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DBA Advanced Accounting

Examining the effects of the Sarbanes Oxley Act

on control methods and board member responsibility.

Dissertation Manuscript

Submitted to Northcentral University

Graduate Faculty of the School of Business
in Partial Fulfillment of the
Requirements for the Degree of

DOCTOR OF BUSINESS ADMINISTRATION

by

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Prescott Valley, Arizona
July 2017

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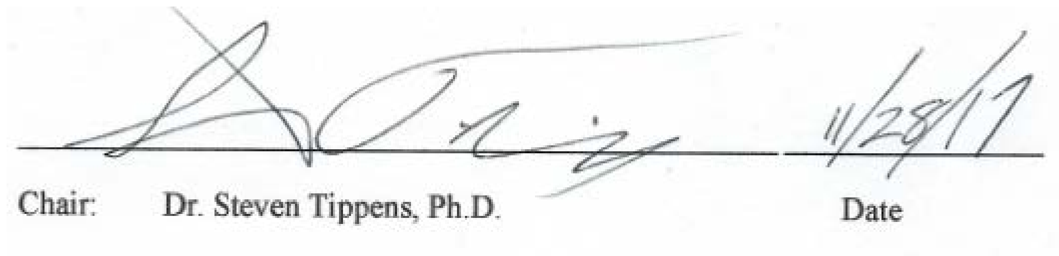

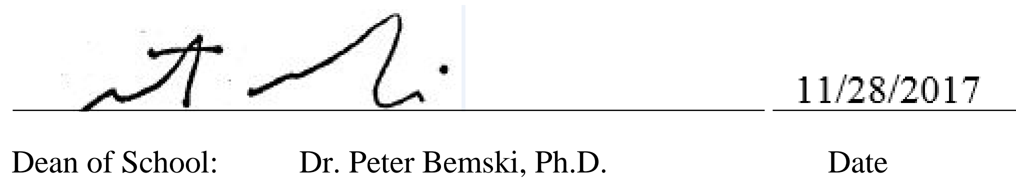

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Abstract

Auditing is an imperative part of the Sarbanes – Oxley Act, and the details related to the implementation of audit controls were the focus of this research. This is a topic area that continues to grow as quickly as the volume of auditing professionals within the industry has needed to grow. Compliance with the internal and external control provisions are crucial to ensuring the intentions of the Act are achieved rather than disregarded or evaded. This research assessed current control methods with respect to effectiveness in implementation and efficiency in handling costs to ensure compliancy with current legislation. These results can be used to provide corporate officials with benchmarks for evaluations as well as a basis for establishing a cost effective and efficient audit team. The purpose of this study was to evaluate how the cost of implementing the Act to ensure corporate compliance has affected the profitability of the firm, the board member stability of the firm, as well as the internal and external control structures of the firm over the period from original implementation to established implementation. One significant section within the Act requires the implementation of a stronger internal control and auditing structure. The analysis of corporate compliance was derived from the data collected from research using primarily quantitative methods. This analysis focused on recorded changes that have occurred with respect to audit practices, auditing staff, and corporate culture. The results from this research reflect a correlation between the costs of implementation and the level of implementation. The stronger companies spent more in staff, training, and equipment then the smaller companies. The stronger the level of implementation the less likely an incidence of fraud had occurred and the stronger the internal and external control teams were. Chief Executive

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turnover was evaluated with a P-value result of less than .0001. Administrative Expenses were evaluated with a P-value result of .0254. The “next step” would be to integrate ethics classes into the required core class structures. To ensure the success of the corporate financial structure and the success of the auditors responsible for verifying that this information is being reported accurately and responsibly, we must challenge ourselves to ensure that we continue to provide the most current information to those that are expected to make decisions based on the information they have. This applies to educational information, ethical information, and legislative information.

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Chapter 1: Introduction

The Financial Accounting Standards Board was established in 1973 as a source for the establishment of standards of financial accounting that govern the preparation of financial reports by nongovernmental entities (FASB, 2016). Additional controls were implemented with the enactment of the Sarbanes-Oxley Act in 2002 (US SEC, 2013). The establishment of the Public Company Accounting Oversight Board was one of the controls established by this legislation (US SEC, 2013). The PCAOB is responsible only to the SEC (US SEC, 2013).

The Sarbanes – Oxley (SOX) Act continues to be the subject of many research projects (Valenti, 2008; Alexander, et al, 2013; Gladstone, et al, 2016). More specifically, there are concerns from the corporate perspective that the cost does not warrant the intended benefit, and there are concerns from the investing public that the corporations are not willing to work in the best interest of the investors (Fogel, et al, 2013; Elson, et al, 2008; Kaserer, et al, 2011; Krishnan, et al, 2008). The creation of the Act came at a time when the American investing public needed to be reassured not only that Corporate America could exercise ethical choices which reflected an image of corporate integrity, but that they were not being taken advantage of and their future financial situations were not being put in a position of jeopardy. The means of acquiring this assurance came from the implementation of the Act as well as the compliance required by the corporations.

Several researchers have attempted to address the requirements of Section 404 of the Act, Management Assessment of Internal Controls, and measure the compliance

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the corporations are giving (Goh, et al, 2013; Office of Economic Analysis, 2009; Holder, et al, 2013). Questions being addressed include those similar to:

What is the benefit of complying with Section 404 as reported by company executives and internal staff (Floyd, 2013)?

What is the benefit of complying with Section 404 as reported by external auditors and other external staff (Francis, 2011)?

From this topic, other related areas of research that may be pursued include the placement of ethics classes as a requirement in all business majors, and the effect ethics classes will have on the individual taking the classes as well as the corporation that ultimately hires this individual. The implementation of the SOX Act required corporations to acknowledge their weakness in staff reporting and control as they were discovered through internal and external auditing. As corporations continue to work to become compliant with the SOX Act, the human resource team must also work to encourage strong ethical choices. Questions that can be researched for this topic cover an extremely broad area as this topic area is new and undeveloped.

Auditing is an imperative part of the Sarbanes – Oxley Act, and the details related to the implementation of audit controls is the focus of this research. This is a topic area that continues to grow as quickly as the volume of auditing professionals within the industry has needed to grow. A primary form of the research that has been and continues to be researched is related to the increase in auditing and to the cost(s) of this implementation. Studies on this topic began as soon as one year after implementation, and reports of research comparisons are ongoing through today (Bell, 2008; Fogel, 2015; Franzel, 2014; Krishnan, 2008). Concerns are for the cost to the

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companies, to the investing public, to the country, as well as to companies in foreign countries. The results of these research projects clearly indicate that the cost of implementation exceeded the expectations that were anticipated (Bell, 2008; Fogel, 2015; Franzel, 2014; Krishnan, 2008). Medium to larger companies in the U.S. can expect to lose profits for the first two to five years of implementing the SOX Act (Bell, 2008; Fogel, 2015; Franzel, 2014; Krishnan, 2008). These types of conditions create the foundations for questions such as:

- Did the implementation of the SOX Act create situations that were counterproductive?
- Does the Act discourage foreign companies from developing in the U.S.?
- Does the Act discourage smaller companies from developing in the U.S.?

