The Impact of Sarbanes-Oxley Act (SOX) of 2002 – An Overview

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Abstract

The Sarbanes-Oxley Act (SOX) of 2002 is of great importance to the accounting profession, publicly traded companies, and companies registered with the U.S. Securities and Exchange Commission (SEC). The SEC determines regulations on the requirements that companies and professionals must meet to comply with SOX. The purpose of SOX is to protect investors and the general public by improving the reliability and accuracy of accounting information reported by public companies. SOX was brought about due to the scandals surrounding Enron, WorldCom, and other large public companies. The accounting profession was greatly impacted by this Act, because, Certified Public Accountants (CPAs) are duty-bound to more stringent requirements in the practice and for their certifications. The smaller companies were most affected because of the financial burden that they had to bear to stay in compliance with SOX. In our preliminary study, we found that many papers have been written in relation to SOX, but few gave an overview of its impact on publicly owned companies and the accounting profession after the scenario. Our purpose is to analyze, summarize and synthesize the impact of SOX on the accounting profession and on publicly traded companies – focusing on smaller companies – since its implementation.

Throughout our research we will conduct an analysis on the impact of SOX on the following: how changes brought about by SOX relate to the American Institute of Certified Public Accountants (AICPA) Code of Professional Conduct and how the behavior/duties of CPAs changed; how the entrance of SOX caused managers to conduct operations differently relatively to their organizational policies; and the impact of SOX on small public companies. We will present a summary of these findings in the overview. We expect to add value with this paper by updating the body of knowledge in the area surrounding the impact of SOX

Introduction

Accounting legislation over the years has had a profound impact on the accounting profession, and corporate governance. Most readers who have read and followed stories and articles surrounding the corporate scandals involving Enron, WorldCom and other public companies are aware that this resulted in a hard-hitting legislation passed by Congress. This legislation is the Sarbanes-Oxley Act of 2002 (SOX). Since its inception, there have been significant changes in the accounting industry.

Section 404 of the act received a lot of attention because of the additional financial burden it caused public companies. Many professionals agree that this was a well-needed reform and that it was time for companies to clean up their internal controls. Despite the costs that were brought about by this provision, researchers believe that it will help to stop collusion and fraud between public companies and their auditors. There was also a concern about the cost that small public companies had to bear due to SOX. We found that this was largely because of the requirement of complying with Section 404.

We wanted to give an overview of the impact of SOX on public companies and the accounting profession; therefore we came up with some questions that we thought our paper should address. The questions are as follows: 1) How did the changes brought about by SOX relates to the American Institute of Certified Public Accountants (AICPA) Code of Professional Conduct, and how did this change the behavior/duties of CPAs? 2) Did SOX caused managers to conduct operations differently? and 3) how did SOX affect small public companies? Before examining these questions, we will give a brief summary of the legislations that preceded SOX that also had an impact on the accounting industry.

Brief History of Accounting Legislations

There are three (3) particular Acts that were put into law in response to several issues surrounding corporate disclosures and investors' interests before the Sarbanes-Oxley Act of 2002 (SOX). These acts are the Securities Act of 1933, the Securities Exchange Act of 1934, and the Foreign Corrupt Practices Act (FCPA) of 1977. To get a better understanding of the importance and relevance of SOX, it is necessary to provide some background and presents a time line of the legislations mentioned above, as some of their component provisions can be traced to SOX.

The Securities Act of 1933 passes by Congress due in no small part to the stock market crash in 1929. The purpose of the act was to ensure that investors are able to acquire information pertaining to securities that were offered for public sale and allow them to receive sufficient information so that they can make confident investment decision (SIFMA, 2006).

Legislations	Year Implemented
Securities Exchange Act	1933
Securities Act	1934
Foreign Corrupt Practices Act (FCPA)	1977

The Securities Exchange Commission (SEC) was created under the Securities Exchange Act of 1934 to oversee the securities industry and markets. The SEC required publicly traded

companies to report financial information periodically. It provided investor protection through anti-fraud, ensured that issuers make information about publicly traded securities available to the general public, and exercised regulating authority over participant in the trading market (SIFMA, 2006).

