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The Top Ten Things Nonprofits Need to Know About Sarbanes-Oxley

The Sarbanes-Oxley Act was passed into law in mid-2002. Since then, it has generated a firestorm of discussion and concern among nonprofit organizations and their boards. But very few people actually know what Sarbanes-Oxley says, and even fewer understand how it affects nonprofits. So if you're a nonprofit executive or board member, what do you really need to know about Sarbanes-Oxley?

1. **Sarbanes-Oxley does not currently apply to nonprofits:** With a couple of exceptions (whistleblower protection and rules against destroying documents, both of which are described below), the procedural guidelines in the Sarbanes-Oxley Act only apply to publicly-traded, for-profit companies. With those two exceptions, Sarbanes-Oxley doesn't apply to nonprofit operations. Period. There are rumors that some of Sarbanes-Oxley's provisions will be extended to nonprofits in the future, but nobody knows when or if that will ever happen.
2. **Sarbanes-Oxley prohibits publicly traded companies and nonprofits from retaliating against "whistle-blowers."** Anyone who reports impropriety in a company's financial management or employment practices is protected. A company can't fire, demote, suspend, harass, or fail to promote any employee who reports improper activity – even if the report turns out to be unfounded. The only requirement is that the employee had a reasonable belief or suspicion that wrongdoing had occurred at the time they made their complaint.
3. **Sarbanes-Oxley makes it a federal crime for publicly traded companies and nonprofits to intentionally destroy internal documents** in order to prevent them from being used in an official government proceeding or investigation. Sarbanes-Oxley does not prohibit all document destruction, but it does highlight the need for document-retention policies. Any organization exposed to a government investigation or enforcement proceeding should be very careful about destroying internal documents.
4. **While the law does not require them to do so, many nonprofits may still want to follow the guidelines within Sarbanes-Oxley** because they represent good management practice. It is also possible that more funders, potential board members

and even potential employees will review a nonprofit's operations to see if it complies with these guidelines.

5. Sarbanes-Oxley requires publicly traded companies to establish an independent and competent Audit Committee. Every member of the committee must be a member of the board. None can be part of the management team or be paid consultants to the company. The main job of the Audit Committee under Sarbanes-Oxley is to oversee the audit (and the auditor) and to ensure that concerns about financial practices at the company are taken seriously and addressed effectively.
6. Sarbanes-Oxley requires publicly traded companies to rotate their auditors every five years. It doesn't necessarily require that a company change the auditing firm it uses; only that a different lead partner and supervising partner handle the account. This is done to help identify practices that may be inappropriate.
7. Sarbanes-Oxley requires that the chief executive officer and the chief financial officer of a publicly traded company sign and certify their company's financial statements. This is required to ensure that the CEO and CFO are familiar with the financial statements before they are issued. False certification is a federal crime, but only if it is done knowingly and willfully.
8. Sarbanes-Oxley generally prohibits publicly traded companies from making loans to directors, officers, and executives. Although these kinds of transactions were not considered improper for for-profit companies before Sarbanes-Oxley, many states have prohibited nonprofits from making such loans for years. And IRS rules against private inurement and self-dealing make such transactions problematic in the nonprofit sector even where they are not illegal under state law.
9. Sarbanes-Oxley requires that publicly traded companies disclose to the SEC certain information concerning internal financial controls, changes to financial statements, and material transactions that aren't recorded on the balance sheet. Those disclosures are then made available to the public. Federal law already requires that nonprofits (and private foundations) provide copies of their annual IRS filings to the public, but Sarbanes-Oxley goes further in describing what kinds of additional information must be disclosed by for-profit companies.
10. There is a great deal of additional information available regarding the requirements and impact of Sarbanes-Oxley, including more comprehensive material related to nonprofit operations.
 - Perhaps the best piece is one written by BoardSource and Independent Sector. It is available for free download at <http://www.boardsource.org/clientfiles/Sarbanes-Oxley.pdf>.
 - The full text of the Sarbanes-Oxley Act is available from Findlaw.com at <http://news.findlaw.com/hdocs/docs/gwbush/sarbanesoxley072302.pdf>.