Background

The creation of the Sarbanes Oxley Act by congress was not intended to create a safety net for the executive, but to create a sense of security for the investor (Lenn, 2012, p3). The Act was quickly created and implemented at a time when the United States needed to show that there would be no tolerance for incidents of a critical nature to our economy similar to that of Enron and WorldCom (Grumet, 2007, p7). Assessing the implementation of the financial disclosure and reporting portion of the SOX Act allowed an assessment of corporate transparency and accountability and how it has affected the investor, the capital markets, and the economy.

Current research related to the Sarbanes Oxley Act is predominantly related to the sections of the Act that deal with auditing, financial transparency related to financial documents released to the investing public, and internal and external control

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methods that are being monitored by the Act (Dah, 2014; Davidson, 2012; Fogel, 2015; Gage, 2015; Litvak, 2014, Jasso, 2009). This research focused on the administrative aspect of the implementation of the Act. Information related to the Chief Financial Officer and the Chief Executive Officer was reviewed to provide a base for assessment and evaluation to determine how the Act has impacted the stability of Executive Boards and the effects the Board Members have had on securing corporate positions in the market with respect to the economic stability. These assessments can also be used to determine the effectiveness of the Board Members in establishing audit standards that comply with the requirements for internal and external control methods that include internal and external audit teams. Additional research options that can be derived from this research to be considered is research that focuses exclusively on the ethical education of those entering the business and administration fields. From these fields positions for future executives, board members, and corporate officials will be filled. Positions for accountants; auditing staff, both internal as well as external; and regulatory personnel will also be filled by members in these fields. Ethics is a necessary ability that is required in any career related to the industry of finance. Ethics is a skill that needs to be taught, it should not be considered a trait that comes without some form of training.

Statement of the Problem

SOX poses a significant financial impact on internal and external control methods, often resulting in increased responsibility that must be addressed by the financial organization (Fogel, et al, 2015, Krishnan, et al, 2008, Office of Economic Analysis, 2009). The SOX Act was enacted by U.S. Congress in order to re-establish

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trust between the investing public and corporate financial decision makers (Zhang, Zhu, & Ding, 2013). However, implementation of this Act has caused boards to respond with actions that could be considered non-compliant and in opposition to the requirements of the Act at the highest level of conflict and non-compliant and evasive to the requirements at the lowest level of conflict (Sun, Lan, & Ma, 2013). Compliance with the internal and external control provisions are crucial to ensuring the intentions of the Act are achieved rather than disregarded or evaded.

Purpose of the Study

The purpose of this quantitative study was to evaluate how the cost of implementing the Act to ensure corporate compliance has affected the profitability of the firm, the board member stability of the firm, as well as the internal and external control structures of the firm over the period of time from original implementation to established implementation. This period of time was expected to differ based on the size of the corporation and the staff responsible for conforming to the legislation.

The proposed research assessed current control methods with respect to effectiveness in implementation and efficiency in handling costs to ensure compliancy with current legislation. Archived data was retrieved from corporate statements that had been publicly filed with government agencies. These statements were retrieved from corporate websites, government websites, and databases accessed from public libraries in Michigan and Mississippi as well as university databases. These results can be used to provide corporate officials with benchmarks for evaluations as well as a basis for establishing a cost effective and efficient audit team. At a time when investors were concerned about corporate fraud and greed, the Sarbanes – Oxley Act of 2002 was

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enacted (Zhang, Zhu, & Ding, 2013). There are however other effects of the implementation of the Act that contribute to the factors of compliance. One significant section within the Act requires the implementation of a stronger internal control and auditing structure. Current, as well as prior, studies are researching factors of implementation and analyzing the effects of the Act with respect to the reception of and influence on the public investors (Dah, 2014; Davidson, 2012; Fogel, 2015; Gage, 2015; Litvak, 2014). Little research is being directed toward the corporation and reception of and influence on the internal control structure. It is the acknowledged belief of Corporate America that a solution was needed to rally the investing public before an unrecoverable economic crisis developed (Jasso, 2009). The implementation of the Sarbanes – Oxley Act brought into the corporate world an ethical objective that corporations are required to address. Compliance with this objective has created other effects and recorded results that can provide data that can be compiled and assessed to determine effectiveness in ethics, market failure and success, as well as how the legal system has evolved to deal with the corporations. Insight gained from this research will be useful for auditing professionals seeking to establish benchmarks as well as for governing bodies such as the PCAOB and the U.S. Department of Justice to set thresholds for precedents.

Financial awareness is no longer confined to the accounting and auditing staff. Legal implications of the Act require corporate responsibility and acknowledgement. The series *Journal of Business Ethics* has several articles that relate to the implications of the SOX Act and the effects on corporate structure and decision making (Ekici, 2013; Floyd, 2013; Zhang, 2013). Strong advocates for ethics support the

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implementation of the Act as well as the implementation of ethics in general business education degrees (Floyd, 2013). In an attempt to control corporate bad behavior, Sarbanes – Oxley also sets the stage for the U.S. Department of Justice to prosecute federal crimes associated with the Act.

The infancy of the Act and the reasonably small amount of research that has already been done relative to the Act and the effects of the Act leave an abundance of research topics to pursue. The current information available related to the implementation of the Act and the continual revisions that have been suggested as well as implemented to assist corporations in meeting the compliancy deadline provide an overwhelming amount of information to apply to researching any of the primary topics of interest. In general, the process of compiling evidence to support a theory for a research project will provide an abundance of information to support (or refute) that theory while at the same time providing additional information for other areas that could be researched. Articles that are referenced throughout this document and are related to the Sarbanes – Oxley Act also offer suggestions for future research.

The financial burden of compliance with the Act currently discourages private held and foreign companies from becoming public held companies in the United States (Fogel, et al, 2015). The legislation in its current state requires compliance from United States companies relative to their status of being a public company in the United States. The Act also requires the implementation of stronger internal controls and auditing structure. This research project explored the control methods being implemented to satisfy compliance requirements of Section 404 of the SOX Act and the effects of the implementation as they are related to audit controls, board

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responsibility, and increased corporate expenses. The research included analyses of corporate perceived and documented compliance from an ethical as well as financial perspective to ensure compliance has been achieved and the process of compliance implemented as a routine process. Results were evaluated and used to propose appropriate procedures and policy intervention as well as recommendations for current and future audit and control personnel.

Research Questions

The Sarbanes-Oxley Act was enacted in July 2002 after several high-profile corporate scandals such as those involving Enron and WorldCom. Section 404, the focus of this research, has been viewed as a financial burden for those complying with the requirements. Reforms have been implemented in an effort to maintain the effectiveness of compliance while at the same time reducing cost.

The analysis of corporate compliance was derived from the data collected from research using quantitative methods. This analysis focused on recorded changes that have occurred with respect to audit practices, auditing staff, and corporate culture.