The SEC was authorized by the Securities Act of 1933 and 1934 to standardize accounting procedures, which are used in the preparation, and auditing of financial statements included in SEC reports (Wegman). The SEC gave this responsibility to an accounting regulatory body namely, the AICPA, which established the Accounting Standards Board (ASB). The accounting profession was left to self-regulation by the ASB, which was later criticized for its lax standards. For example, at Enron's Congressional hearing, Lynn Turner, former Chief Accountant at the SEC stated that "… those standards tend to be written to protect the accounting firms in case they get in trouble on an audit ... it is not drafted with the public interest in mind" (Wegman). It is believed that, the failure of demonstrating adequate self-regulation by the accounting profession and the need for improvement led to the creation and passage of SOX (Wegman).

Another important legislation that relates to the passage of SOX is the Foreign Corrupt Practices Act (FCPA or the Act), which was passed into law in 1977 by Congress and the Executive Branch. The motivation behind this act stemmed from numerous political scandals surrounding the corruption of government officials starting in 1972. The general term that was used to describe this outrageous episode was "Watergate". In a CRS Report to Congress written by Michael V. Seitzinger (1999), attorney in the American Law Division, he stated that the FCPA was created to prohibit corporate bribery of foreign officials by American Corporations.

The section of the Act that is of most importance to the subject matter discussed in this paper is the accounting provision that required issuers registered with the SEC to maintain a responsible accounting internal control system. The Act's accounting provisions amended section 13(b) of the Securities Exchange Act. In addition, it stipulates that corporations needed to keep accurate books, records, and accounts; and made it a crime to create misleading entries and falsify financial information on a company's books. Failure to enforce the accounting laws of the FCPA led to provisions made under SOX included in Section 404. This strict legislation should help clean up the accounting industry in areas of manipulation, fraud, false financial reporting and providing deceitful information geared towards attracting investors.

Background of SOX

The Sarbanes-Oxley Act of 2002 (SOX) is said to have brought about the most significant changes of the acts referred to above. This was a bill written by legislators Michael Oxley and Paul Sarbanes that was passed into law by President Bush on July 30, 2002. It is said to be one of the toughest securities related laws since the Securities Act of 1933 and 1934. According to the Foreign Corrupt Practices Act Handbook – 2005, since SOX came into effect, "Congress, the U.S. Securities and Exchange Commission ("SEC"), the U.S. Department of Justice ("DOJ"), the Self-Regulatory Organizations ("SROs"), and others have issued more guidance on corporate governance than at any time since the Great Depression." The U.S. Securities and Exchange Commission (SEC) who sets regulations that public companies and accounting professionals must comply with enforces this act. The SEC also oversees the Public

Company Accounting Oversight Board (PCAOB) that was set up due to the SOX reform. The PCAOB role is to supervise auditors of public companies with the aim of protecting users of these companies financial information.

SOX came about due to the uprising corporate scandals that surrounded Enron, WorldCom, Global Crossing and other large public companies. These firms were involved in accounting fraud as "cozy relationships between investment analysts, auditors and corporations were tolerated while the economy and stock market were booming" (Wegman). The different issues surrounding these companies stemmed from poor execution internal controls and from providing the public with deceitful financial information. SOX was implemented to restore investors' confidence in financial reporting by public companies and reflect similar provisions mandated by the FCPA accounting provisions. "Sarbanes-Oxley not only requires enhancements to internal controls; it may also require companies to disclose in their SEC filings when they uncover FCPA violations (Wegman).

The entrance of SOX brought with it certain costs that affected public companies and the accounting profession on a whole. Studies have found that compliance costs experienced by the accounting industry have increase since the passage of SOX. Figure 1 and Figure 2 illustrate some of the costs that were found due to SOX compliance.

