each party plays a critical interrelated role. Perhaps the key to good governance is understanding its characteristics and your responsibility; then keep rehearsing the mantra - inspect what you expect!

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