Quantitative:

Q1. What is the relationship between the corporate declared cost of complying with Section 404 of the SOX Act and the level of implementation of control methods and delegation of board member responsibility?

$H1_0$. The implementation of the Sarbanes-Oxley Act, specifically Section 404, is unrelated to any additional financial burden companies may be experiencing including internal or external costs of operation.

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$H1_a$. The implementation of the Sarbanes-Oxley Act, specifically Section 404, is related to additional financial burden companies may be experiencing including internal or external costs of operation.

Q1a. What correlations can be made between the cost of compliance and the level of implementation?

$H1_0$. As the level of implementation of the Sarbanes-Oxley Act increases, specifically Section 404, the financial burden companies may be experiencing including internal or external costs of operation remains the same.

$H1_a$. As the level of implementation of the Sarbanes-Oxley Act increases, specifically Section 404, the financial burden companies may be experiencing including internal or external costs of operation increases.

Q1b. What correlations can be made between the cost of compliance and the level of board responsibility and public trust?

$H1_0$. As the cost of implementation of the Sarbanes-Oxley Act increases, specifically Section 404, the level of board responsibility and public trust remains the same.

$H1_a$. As the cost of implementation of the Sarbanes-Oxley Act increases, specifically Section 404, the level of board responsibility and public trust increases.

Nature of the Study

This correlation study examined the effect that the implementation of the SOX Act had on increasing the expenditures by those who were required to adapt to the

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new regulations and the resulting net income. The assessment included the financial and staffing burden experienced by the corporations. Other variables that were considered in this correlational study were the companies that were not public and therefore not required to adapt to the SOX Act implementations or expenditures associated with the Act.

This quantitative study was used to yield information that would be summarized through statistical analysis. The numerical result of this form of study is advantageous only in the respect that it drives the researcher to formulate a plausible solution based on interpretation of the statistical data. The numerical data must be used to supplement this type of research, not govern it. Although there is documented proof (Lehmann, 2010) that the Sarbanes-Oxley Act and reforms have made a positive impact on corporate fraud and greed, this research was on other factors that were affected by this implementation related to internal and external controls. This research project explored the control methods being implemented to satisfy compliance requirements of Section 404 of the SOX Act and the effects of the implementation as they are related to audit controls, board responsibility, and increased corporate expenses. The research included analyses of corporate perceived and documented compliance from an ethical as well as financial perspective to ensure compliance had been achieved and the process of compliance implemented as a routine process. Results were evaluated and used to propose appropriate procedures and policy intervention as well as recommendations for current and future continuing education for audit and control personnel.

Significance of the Study

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The creation of the Act was not intended to create a safety net for the executive, but to create a sense of security for the investor (Lenn, 2012). The Act was quickly created and implemented at a time when the U.S. needed to show that there would be no tolerance for incidents similar to that of Enron and WorldCom (Grumet, 2007). Assessing the implementation of the financial disclosure and reporting portion of the SOX Act will allow an assessment of corporate transparency and accountability, and provide a means to show how it has affected the investor, the capital markets, and the economy. Future research should be considered that focuses exclusively on the ethical education of those entering the business and administration fields. From these fields positions for future executives, board members, and corporate officials will be filled. Positions for accountants, auditing staff, both internal as well as external, and regulatory personnel will also be filled by members in these fields. Ethics is a necessary trait that should be expected from all, not a talent that some of us have and some of us do not have.

Definition of Key Terms

Cost. Cost, as used by the researcher, includes any expenditures corporations experience that are related to becoming compliant with Section 404 of the SOX Act and may be in the form of money spent, lost revenue, employee turnover, and similarly recorded situations (Business Dictionary, 2016).

Social value. Social value, as used by the researcher, is the value received by the corporation from the public with respect to confidence in the integrity of the financial statements produced for review by lenders, securities analysts, credit rating agencies, and other investors (Business Dictionary, 2016).

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SOX. SOX is the accepted and acknowledged abbreviation for Sarbanes-Oxley Act of 2002; it is also referred to as SOX Act, Act, and the Act (Investor Words, 2016).

Summary

The theoretical foundations of this study are based on a review of old and new literature surrounding the implementation of the SOX Act. The SOX Act is currently the subject of many research projects, both finished and pending (Ekici, 2013; Floyd, 2013; Zhang, 2013). The Act is continuously evaluated for its impact on the financial market, social policy, and the law (Jasso, 2009). This paper addresses the issue of Sarbanes-Oxley achieving results to protect against market failure through the implementation of internal and external controls related to ethical corporate governance.

It is the acknowledged belief of Corporate America that a solution was needed to rally the investing public before an unrecoverable economic crisis developed (Jasso, 2009). The implementation of the SOX Act brought about an ethical objective that required corporate compliance (Floyd, 2013). Compliance with this objective has created other effects and results that provide us with data that can be compiled and assessed to determine effectiveness in ethics, market failure and success, as well as how the legal system has evolved to deal with this new enforceable requirement (Alleyne, 2013). Financial awareness is no longer confined to the accounting and auditing staff, legal implications of the Act require corporate responsibility and acknowledgement (Zhang, et al, 2013).

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Chapter 2: Literature Review

Evaluating how the cost of implementing the Act to ensure corporate compliance has affected the profitability of the firm, the board member stability of the firm, as well as the internal and external control structures of the firm over the period of time from original implementation to established implementation is the purpose of this study. The primary factors that affect the results of these research items include market, finance, ethics, and legal aspects. Secondary factors include fraud, internal control, technology, executive compensation, internal and external auditors, the SEC, the PCAOB, and Section 404 of the Sarbanes – Oxley Act. The period of time that was the focus of this research was expected to differ within a reasonable measure per subject based on the size of the corporation and the staff that is being given the responsibility for conforming to the legislation. Section 404 is considered one of the significant sections within the Act and requires the implementation of a stronger internal control and auditing structure. The reviews and results that are derived from the research of these factors are broken into primary sections that are listed under headings similar to those listed above as primary and secondary factors.

Documentation

Peer reviewed sources were gathered from the use of advanced search queries. The advanced search queries limited searches to articles that were published no later than the first- year publishing date of the original Sarbanes Oxley Act, which occurred in 2002. Searches were conducted using online library databases from Baker College, Northcentral University, and University of Michigan; as well as databases in local libraries from communities in Michigan and Mississippi. Key words used in the

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advanced search queries that limited results available included Sarbanes-Oxley Act, Sox Act, implementation of Act, auditing controls, research related to SOX, and variations that included these keywords.

Other documentation gathered was related to corporate financial history and board member employment history. Board member employment was determined by comparing lists of published board members for successive periods of time. Financial history was gathered from published financial documents retrieved from the corporate website as well as financial documents retrieved from those that were filed with the SEC. This information was compiled and evaluated in a spreadsheet format.