Figure 1

The Empirical Evidence of Compliance Costs

- Auditors face additional costs that will be passed to client firms. For example, costs undergoing quality review and rotating audit partners
- Compliance cost due to a doubling the estimate of executive hours spend on compliance activities
- Increase in cost attributable to auditors' attestations about internal controls
- The requirement that outside auditors attest to and report on managements' assessment of internal controls increase audit costs
- Higher directors fee from increased activities required of audit committee
- Litigation costs

Source: Carney, William J. (2006), "The Cost of Being Public After Sarbanes-Oxley: The irony of Going Private"

Similar results by GAO showed the following costs:

Figure 2

GAO Report

- Implementation costs of SOX internal control provision (Section 404)
- Other costs of Section 404 and other provisions of the act, which includes resources and expert limitation

- Auditing fees
- Missed "opportunity costs"

Source: GAO (2006), "Report to Committee on Small Business and Entrepreneurship",

The SOX legislation is very important to investors' and public companies. Investors seek reliable information to make important investment decisions. Non-compliance by public companies can affect their stock price, investment decisions and shareholders equity. The impact of some specific costs brought about by SOX will be noted in the next section.

The Impact of Section 404 on Small Public Companies

The major impact brought about by SOX was the high cost of compliance of Section 404 particularly for small public companies. Establishing and maintaining effective internal controls is not something new to the accounting industry. Section 404 was just a way to revive and enforce the laws of the FCPA after its failure. Section 404 of SOX refers to "Management Assessment of Internal Controls", which require managers to issue an annual report on the effectiveness of the firm's internal control and a separate report on the responsibilities of management in establishing and maintaining such controls. It is said to be the most costly portion of the SOX legislation.

Upon the enactment of this Section in 2004, small firms were the ones mainly affected. They were burdened with the cost of compliance including an increase in audit fees. For example, in her article "Surviving Sarbanes-Oxley" (2005), Amy Feldman referred to a study that was done by Nasdaq and reported that small companies were spending an average of 1.3% of their revenue on compliance. Several researchers have also agreed that this Section has added a rather significant portion of the costs to audit. There were speculations about the cost of compliance decreasing in subsequent years relying on the fact that the implementation year costs are usually higher. Research has shown that the costs have decreased in the subsequent year because of the learning curve, change in efforts, and decline in third party readiness activities (CRA International, 2006). The table below shows the results of a summary of Section 404 implementation costs for smaller and larger companies in a survey done by CRA International

Table 1 ***Average Costs Per Smaller Company***

	Year two In 000s ($)	**Year two In 000s ($)**	**Percent Change**
Section 404 Audit Fees	336	423	-20.6%
Internal Issuer and Third Party 404 Costs	524	818	-36.0%
Total Section 404 Costs	860	1,241	-30.7%
Average Company Revenue	359,680	324,230	
Total Section 404 Costs as a Percentage of Revenue	0.24%	0.38%	
Section 404 Audit Fees as a percentage of Revenue	0.09%	0.13%	

Source: CRA International, April 17, 2006

Table 2 ***Average Costs Per Larger Company***

	Year two In 000s ($)	**Year two In 000s ($)**	**Percent Change**
Section 404 Audit Fees	1,570	2,020	-22.3%

Internal Issuer and Third Party 404 Costs	3,200	6490	-50.7%
Total Section 404 Costs	4,770	8,510	-43.9%
Average Company Revenue	8,820,000	7,920,000	
Total Section 404 Costs as a Percentage of Revenue	0.05%	0.11%	
Section 404 Audit Fees as a percentage of Revenue	0.02%	0.03%	

Source: CRA International, April 17, 2006

The results of the study shows that total Section 404 cost as a percentage of revenue for smaller companies were significantly more when compared to larger companies in year 1 and year 2. Smaller companies experienced a significant decrease of .14% from year 1 to year 2 in total Section 404 costs as a percentage of revenue. Even with this decrease, they seem to be spending a substantial portion of their revenue on compliance with this section compared to larger companies.

To stay in compliance with Section 404, small companies are more likely to face internal control problems than do larger companies. For example, of the number of companies that reported internal control problems in 2004, smaller companies declared a higher percentage, which was a significant increase from 2003 (Turner, Williams, &Weirich, 2005). In addition, even though companies were aware of internal control requirements "the number of companies reporting that their internal controls were inadequate nearly doubled, from 58 in 2003 to 102 in 2004, despite earlier requirement that CEO and the CFO disclose such weaknesses, beginning in August 2002" (Turner, Williams, & Weirich, 2005). This is an indication that smaller companies find it more difficult to implement or maintain effective controls pertaining to accounting problems and auditing issues. Non-compliance could be attributed to the cost of cleaning up internal control systems, which poses a financial burden. Unlike smaller firms, larger firms have the resources and revenue to support the cost of establishing and maintaining an effective internal control system and are able to attract better quality financial experts to work for them (Turner, Williams, & Weirich, 2005).

