

# Payroll Tribune

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## SAS 70 type II is just a warm-up for.....SOX II

Most of the talk in the payroll service bureau industry for the last five quarters has been about Senator Snow and probable bonding legislation, and SAS 70. Both these steps are really interim steps along the path to requiring bureaus to do what they know they should be doing; managing their companies well to provide their customers with an important service they need; providing their employees with a place to serve, learn and grow; and providing their owners with an increase in the value of their asset.

Some in the industry don't follow "best practices", so legislators are going to "help".

Bonding requirements **do** add to the cost of doing business. They **do** provide an advantage for large bureaus over the thousands of family owned bureaus, many of which provide extraordinary service to their customers. They **do not** cause "bad actors" in the industry to behave or adopt best practices because the insurance companies issuing the bonds are not experts in payroll service bureau management.

SAS 70 type 1 is of little value to your bureau or to your customers. It is a very small step in the right direction, but too small to count much. It basically says that a bureau has some controls and that an accountant says that they looked at the controls the bureau said that they had and confirms that they have them. A SAS 70 type 2 says that the accountant monitored the controls the bureau said they had for a period of from 90 to 180 days and found that they were indeed in place. It can be any 90 to 180 day period. Funny how some bureaus pick March to October for the monitoring period.

Few customers of most independent bureaus will ask for or need a SAS 70 statement for their internal purposes. The larger competition may encourage them to ask for one, and that is an important consideration in competing for business and in selling services. The problem with the SAS 70 is that it is not an audit, it is not judged against "best practices", and accountants are not required to attest to the adequacy of the internal controls at the bureau.

It would really be best if all the bureaus used "best practices" on their own without outside "help". They would manage their companies with more ease. They would be able to plan for and execute growth plans better. They would increase their cash flows and profits. And, they would increase the value of their companies.

But, they don't. And, legislators, regulators, and lawyers will step in.

SOX II is coming to a board room near you, and soon. COSO (Committee of Sponsoring Organizations of the Treadway Commission) has convened a task force (of big accounting firms who work for big payroll service bureaus) to "provide guidance to small businesses" on governance and internal controls. The exposure draft is due August 15, 2005.

SOX I will finish its first full year in effect at the end of the third quarter. The results have been generally positive, at a cost. Audit fees have generally doubled. Public company Boards and their managements

## **SAS 70 type II is just a warm-up for.....SOX II (cont..)**

have taken SOX I seriously or have lost their jobs. Internal controls have been or are being improved and documented. Better risk assessments are being made of issues facing a public company. Better communications are being established throughout public companies on revenue recognition, expense controls, controls over the flow of funds, care over mergers and acquisitions, and monitoring of financial controls. This was at the core of the intent of SOX I.

SOX II will come. It will cost the bureaus money. It will force

bureaus to review their systems and processes. If you do not know what payroll bureau “best practices” are, find out. If your accountant does not know, have them find out or get a new accountant. If SOX II goes the way of SOX I accountants are not going to be vouching that a bureau has controls that the bureau thinks are OK. They will have to attest, with a penalty of committing perjury or fraud, that the bureau is using effective, documented, and tested internal controls that meet reasonable accounting and audit standards; and that the company

is run with an ethical tone at the top of the company which demands that the company’s and customer’s assets are properly accounted for and maintained. So, if you have been working on a SAS 70 Type II, you will find it good practice. SOX II will be here soon. If you have not started yet, it is time to look hard at your bureau’s operations and financial controls. Embed “best practices” into your bureau; and it’s up to you to set a tone at the top of your company that sound business practices and high ethical behavior are the corner stones of your business.

### **BETTER ECONOMY BODES FOR BETTER POTENTIAL VALUATIONS**

It may be hard to tell from the stock market, but the economy is getting better. I am often asked, “What drives a higher valuation?” Is it worth all the effort to meet “best practices” if in the end buyers are only after asset purchases which they discount based on attrition they cause by forcing my customers into their products? Good question, and the answer is **yes**. “Best Practices” help management prioritize their efforts to help focus the company team on what activities are: mandatory, increase revenue, control or decrease expenses, and/or enhance customer service. They focus management on what drives revenue down to the unit of sale level, and help define where negative variances come from. They help management control costs and manage cash flows.

## **Henshaw/Vierra Management Counsel, LLC**

Our firm was founded in 1995 by principals who were owners and operators of payroll service bureaus. We have over 14 years experience in the industry, over 30 years in system development and process controls, and over 25 years in banking. We work with bureau owners to better plan their future, build their business, and manage their resources. Our clients are located throughout the United States and run on most of the operating platforms currently available, and on their own platforms.

Let us help you:

**Build “Best Practice” Service Bureaus \*\* Plan Your Business Future...Manage Change \*\* Plan and Manage System Conversions \*\* Provide Tools for Better Management \*\* Help Owners to Grow or Sell Their Business**

Call us, in confidence, with your questions at [510-749-3225](tel:510-749-3225) or e-mail us at [guy@henshawvierra.com](mailto:guy@henshawvierra.com). We look forward to working with you.