Timeline

In 2002, the U.S. legislature passed the Sarbanes – Oxley Act (SOX) of 2002. This Act was quickly passed as a reaction to corporate scandals that were ultimately determined to be accounting scandals; notably those related to Enron and WorldCom (Jasso, 2009). Financial statements were drafted and published that contained financial information that not only incorrectly stated the value of assets, but mislead investors to believe the company was making substantial profits and would be a profitable choice to invest in. In 2009, a Study of the Sarbanes – Oxley Act of 2002 Section 404 was conducted. This study, as reported by the Office of Economic Analysis (2009), researched the problem of Internal Control over Financial Reporting (ICFR) requirements compliance and the cost involved in obtaining this compliance. The SOX Act of 2002 had been reformed in 2007 in response to concerns that complying with internal control demands was creating cost burdens to U.S. corporations (Holder, et al, 2013). Although the associated cost varies with the size of the

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corporation, the study indicates that the compliance cost related to Section 404 compliance has declined since implementation of the reform (Office of Economic, 2009). Information received from survey participants indicates that this trend will continue. As budgetary means are established for the continued maintenance of the established control teams, internal and external, additional costs should not be a factor.

Internal controls are a significant factor in establishing integrity for a corporation's accounting and auditing staff. Internal controls affect hiring practices, financial decisions with clients and vendors, asset acquisition and sale decisions, employee expense allocations, and business disaster plans just to name a few of the concerned areas. Lehmann (2010) notes that a "strong internal control system" has been a central theme for auditing and accounting education prior to the implementation of the Sarbanes – Oxley Act of 2002. The Act, stated simply, requires the organizations to ensure that this system of internal control is in place and working efficiently. The Act does not address how this system is to be put in place, or how the internal control measures should be set up or established. The Act does address the significance of the lack of internal controls, lack of properly executed external controls, and the responsibility of the chief board member to verify accurate financial reports.

Kinney, Martin, and Shepardson (2013) found monitoring, auditing, and recording internal control design to be difficult at best and more likely impossible. Internal audits may in fact occur, but formal records of these audits do not always exist. Audit implementation was observed in the capacities of auditing educators,

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advisors to the Public Company Accounting Oversight Board, standards setter as a member of the International Auditing and Assurance Standards Board, and a Big 4 audit manager. In none of these occurrences was there any formal internal control weakness identified. The benefit of sustaining a design of internal control is lost if the design is not being implemented. Insuring that internal control is being addressed should include a formal audit disclosure.

Brown and Jones (2011) wrote a similar review regarding the intended results of the SOX Act. For those who have limited knowledge and experience in the field of auditing, the benefit of audit quality appears to be improved. However, for those who are more knowledgeable and experienced, the results are similar to those expressed by Kinney, Martin, and Shepardson (2013). Those who are experienced do not seem to generally acknowledge increased benefit or better audit quality. Although the participants in this study were college students, 73% had an Associate Degree or higher, 91.7% were currently taking classes required for a business degree, and 95.8% were currently enrolled in a business major (Brown, 2011).

The creation and implementation of the JOBS Act came in April 2012 (Townsend, 2014). This act removed, in essence deregulated, the Sox Act section 404b's mandatory requirement of obtaining an outsider audit statement assessing the reports of management. The intended result of this Act was to benefit the U.S. economy by increasing job creation and reducing cost related to regulatory compliance. The opposition to this part of the Act points out that the benefit of an outsider audit tends to overwhelmingly outweigh the cost. Outsider audits provide the benefit of increased efficiency while promoting stronger internal controls. The deregulation of this form of

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control is thought to decrease internal control measures as well as encourage the increase of fraudulent activity.

The Market Effect

Carlson and Basak (2011) use the effect of the SOX Act to evaluate the market and economic trends of small businesses. This information is derived from both old and new interviews with corporate representatives. Their research also combines information related to the social value that can be derived from compliance with the Act.

One of the debates regarding internal audits is addressed by Prawitt, Sharp, and Wood (2012) in their research regarding outsourcing and the risk of misleading or fraudulent financial reporting. The issue, also addressed by Brown and Jones (2011), was researched to examine the spillover of client familiarity. By performing the external audit as well as some non-audit services, the auditor has a clearer and deeper understanding of the client. This understanding includes general operations, internal controls, as well as financial background. The debate involves familiarity breeding higher potential for overlooking misstatements, errors, and / or fraudulent practices. Prawitt, Sharp, and Wood (2012) report that the "more work the company outsources to the external auditor, the more accounting risk decreases". The external auditor that has familiarity is not only more likely to notice misstatements, errors, or possible fraudulent situations, but because the integrity and the reputation of the auditor are subject to professional and public review, the auditor is less likely to allow fraudulent practices to go unreported.

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The act of communication is a significant factor in the establishment and maintenance of an accounting professional's image. Weber, Erickson, and Stone (2011) note that communication is required in the written form for the completion of the SOX Section 404 reports. These reports require annual notices regarding the establishment and maintenance of an adequate control system, a framework used for evaluating the internal controls, the effectiveness and noted material weaknesses of the internal control system, as well as a statement regarding the reporting on internal controls from an external auditor. An external auditor must express his opinion in a written report that is attached to the published financial statements of the corporation. This opinion can be expressed in one of four ways. The opinion can be unqualified, qualified, adverse, or a disclaimer. An unqualified opinion is the best form of opinion. This states that the auditor does not find any misrepresentation of financial information within the statements. A qualified opinion is not the best form, but it is not the worst form either. This form of opinion will state why the opinion is qualified, but the overall representation of this form of opinion is to present how the corporate financial recordkeeping has departed from traditional bookkeeping standards. An adverse opinion is the worst form of opinion. This form of opinion will reflect that the recordkeeping is not compliant with bookkeeping standards as outlined by GAAP (Generally Accepted Accounting Principles), as well as reflect a misrepresentation of the true business records in the financial statements as they have been provided. The last form of opinion is a disclaimer. This form is simply a statement that an opinion cannot be given based on the information that has been received.

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The market effect of corporate governance is expanded by Sneed, Sneed, and Boozer, Jr. (2015) to include issues related to fraud that are found in municipal governments. An implementation of a provisions such as is found in the SOX Act that could promote taxpayer trust in their governments, would lead the taxpayer to support a tax increase. An application of a SOX provision that requires structure and oversight would alert government officials, in a timely fashion, if fraudulent activity or reporting was occurring and save taxpayers money as well as time and money spent for the prosecution of fraud.

The implementation of the SOX Act has created a means by which corporate bankruptcy can be predicted (Chan, 2016). Chan and others suggest that the type of corporate scandals that led to the creation of the SOX Act should now be able to be predicted based on the reforms and disclosures that are required by the SOX Act. This type of prediction will help caution possible investors, as well as warn current investors. Firms that have weak corporate governance are often documented as having weak or poor performance (Chan, 2016).

The Ethical Effect

Many articles can be reviewed from the Journal of Business Ethics relating to the implication of the SOX Act and the effect on corporate structure and decision making. Strong advocates for ethics support the implementation of the Act as well as the implementation of ethics in general business education degrees (Floyd, 2013). Ethics should be included in the core curriculum of all business degrees, rather than as an elective that may or may not be selected as an alternate option.