In response to the issues surrounding Section 404, the SEC appointed an advisory panel to examine ways to relieve small companies of these costs. Based the recommendations that were made by the advisory panel, small companies were to be to be relieved of the high compliance costs based on a cap proposed. In May 2006, the SEC exempt small companies with market capitalization of $75 million from complying with Section 404, extending their cut-off date to July 15, 2007. The SEC also encouraged the Committee of Sponsoring Organizations of the Treadway Commission (COSO) to develop guidance for smaller public companies in the implementation of internal controls over financial reporting so that it will be economical to them (GAO, 2006).

Based on the exemption of Section 404 for smaller companies, there were immediate concerns. This mandate received much attention and review by both proponents and opponents of the legislation. This was evident in surveys completed and articles written on the impact of SOX. Authors expressed that small public companies are the ones that tend to become large companies, and not holding them accountable for Section 404 could prove disadvantageous to them. However, there has been some resolve that eventually all companies will have to comply

with Section 404, but the smaller public companies may have different provisions as opposed to the larger public companies. There has been ongoing discussion about different matters of Section 404. On December 13, 2006, the SEC hosted an open meeting to consider recommendations on the subject of Section 404. In the news release announcing this meeting, SEC Chairman Christopher Cox said "the Commission's proposed guidance to management is an important next step in making Section 404 of the Sarbanes-Oxley Act cost-effective and risk-based". Items on the agenda included:

1. Consideration of whether to *propose interpretive guidance to assist management in planning and performing its annual assessment of internal control over financial reporting*. This would include management of a company reporting under the Securities Exchange Act of 1934 (Exchange Act), other than an investment company registered under Section 8 of the Investment Company Act of 1940.

2. Consideration of whether to *propose amendments to Rules 13a-15 and 15d-15* under the Exchange Act that would clarify that a company choosing to perform an evaluation of internal control in accordance with the interpretive guidance noted above would satisfy the annual evaluation required by those rules (2006a).

It seems safe to assume that there will be continuous changes to this section in the future.

Section 404 is a meaningful reform under SOX despite the costs for small companies. As these companies adjust, they will see diminishing costs and begin to reap the benefits of maintaining an effective internal control system. The requirements under this section will help companies to be more aggressive in their approach to providing the general public with more reliable information, which will be useful to investors.

The Effect of SOX on Small Public Companies vs. Large Public Companies

SOX has had a profound impact on small public companies when compared to larger public companies. Before Section 404 was brought into effect in 2004, small companies had to bear the forthright costs associated with the enactment of SOX. For example, studies have shown that accounting costs increased dramatically between 2000 and 2002 due to the aftermath of Enron and the establishment of SOX laws (Carney). Since its implementation many small companies have been forced to sell their business or go private because of the cost of compliance. This was proven in a study done by Kamar, Karaca-Mandic& Talley (2006) from University of Southern California Law School. Based on the group's theoretical model of regulatory shocks and going private transactions, it was found that the cost of complying with SOX prompted small firms to sell. The study further suggested that there could be a higher probability for small firms to sell to private acquirers since the implementation of SOX when compared to larger firms. This could be due to the cost of being public, which is higher than the costs that larger firms bear; and also the benefits that they receive, which is comparatively lower than those of larger firms. The group concluded that, "the Sarbanes-Oxley Act of 2002 disproportionately burdens small firms" which is consistent with the findings of the Small Business Administration according to the U.S. Government Accountability Office (GAO).

