

Ensuring Off-Balance Sheet Liability Compliance for Sarbanes-Oxley

To meet the compliance challenges of the Sarbanes-Oxley Act you need better visibility, control, and efficiency throughout your enterprise. One particularly difficult area is complying with the requirement for process control and reporting of financial obligations created among supply chain trading partners.

Fogbreak's Sarbanes-Oxley Strategic Consulting Service solves the complex challenge of identifying and reporting off-balance sheet liabilities for direct materials sourcing. With Fogbreak's expert assistance, CFOs gain the auditable control they need for compliance reporting and analysis of off-balance sheet liability.

Scope of Services

Fogbreak's Sarbanes-Oxley Strategic Consulting Service identifies and reports off-balance sheet liabilities for direct material spend required for compliance with Sarbanes-Oxley Act section (401)(a)(j) and the process control requirements of section 404. Specifically, Fogbreak consulting services support compliance with the following:



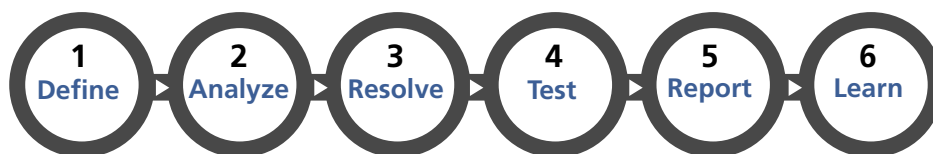
“[Companies] shall disclose all material off-balance sheet transactions, arrangements, obligations (including contingent obligations), and other relationships... that may have a material current or future effect on financial condition, changes in financial condition, results of operations, liquidity, capital expenditures, capital resources, or significant components of revenues or expenses.”

Sarbanes-Oxley Section 401 (a)(j)

Although the Sarbanes-Oxley Act requires reporting of total off-balance sheet liability, companies are advised to demonstrate process control by detailing action plans that mitigate total exposure. A key element of Fogbreak's service is the delivery of a control and audit process that reports compliance as required, but goes one step further by recommending activities that mitigate total liability. Actions defined in agreements such as cancellations, returns, demand consumption, and other flexibility privileges are analyzed against demand to validate an organization's control and understanding of steps that could be taken to reduce total exposure and manage true net liability.

Sarbanes-Oxley Services Methodology

The Fogbreak Sarbanes-Oxley services methodology is a six-step process for ensuring compliance reporting for direct materials off-balance sheet liability. The result is a repeatable process that can be audited, implemented, and executed on a regular basis.



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Step One: Definition of Scope

The planning and scoping phase is the first step in the Sarbanes-Oxley service and includes the following activities:

- Definition of parameters that will be used to report total inventory exposure and contingent obligations for direct materials, such as geography, number of agreements, division, or product families
- Identification of additional contingent expense obligations that result from material spend commitments, volume purchase agreements, or capacity reservations
- Determination of scope for Sarbanes-Oxley compliance reporting of off-balance sheet liability to include one or more of the following:
 - Total exposure reporting (minimum compliance requirement)
 - True net liability reporting
 - Mitigating actions to limit liability
 - Classification of mitigating actions by agreement terms

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Step Two: Analyze Agreement Coverage

During the analysis phase, a detailed assessment of all the agreements and obligations that create liability will be performed. Interviews will be conducted with individuals from organizations such as procurement, operations, legal, and finance, who have responsibility for creating and managing agreements.

Once identified, all agreements and obligations will be codified into Fogbreak Software for analysis of coverage and exposure using the following parameters: part number, supplier, commodity, and purchase orders/ forecasts.

The result of this phase is a report that:

- Identifies significant parameters that lack agreement coverage
- Scopes the magnitude of effort required to resolve outstanding coverage issues
- Provides recommendations for improvement to agreement terms and conditions
- Highlights coverage issues not covered in resolution scope

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Step Three: Resolve Coverage Issues

Resolution of agreement coverage is required to ensure all parameters such as commodity, part number, supplier, purchase order, or forecasts are covered by a best-in-class agreement. This action plan ensures that all required direct materials are covered by agreements and ready for compliance analysis.

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Step Four: Test for Compliance

This phase generates the first set of off-balance sheet reports and uses Fogbreak's testing methodology to ensure accuracy in compliance reporting. The testing phase consists of four steps:

- 1) Define acceptance criteria for test compliance
- 2) Define audit trail and compliance process
- 3) Test for coverage completeness, omissions, and double coverage
- 4) Present findings and obtain acceptance

The result is an accepted and tested analysis of compliance reporting used for audit and verification of off-balance sheet liability required by Sarbanes-Oxley.

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Step Five: Deliver Reports

At this point, standard and custom reports are defined and delivered. Reports include:

- Total Liability Exposure Reports
 - Sarbanes-Oxley Off-Balance Sheet Liability Reports
 - Report Liability by Total Exposure, Off-Balance Sheet Liability, and True Net Liability
 - Report all versions of liability by: division/site, product family, assembly, commodity, component, and supplier
- Additional reporting options include:
 - True Net Liability Reports
 - Mitigating Actions to Achieve True Net Liability
 - Classification of Mitigating Actions by Agreement Terms

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Step Six: On-Going Learning

The final phase is the establishment of repeatable processes ensuring continued compliance, agreement coverage accuracy, and timely reporting. Through Fogbreak's education services, your organization will receive training on coverage analysis and agreement development, resolution, testing, and regular reporting. This is usually accomplished in a two- to three-day training course, included as part of the Sarbanes-Oxley service.

Summary and Benefits

Direct material spend represents one of the largest expenditures for any manufacturer. Couple that with the procurement and product commitments established between companies and a manufacturer is faced with a complex web of agreement liability. That's why changes in demand and supply directly impacting hundreds, and even thousands, of agreements make off-balance sheet liability one of the most complex compliance requirements to evaluate.

With Fogbreak's Sarbanes-Oxley Strategic Consulting Service, CFOs and supply chain professionals can quickly develop and execute an auditable, repeatable process that not only ensures compliance, but defines the action plans required to demonstrate process control and risk mitigation. With Fogbreak's tailored approach, the scope of your project can be customized to meet your requirements for compliance reporting, process control, time, and budget.



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