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“Is the Sarbanes – Oxley Act working?” This is the broadest form of a theory for research. The implication is that a simple yes or no response is required. The Act came at a time that congress had decided they were going to crack down on corporate fraud. The Act was intended to create financial reporting transparency as well as restore investor confidence (Willits, 2014). Additional objectives of the Act included enhancing auditor independence, creating the PCAOB, and reducing fraudulent financial reporting. The Act was adversely critiqued for the cost required for little benefit received. Under political pressure to provide relief, the SEC and PCAOB implemented an amendment to the Act in 2007. An additional Act(s) created more changes to the Act in 2010 (Willits, 2014). Willits (2014) notes that the impact the Act has had on small companies has been a greater disadvantage than the impact on auditors.

Gupta, Weirich, and Turner (2013) offer an opposing theory in their article, “Sarbanes – Oxley and Public Reporting on Internal Control: Hasty Reaction or Delayed Action?” Gupta (2013) notes that although the SOX Act is over ten years old, it continues to come under attack for the “hasty reaction” to corporate fraud. The decision to amend the Act has created an escape route for “nearly 6000” companies to be released from the obligation of filing internal control attestation requirements (Gupta, 2013). The lack of acquiring this form could cost these companies the benefit of higher revenue and earnings quality. A review of history shows back as far as 1936 a need for an effective system of internal control (Gupta, 2013). Corporate fraud is recorded as far back as 1938 (Gupta, 2013). Gupta (2013) believes the possible origin of the SOX Act can be traced back to the Foreign Corrupt Practices Act of 1977. The current SOX Act of 2002 is in essence almost identical to the legislation proposed in

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1978 (Gupta, 2013). Effective internal control contributed to stock return performance. While the Act was enacted in 2002, the implementation did not occur until 2004. In just three years, 2007, an amendment to the act was being implemented. Yet again in 2010 and 2012 additional changes have been implemented.

Implementation of the Act has created consequences in other areas not directly related to the cost vs benefit scenario. As researched by Jelinek and Jelinek (2010), buying and selling accounting services has gone from "clear to complicated". The independence provision in the SOX Act takes the audit purchase decision away from the company executives and gives the decision to an audit committee. Another similar provision forbids a company from buying an audit and consultation from the same accounting firm. The relationship that had been one of a client – auditor nature has now become one of a buyer – seller nature. Additional provisions of the SOX Act address a former auditor accepting employment with a former or current client; a cooling off period is required or the auditor's firm is unable to perform the audit (Jelinek, 2010). The audit committee, less significant in the past, have now been escalated to a position that is significantly involved in auditing. The audit committee is now responsible for hiring and compensating the auditor. The auditor reports directly to the audit committee. Members of the audit committee are also responsible for disclosing their abilities as they relate to finances.

Audit fees associated with remediation of internal control weakness continue to be assessed after the remediation has been resolved (Munsif, 2011). Munsif (2011) examines the concept of "sticky fees" as they are related to firms that disclose internal control problems. In a group of 165 firms, 128 had disclosed a material weakness in

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year one. Yet all of the 128 firms continued to pay for an audit with a remediation surcharge for the next three years (Munsif, 2011). The SOX Act is criticized for excessive cost and no benefit. This is an issue of cost that is directly related to the auditor. The fee being assessed on a yearly basis is not a fair charge for the service being given, or the service being received.

Christoph Kaserer is a Professor of Finance at the Technical University located in Munich, Germany. Professor Kaserer examined the impact of the Sarbanes – Oxley Act on the cost of going public. Kaserer (2011) notes that comparing stock prices of foreign firms with U.S. firms indicates that the cost currently outweighs the benefit. Evidence can also be found that reflects an increasing tendency of public companies going private to leave the U.S. market.

While the main intention of the SOX Act was to improve corporate transparency, additional measures were established to enforce monitoring requirements. Kaserer (2011) notes the Act addresses the problem of analysts overstating the value of a company, and the Act puts pressure on the 'gatekeepers' to perform fairly. The findings reported by Kaserer (2011) regarding IPO expenses indicate that the degree of risk in this market has declined. This supports the general theory that small and risky companies would rather stay private.

Alexander, Bauguess, Bernile, Lee, and Marietta-Westberg (2013) support the theory of cost exceeding benefit with respect to Sarbanes – Oxley Act Section 404. From the perspective of a corporate insider (a surveyed group of 2901 corporate executives), the net benefit is not realized until after year three (Alexander, 2013). The first year contains a startup cost and cost that is related to implementation and

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compliance. The second year contains implementation cost, compliance cost, and any remaining auditing cost. The third year includes auditing and compliance cost. The corporate insiders acknowledge the benefit that will come with strong internal governance, but perceive the cost to ultimately outweigh the benefit (Alexander, 2013).

In a report issued by Dah, Frye, and Hurst (2014), the unanticipated effects of the Sarbanes – Oxley Act include board changes and CEO turnover. Additional research supports independent boards as better monitors. Insiders are thought to be poor monitors. Insiders are thought to better serve the company in the capacity of an advisor (Dah, 2014). The independence threshold noted for independent boards is 50% (Dah, 2014). This is considered a reference as well as a benchmark. This research suggests that firms that were considered compliant with the board independence requirement made board changes anyway immediately following the enactment of the new legislation. Creating independent boards provided the firms with a more solid monitoring system. With the board of directors as monitors, the CEO turnover frequencies for compliant firms declined. Alderson (2014) researched the benefit related to a CEO turnover. The replacement of the CEO provides opportunities related to price sensitivity. The new CEO holds less stock and is more willing to take bigger risks. Alderson points out that new managerial share ownership will create a link between the wealth of the manager and the corporate level investment that ties the interest of the manager into maximizing the company stock share price (Alderson, 2014). Alderson encourages companies to offer new managers packages that include options and stock grants. Compensation packages are the topic of the research paper,

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“Post-Sarbanes-Oxley Changes in the Composition of Boards: Have they impacted the CEO Compensation?” (Coville, 2013). The research reviews the CEO compensation packages that may relate to Sarbanes-Oxley, as well as those that may relate to changes currently occurring in the stock exchange. As noted earlier, the compensation packages are set by the board of directors. The only inside board member is recommended to be the CEO (Coville, 2013). The CEO compensation packages have been the responsibility of the board of directors prior to the enactment of the SOX Act. Equity based compensation is the primary option used with outside directors.

Financial performance is only one of the aspects that SOX influenced. Zhang, Zhu, and Ding (2013) explore the composition of the board of directors and the effects this composition could have on corporate social responsibility. Public firms are increasingly adding outside directors to their boards to accommodate independence requirements of SOX. Based on this new trend, Zhang (2013) is suggesting an update to determine how these outside and women directors are influencing the company’s performance. After developing a hypothesis and alternate hypothesis, testing the hypothesis, creating a model, and analyzing data results were arrived at for discussion and implications for future research were established. This area has limited exposure because of limited prior research. Zhang’s (2013) work shows that outside and women directors not only enhanced the firm’s management but established a moral legitimacy for the company investors.