According to Kamar, Karaca-Mandic& Talley, under their "new sales hypothesis" and "all sales hypothesis", they suggested that small firms are more likely to go private than are larger firms because of the different costs versus the benefits that are associated with being public. To corroborate the benefits of being public for a small firm versus a large firm, they cited a study done by Jain, Kim and Razaee (2004), which found that after the mandate of SOX, larger firms reaped the benefits of a larger increase in stock market liquidity. Other studies have shown that the cost of compliance for smaller firms could be more material when compare to larger firms. Furthermore, it was found that most small companies that filed to go private in 2004 were faced with high compliance costs stemming from securities laws. Such companies include Cox Communications and First Commerce Community Bankshares (Carney).

The overall cost for small companies to comply with Section 404 has had a higher percentage increase than those of larger companies. According to the GAO, in 2004, there was a growth in the percentage difference between median audit fees paid by smaller public companies as opposed to larger public companies in regards to implementing Section 404. GAO also reported that other costs associated with Section 404 and other stipulations brought about by SOX were revealed by small public companies to include use of resource for compliance rather than for business activities, resources and expert limitation, and lack of familiarity with formal internal control frameworks. Research studies conducted by Glass, Lewis and Co., showed that small public companies filed more than twice the amount of restatements compared to larger public companies (GAO, 2005). The SEC is constantly trying to address some of the concerns that smaller companies are having with Section 404 because they realize that these companies might lack a more formal or well-structured system of internal control over financial reporting as larger companies (GAO, 2005).

Other findings suggests that auditing costs associated with implementing the SOX mandate will be more for smaller companies when compared to larger companies. This is mainly because most small companies do not have enough staff to carry out the separate controls; therefore there is little segregation of duties, which can create issues resulting in ineffective internal controls. Larger companies usually operate on larger economies of scale and are able to hire more experts and maintain a more sophisticated internal controls system.

Based on the evidence we accumulated through our research, there seems to be a consensus that small public companies were mostly affected by the passage of SOX. Since small companies are disproportionately burdened, they should be treated differently than large public companies in terms of compliance with Section 404 (not exempted). This is supported by the fact that all companies are set up differently and what works for one company might not work for others. The SEC does acknowledge this and plans to provide management with assistance in performing a careful assessment of internal control over financial reporting.

The Impact of SOX on the AICPA's Code of Professional Conduct and Accounting Professionals

The American Institute of Certified Public Accountants (AICPA) is the regulatory body for all accountants that actively practice as CPAs with respects to conducting business in a professional manner and acting ethically. This institute provides representation for its members,

and set standards and requirements for practicing CPAs. They also provide other services towards the development of professionalism of CPAs, which will help them to provide quality services.

Since the passage of SOX, some requirements have changed, affecting the accounting profession. When the PCAOB was established by the SEC under the SOX mandate, it "adopted interim quality control standards that were based on the AICPA's standard". "Those standards require registered public accounting firms and their associated persons to meet the standards on Quality Control Standards and the requirement for membership in the AICPA's Center for Public Company Audit Firms" (Anonymous, 2005). Practicing CPAs are required to fulfill AICPA's membership requirement by completing a certain number of Continuing Professional Education (CPE) credits to stay in compliance with PCAOB standards. This is intended to help CPAs maintain professional competency and expertise in the practice and to stay abreast of changes relating to the accounting field. This is a great benefit to CPAs as it helps them to be more proficient in performing better audits.

Subsequent to the implementation of SOX, accountants who practice as CPAs felt pressured because they were required to do more work. The PCAOB acts as a watchdog over the work accountants now do and monitor them closely. The SOX legislation also required more work to be done by auditors, which led to the double-checking of work completed, and the performing of extra tests to take care of any loopholes. To comply with section 404, auditors will have to perform more comprehensive test of controls and substantive testing of financial statements, which adds to the firms auditor cost. According to Beck (2006), a study by PricewaterhouseCoopers (PWC) revealed that there was a high turnover rate in public accounting firms, mainly because of the long hours and the lack of compensation. At the same time, there was a shortage of qualified accountants (candidates who did not fulfill the CPA requirements) (Beck, 2006), which could be directly related to the increase in demand by accounting firms to keep up with the work load required by SOX.

New roles for auditors were brought by the enactment of SOX laws. On June 14, 2004, the SEC passed into law the PCAOB Auditing Standard No. 2, "An Audit of Internal Control over Financial Reporting Performed in Conjunction with an Audit of the Financial Statements" (AS No. 2) (SEC). This required auditors to be independent of the client they provide services to, in regards to their evaluation of internal control over financial reporting. The AICPA's Code of Professional Conduct: Independence Rule – 101 also enforce this, requiring members who practice to be independent of the person they provide services to. Other roles include the requirement that they serve as members on the clients' Board. In doing so, they are required to serve on a fulltime basis as appointed by the SEC. They also have to evaluate management's effectiveness of internal controls, which includes investigating procedures to ensure that the companies records reflect that transactions are reported accurately, provide reasonable assurance that these transactions are in accordance with General Accepted Accounting Principles (GAAP), and provide a description of any material weaknesses in internal control ("Summary," 2003).

In addition, Auditors were now limited to the amount of non-audit services they could provide to issuers. For instance, SOX Section 201 makes it "unlawful to provide services such as 1) Bookkeeping, 2) Financial information Systems Design and Implementation, 3) Appraisal

or Valuation Services, 4) Actuarial Services, 5) Internal Auditing, 6) Outsourcing Services, 7) Management Functions, 8) Broker or Dealer Services, 9) Legal services related to Audit and any other services that the Board determines, by regulation is impermissible" ("Summary," 2003).

The behaviors of accountants changed after provisions of SOX were put into place. Auditors were reluctant to provide services to smaller clients who were more likely to be at a disadvantage as they struggle towards compliance (Feldman, 2005). Seeing that many smaller clients are not able to withstand the cost of the new mandate (Section 404, audit fees and other costs), auditors are more likely to turn them down due to the extent of the work they may have to put in to clean up internal controls. Also there is a higher risk of auditing a small company because they may have ineffective internal controls.

A big issue that CPAs are faced with is the problem concerning ethics. Auditor partners (person who oversees the audit team and make decisions regarding significant problems affecting financial statements) are now required to rotate every 5 years before returning to the same client. This aim is in conjunction with upholding the professions' ethical requirement. This is supposed to discourage long-term relationships between the client and auditors to prevent collusion as in the case with Enron and Arthur Anderson. Since the implementation of SOX, CPAs have been working harder to improve their steps towards ethical behavior and conforming to the changes that were put into practice (Kroll, 2005). CPAs are transforming their attitudes towards corporate ethics and taking on the responsibility of ensuring that it becomes second nature to them. They are more instrumental in helping their client's staff in understanding and applying ethical principles in the daily activities they perform. This is a very important task for a CPA as this helps them to do their job more effectively and also helps their client in producing more reliable financial reports to the general public. The AICPA is working on helping its member CPAs to adapt to the changes and new requirements brought about by SOX.

There was an announcement that the PCAOB would hold a meeting on December 19, 2006 to include a discussion about the "New Auditing Standard to Supersede AS 2". According to a statement made by Mark Olson, Chairman of the PCAOB, "although the current internal control requirements of the Sarbanes-Oxley Act of 2002 provide great benefits to companies and their investors, the costs and the benefits are not aligned. The PCAOB is attempting to provide a much more "efficient, risk-based, scalable implementation" of the internal control requirements." ("PCAOB," 2006). Many accounting provisions have already changed. More follow-up studies can be done to note the proposals and changes that affect auditors brought about by PCAOB.

The Impact of SOX on Managers and Business Operations

Managers have changed the way they operate their business. Since the passing of SOX laws, managers have stepped up to the challenge and are becoming more active in ensuring that they play a vital role in establishing and implementing ethical policies that will resonate throughout their organization. They have been working harder to set a positive tone from the top and becoming more involved in the financial accounting aspects of the business. They are also hiring more internal auditors and accountants. As one example, a recent survey showed that 36% of companies now have a compliance officer to deal with reporting issues (Carney, 2005).

SOX affected the duties manager (CFO, CEO) have to perform in terms of business operations, by requiring them to comply with new provisions. Under Section 404 "Management Assessment of Internal Controls", managers are required to report on the effectiveness of their internal control system. "Management must now assess and make representations about the effectiveness of the internal control structure and procedures of the issuer for financial reporting" (BAPGSU, 2002). Managers will have to work hard to establish and maintain acceptable operating standards to stay in compliance.