Part of the SOX Act was used to create a ‘revision’ of the structure that had been used for the public accounting and auditing profession as well as had provided support to affirm corporate governance (Verschoor, 2012). SOX strengthened two primary areas

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related to investor protection. The first area is related to holding the CEO and CFO accountable and responsible for financial disclosures and internal controls. The second area is related to the professionalism and interactivity of the corporate audit committees. With the enactment of SOX, the public accountants were divided into auditors of publicly held companies and auditors of all other entities. SOX continues to be successful in developing corporate focus on a strong ethical culture in publicly owned companies.

The Securities and Exchange Commission's Federal Securities Acts of 1933 and 1934 and the Sarbanes – Oxley Act of 2002 are considered to be two of the most powerful pieces of legislation in regulating corporate financial representation and accountability (Alleyne, 2013). All of these Acts were developed with the intent to eliminate fraud in the corporate world. Each of these Acts was enacted after the emergence of a corporate scandal. While corporate fraud continues to be the unmanageable problem, statistics continue to rise ensuring fraud will be accounted for. Fraud is not a national problem, but a global problem. Fraud in the corporate community, or white – collar crime, is published by the Association of Certified Fraud Examiners (Alleyne, 2013). The data collected is analyzed based on the cost, victim, perpetrator, and method used (Alleyne, 2013). Alleyne defines fraud as asset misappropriation, non-asset misappropriation, corruption schemes, and fraudulent statements. Alleyne (2013) notes that asset misappropriation accounts for almost 94% of the fraud cases. This misappropriation is directly related to the position an individual has held within an organization. Statistically, Alleyne (2013) reports that, fraud is committed by males more than females and tend to be in the 41-50 age group.

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Although the implementation of the SOX Act seems to be effective in catching acts of fraud being committed, concern exists about the potential acts of fraud that the Act is not catching. Future recommendations for research relating to the SOX Act include ensuring that corporations are implementing Sarbanes – Oxley in an effective manner and ensuring auditors can identify fraud during an audit. Other areas of interest which may be researched relate to educating business students on the principles of ethics.

The effect of Sarbanes – Oxley also included financial restatements. Chakrabarty (2014) discusses concern related to institutional versus retail trades following financial restatements. Financial statement restatements are announcements that correct previously issued financial statement errors. The SEC is committed to making these financial disclosures understandable to both the average investor and the institutional investor. This study uses restatements from the period 1997-2006. Financial statement restatements are often confusing and difficult to understand. Although the intention of SOX was to make the understandability of restatements easier, the passage of SOX created a flood of accounting restatements. It is undetermined if the increased volume was related to defensive statements or restatements of a material nature. Using the data acquired, Chakrabarty (2014) can ascertain the ending result indicating that the implementation of the SOX Act and the increase in financial restatements have no effect on either of the investor groups. The article also provides direct evidence from institutional trade, summary, conclusion, and limitation.

The Legal Effect

To control corporate bad behavior, Sarbanes-Oxley sets the stage for the U.S. Department of Justice to prosecute federal crimes associated with the Act. This is

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defined as "attempts or conspiracies to commit fraud, certifying false financial statements, document destruction or tampering, and retaliating against corporate whistleblowers" (Jasso, 2009). The theory status of Sarbanes – Oxley was short lived, quickly moving to application.

Coming on the heels of the outrage of the American people, the Act was drafted, enacted, and implemented in a short period of time. "Sarbanes – Oxley Act 2002 (SOX) – 10 years later" reviews the history of corporate corruption and the legislators' response that led to the enactment of the Act (Lenn, 2012). Touted as the most dramatic change to federal securities law since 1933, the Act was created to protect investors by improving accountability and reliability of corporate disclosures. The Act requires corporate accountability that is enforced by penalties that include fines up to $5,000,000 and or imprisonment up to 20 years. The Act also established the Public Company Accounting Oversight Board (PCAOB). This board was considered by many in the accounting field as a threat. Its creation was derived by the "deep failings in the U.S. accounting ability to regulate itself" (Lenn, 2012, p. 6). Implementation of the Act was swift, and came with implementation problems. Lack of compliance was evident, and a modification to the original Act was announced in 2007. Generally speaking, the overall impact of the Act as recorded in 2012 indicates financial reports are more accurate and reliable, compliance with the Act has helped prevent or detect fraud, and investor confidence in financial reports is higher.

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increasingly adding outside directors to their boards to accommodate independence requirements of SOX. Based on this new trend, Zhang (2013) is suggesting an update to determine how these outside and women directors are influencing the company's performance. After developing a hypothesis and alternate hypothesis, testing the hypothesis, creating a model, and analyzing data results were arrived at for discussion, implications for future research were established. This area has limited exposure because of limited prior research. Zhang's (2013) work shows that outside and women directors not only enhanced the firm's management but established a moral legitimacy for the company investors.

Coville (2013) also examines a relationship related to the SOX generated changes in board composition. His investigation is related to the relationship between risk-adjusted returns and SOX; more specifically the associated stock exchange regulations. Coville and others have discussed the influence of boards of directors over the past several decades. After the influence of corporate scandals affected the Dow Jones and NASDAQ markets, the use of independent directors became a regulatory requirement. Coville establishes a primary independent variable and hypothesis. Using the data and modeled relationships, Coville arrives at the conclusion that the increased use of independent directors and independent committees has caused the risk- adjusted returns to be lower. Other factors involved in the relationship suggest that additional investigations and research should be conducted.

In a research report drafted by Foster, McClain, and Shastri (2010), the responsibility of fraud detection is under debate. Prior to the implementation of the SOX Act, fraud detection responsibility was given to both the auditor and the investor.

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In 1973, it was noted in SAS No. 1 that an entity's accounting system should prevent and detect fraud (Foster, 2010). SASs 16, 53, 82, and 99 have attempted to shift that responsibility to the auditor. The SOX Act shifted the standard setting from AICPA to PCAOB. Users view fraud detection as a reasonable expectation of audits and therefore more of a responsibility of the auditor. No significant results were found in comparing pre- and post-SOX groups until "limitations paragraphs" and "fraud wording" were included. "Users expect auditors to detect fraud" (Foster, 2010). Future research should examine the internal control report format and wording, and address the gap between auditor and user expectation.

With the enactment of the SOX Act also came the expanded legal role and authority for the Chief Compliance Officer (Silverstein, 2015). In a truly seamless corporation, the General Counsel and the Chief Compliance Officer work as a team along with the board members. It is the job of the General Counsel to be a trusted legal advisor. In his position, as senior attorney for the company, it is his responsibility to ensure the company is operating legally at all times. The Sox Act also gave the Chief Compliance Officer more authority. His job requires him to: design and implement internal controls; lead compliance efforts; ensure policies and procedures related to local, state, and federal laws are being complied with; and manage audits and investigations related to regulatory and compliance issues. The SOX Act is now a legal part of how companies are required to do business (Silverstein, 2015).

Financial Statement Fraud

Financial statement fraud creates problems in the economic world. A cause of fraud is using different methods to value assets and liabilities. Internal controls can be

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implemented to improve the processes used by management in the company which will improve the quality of the financial statements produced. While there is no fail-safe method to control the quality of a financial statement, an internal control system that includes control and compliance can detect and prevent falsification and manipulation of financial statements (Kulikova, 2016). Internal control became a popular phrase in the United States after major corporate scandals. In 2002, the United States Congress enacted the Sarbanes – Oxley Act. "The purpose of the Sarbanes – Oxley Act is to protect investors, to increase the reliability of the financial statement, which is the foundation of a prosperous economy and a developed capital market." (Kulikova, 2016, p. 93) The Act requires managers and chief financial officers to acknowledge understanding as well as taking more responsibility for financial statements. The structure of most company internal control systems includes: internal audit, revision, and risk recognition and management as depicted in figure 1. Kulikova suggests that an internal control system should include compliance – control as depicted in figure 2. Financial statement fraud is a relevant problem that exists today. Losses that are incurred from falsifying accounting data affect internal users such as the management, staff, and shareholders, as well as external users such as investors, banks, and vendors. The acts of detection and prevention are both necessary to prevent the distortion and manipulation of accounting data (Kulikova, 2016).

Making Internal Control a Priority

Internal control is necessary for all forms of organizations. Lawmakers in Indiana recently enacted new control requirements that will affect government units statewide. Just as internal control can enhance the success of a commercial

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organization, the application of an internal control system can enhance the success of a government unit. By adopting controls these government units will enhance their financial management and their overall performance (Urbanik, 2016). Legislation passed by the Indiana state legislators require new control requirements to be implemented in municipalities, county governments, schools, and local governments (Urbanik, 2016). Training must be provided to the employees that handle money in local government units. Local government managers must certify compliance with the internal control requirements when they submit their annual financial report or risk losing acceptance of their annual budgets. Challenges that are expected to the process of implementation include resistance of long-time employees to change and employees not able to understand the new processes they are required to implement (Urbanik, 2016). The approach taken by one government unit was to introduce the concept of internal control in phases. Several employee meetings were set up and training began one phase at a time. The training focused first on explaining what internal control was and how it would be implemented. The employees were given a part and told that everyone would be included. All the levels of the organization were needed to ensure that this effort would be successful. This system was not an independent task, this system was a project that required a group effort. Indiana's new system has an objective of providing accountability and transparency on behalf of the taxpayers. Government workers will use their training and new knowledge to implement an internal control system that will include control, risk assessment, information and communication, and monitoring (Urbanik, 2016).

Internal Control Weakness

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Internal control weakness is an ongoing interest for studies. Evidence compiled from the post-Sarbanes-Oxley period supports the theory that more firms are using accounting conservatism (Mitra, 2013). The study demonstrates that those firms exhibiting higher internal control weaknesses, also exhibit lower conservatism. The evidence suggests that companies that have low to no monitoring or control over their executives are encouraging these staff members to make poor financial choices. Post-SOX scrutiny has encouraged more conservatism, possibly to avoid risk related to required reports.

Applying punishment based on the crime is supported by the SOX Act in a section (406) that is devoted to establishing sentences and / or fines (Winrow, 2015). The SOX Act is clear in the guidelines that should be applied by a judge should a situation occur that needs to be resolved in the courts. The SOX Act and the revised U.S. Federal Sentencing Guidelines for Organizations were designed to work together to regulate business conduct. One intention of the SEC was to encourage the prevention of unethical behavior in companies through the creation of a code of ethics. By preventing unethical behavior, the companies would also deter the occurrence of fraud incidents.

In a study done by Lenard, Petruska, Alam, and Yu (2016), US public firms that report internal control weakness disclosures as required by the SOX Act are examined for evidence of real activities manipulation. Real activities manipulation is described as accruing smaller expense amounts, postponing or eliminating research and development projects, reducing projected budgets, or delaying or cancelling expansion type projects. These types of accounting manipulations are found to draw less attention from auditing teams, but ultimately affect the figures for successive

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years (Lenard, 2016). Lenard et al. (2016) also cite that situations of public disclosure related to internal control weaknesses force management to use real activity manipulation to lessen the negative impact of shareholder reactions. The effect on the quality of shareholder earnings is directly related to the motivation of management to use real activities management (Lenard, 2016).

The PCAOB was noted as having concerns with the training levels and experience of those conducting the audits of internal controls in one of their issued standard alerts (2013). These concerns are related to the question of appropriate experience and the application of this experience in those that are making the evaluations of material weaknesses in the company's internal controls. The PCAOB alert discusses deficiencies in auditing practices and related risks and corrective measures that should be implemented to reinforce the auditor's ability to perform successful audits as well as measures that should be followed to comply with existing PCAOB guidelines (2013).

Internal control weaknesses have also been found to be mitigated by the diversity of the board member gender. In a study by Chen, Eshleman, and Soileau the behavioral characteristics of men and women were evaluated. This evaluation was used to determine if there is a relationship between the presence of females on the board and the level of internal control weakness (2016). Women have been found to be more averse to competition and risk taking than men, as well as less overconfident and better monitors (Chen, 2016). Women bring diversity to the company not only by their behavior characteristics, but by their decision-making styles. Women are found to demand different information from top management than their male counterparts. The

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study provides support for the theory that board diversity that includes females results in “higher accounting quality and higher disclosure quality” (Chen, 2016, p. 13).

Internal control weakness disclosure is also directly related to firm investment. The SOX Act, Section 404, requires an assessment from firm management as well as the auditor on the effectiveness of internal control over financial reporting. This is also referred to as ICOFR. In a study by Sun (2016), auditor opinions on the effectiveness of ICOFR are used to evaluate the relationship between firm investment and the disclosure of the internal control weaknesses. Section 404 mandatory disclosures provide the public with information that is not available to them otherwise. The study provides evidence to support the theory that “firms that receive adverse auditor internal control opinions have significantly lower investment than firms that receive clean opinions” (Sun, 2016, p. 277). Firms that receive adverse opinions find they are susceptible to additional scrutiny and less investor interest. Firms that receive clean opinions are more likely to acquire more investor interest and less scrutiny. Those companies that can present the impression of a safe investment and a controlled financial risk are more likely to benefit from financial investment interest.

Anti-fraud provisions were tightened with the passage of the SOX Act. Firms and their external auditors are now required to include a statement of assessment of the internal control effectiveness (Li, 2016). Management is also required to make an “unaudited disclosure” about internal control effectiveness in quarterly reports (Li, 2016). Internal control weaknesses that are remedied and reported remedied produce better company stock values (Li, 2016). Companies that disclose internal control weaknesses are subject to negative market reaction.