Another important duty managers have to perform is described under Section 302 "Corporate Responsibility for Financial Statements". This requires managers to certify the company's financial statements. Managers now know that they are at high risk of losing their jobs and can end up being prosecuted if they are in violation of this provision. Therefore, they are ensuring that there are adequate controls put in place to detect fraud.

Other changes that managers had to adhere to, is Section 206 of the SOX mandate. Under Section 206 "Conflicts of Interest", the CEO, CFO, Controllers, Chief Accounting Officer or anyone in similar rank should not have had employment history with their audit firm during the first year following the audit "Summary," 2003). This is a positive move towards helping to protect the integrity of an auditor's work. Harboring noncompliance could impair the auditor's ability to be objective and thereby issuing the wrong opinions about the financial state of a company.

Managers are now working closely with auditors and providing them with reliable information because they know it will cost them if they have to issue a restatement. Also, if the auditors do not issue a clean opinion, the company may not be as attractive to investors and could deter potential investors. Managers know that providing the public with misleading information could also ruin the company's reputation, decrease investment and affect stock price.

Findings

After collecting all the useful data surrounding the impact of SOX on public companies and the accounting profession, we were not surprised by the results we found. We expected to find data supporting numerous changes brought about by SOX leading to its effect on the accounting industry and practice. The results were consistent with our hypothesis. Overwhelmingly, there was a strong consensus that the cost of complying with SOX affected smaller companies when compare to larger companies. Results show that total cost of Section 404 compliance, as a percentage of revenue was higher for smaller companies when compared to larger companies. It also showed that the costs decreased after the implementation year. These results can be found in Table 1 and Table 2.

When looking at the major cost brought about by the SOX legislation. It was found that the Section 404 mandate contributed a significant portion of these costs. These costs affected mainly the smaller companies causing some of them to sell their business or go private.

We also found that there were new roles for CPAs and managers as it relates to SOX compliance. Results from our research showed that CPAs are now required to do more work and

make an assessment of internal controls while managers have to prepare an annual report reporting on the effectiveness of the companies internal control system. This has helped to shape the behavior of managers and CPAs as they are more aware of ethical issues they are faced with, thereby recognizing the importance of acting with integrity and being independent of their clients.

Conclusions

The Sarbanes-Oxley Act of 2002 had a profound impact on public companies and the accounting profession. When a law such as requiring companies to clean up their act is put in place, someone is bound to complain. They will show discontent because they probably were getting away with a clean bill of health. Small companies were the ones that complained the most about the costs of compliance and true enough they were the ones found to have more internal control problems.

Complying with SOX proved very costly for small companies, but "cost" is a by-product of being in business. It is just unfortunate that complying with SOX seemed to be one of the highest costs many small companies had to bear. However, there is indication that it will prove less costly for them in the long run. The bright side of this is that the cost will decrease overtime because of the learning curve, and the fact that managers and continuing auditors will know what to expect. Other reasons for decreasing costs include internal control provisions that are being considered with respects to treating smaller companies differently from larger companies, and also the guidance that is provided by regulatory bodies.

Auditors cannot perform effective audits of internal control if there is no internal control. Therefore, the extension that smaller companies received for complying with Section 404 is warranted since they need more help with their internal control system.

The passage of SOX brought about new roles for managers and CPAs. Everyone is doing their part and working to clean up the system based on the new reforms. They are tackling ethical issues in their companies and taking on additional duties mandated by SOX. Transparency and investors' confidence has also increased.

We agree that even though SOX had a significant impact on the on managers, CPAs and small public companies, it was a good move for the accounting industry. It helped to enforce the accounting laws by eradicating the issues that surrounded public companies, corporate governance, and the accounting profession. The accounting industry needed improvement and with the established standards, we believe the purpose of SOX is fulfilled.

Limitations on Results

- This research took into account only domestic companies. There was no mention of how SOX impacted foreign markets or if they have legislations that parallel SOX that would have created an impact on companies.

- There was no mention of other forces outside of the costs of SOX that could have caused small public companies to sell or go private. This research only took into account the effect of SOX.
- Research was limited to the effects o SOX on public companies and did not take into account the effect on private companies.

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