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Internal control is historically defined as the efforts exerted to safeguard a company's assets and ensure that the accounting records are accurate (Frazer, 2016). Early audits were performed to detect clerical errors and possible fraud. Under Section 404 of the SOX Act, "public companies must attest to the effectiveness of their internal control over financial reporting when they file their annual reports" (Frazer, 2016). Section 404 highlights the connection between a strong internal control system and reliable financial statements. The corporate scandals associated with the early 1980s were found to be plagued with improper internal control. The viability of internal control is determined by the authenticity and noteworthiness of all the financial statements that are generated from all business activities of the corporation. The control environment, per COSO (Committee of Sponsoring Organizations), is the foundation for all the components of internal control. The other components include risk assessment, control activities, information and communication, and monitoring. As long as people are involved, the internal control system is subject to human error. Controls can be manipulated by a method called collusion. Active involvement by the owner can be a means of establishing separation of duties. Determination of the best internal control system must include a cost versus benefit analysis. If the cost outweighs the benefit, it is no longer a benefit. Smaller companies tend to use preventative or detective controls because they are subject to the threat of collusion (Frazer, 2016).

Security Exchange Commission (SEC)

Gietzmann, Marra, and Pettinicchio (2016) research the effect of Comment Letters from the SEC on the turnover rate of the CFO in a survival analysis. The

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analysis uses a model to determine if the CFO turnover rate increases as the number of Comment Letters received increases. Post-SOX statistics support Gietzmann et al hypothesis that Comment Letters received from the SEC increases the rate of turnover of the recipient (2016). This applies for the CFO turnover rate of the company as well as the CEO turnover rate. Comment Letters are the primary form used by the SEC to request additional disclosure information from companies. Investigations are done on a more frequent basis since the passing of the SOX Act (Gietzmann, 2016).

Technology

Mr. Rowe (2015) suggests that technology will provide a positive means of reinforcing your understanding of the relevance of disclosure as required by the SOX Act. Original reporting was done on a periodic basis. Investigations were handled randomly. Investigations could occur as infrequent as one time every three to ten years. Technology has provided a means of continuous reporting, and up-to-the-minute disclosures (Rowe, 2015). The scandals that came from lack of disclosures that ultimately led up to the enactment of the SOX act undermined the faith the investors had in the stock market. This was also a time of limited required disclosure, further increasing the doubt and suspicions of the investing market. The rules related to disclosure changed with the enactment of the SOX Act. As the realm of business relationships continues to grow and get more complicated, the laws that regulate and govern need to address these changes (Rowe, 2015). Using law and technology, a more secure environment for the investing public can be developed.

Information Technology (IT)

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To improve the quality of financial data reporting and the output of reports to benefit the company in decision making companies are investing in information technology. The investment comes at a time when information technology is being reported as an effective resource to supplement a control system (Haislip, 2016). The resource is only useful when it is supporting the control system. If the resource allows breaches to the control system, it becomes a weakness rather than an advantage. Current literature suggests that the inclusion of information technology improves operational performance of a company (Haislip, 2016). In addition, if the auditing staff is also proficient with information technology, the strength of the internal control increases. Recent research reports information technology material weaknesses could have been detected by IT auditors ahead of time if they were more knowledgeable about information technology and how it can be used with auditing. The lack of understanding exhibited by the auditor will cause the company to switch to an auditor that can understand how information technology works with financial data and control systems and has a greater IT expertise (Haislip, 2016). Just as you seek an auditor that has knowledge of your industry, you will seek an auditor that can give you IT expertise to improve your IT controls. Information technology is an area of exceptionally high risk. Internal controls are crucial to minimize the volume of IT material weaknesses. Executives as well as other staff members are promptly dismissed for instances of IT material weakness. Current research suggests that dismissed parties are replaced with more qualified individuals (Haislip, 2016). For example, an auditor that is not IT knowledgeable would be replaced with and auditor that is IT knowledgeable. The same scenario would apply for the executive or staff member. The executive or staff member

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dismissed for an instance of IT material weakness would be replaced by a new staff member that is more knowledgeable about IT control measures. The AICPA strongly recommends that auditors acquire a general understanding of how information flows through IT systems (Haislip, 2016). They also suggest that the auditor be aware of the IT system their client is using prior to their in-person contact. Research suggests that companies are more likely to work with an auditor that can work with their system and maintain the corporate control system without system breaches (Haislip, 2016). The companies are more likely to switch to a new auditor if they feel their current auditor is not knowledgeable and unable to keep their company financial information secure. Successful auditor switches will provide opportunities for the company's IT resources to advance. Testing suggests that successful auditor switches will also provide the development of better structured control systems and a decrease in IT material weaknesses within a year (Haislip, 2016).

Section 304

One of the goals of the current President, George W. Bush, at the time the SOX Act was drafted was to provide a means of retrieving any compensation given to the CEO or CFO based on information that was misstated and misrepresented the true financial positon of the corporation to the investing public (Fichtner, 2015). This specifically targeted inflating the actual value of assets as well as overstating income. Both of these measures were used as a means of showing that the CEO and/or CFO were making profitable decisions, and producing income for the corporation. Their commissions were based on how profitable they could make the business. Collectively, SOX was created with governing rules that were designed to produce reliable and quality financial

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statements and make the CEO, CFO, and auditors of a company more accountable for the financial reports they produced. Section 304 deals specifically with the processes that need to follow when a restatement is made to show a company's true financial position (Fichtner, 2015). The processes set in motion a "clawback" or disgorgement of funds that were dispersed based on inflated financial statement values. This claim process is only available to the SEC, and they do not use this resource very often. Private groups of shareholders do not have the right to take this type of claim to court. The low volume of use by the SEC to file Section 304 claims since this Act has been enacted could be related to the lack of incentive (Fichtner, 2015). Claims filed by the SEC under Section 304 do not result in any gain for the government; money is returned to the company and criminal penalties are not associated with this type of claim. Although the volume of restatements has risen since the signing of the SOX Act, the SEC has chosen to pursue only a few of the Section 304 claims available for recovery (Fichtner, 2015). The original intent of this section to "deter and punish corporate and accounting fraud and corruption" cannot be realized if the SEC does not choose to use Section 304 against all of the companies that issue a restatement because of misconduct (Fichtner, 2015).

Compensation

Another factor that could be considered a cost of compliance with the SOX Act is that of CEO compensation. Post-SOX regulatory burdens motivate corporations to develop compensation packages to retain older CEOs (Adhikari, 2015). Older CEOs are thought to have an age advantage because they are viewed as ethical, reliable, and responsible (Adhikari, 2015). Their younger counterparts are at a disadvantage because

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they are viewed as inexperienced and unknowledgeable with respect to the dynamics of handling corporate decisions. The advantage of youth is found in the labor market not in business. This same perception, or stereotype is also applied to other executive positions. Older employees are often indispensable to a firm and become a valuable commodity. Over the period of 1992 through 2012, Adhikari et al. notes the trend of CEOs age 60 or greater to increase in number (2015). While some supporting literature suggests the older CEOs try to protect their future compensation by ensuring the firm performs well and make safe decisions, others suggest the older CEOs are not affected by these concerns and make safe but riskier decisions (Adhikari, 2015). The results of Adhikari et al. findings reflect significant differences in total compensation for the CEOs. Prior to SOX compensation is noticeably lower than after SOX compensation (Adhikari, 2015). As noted above, older CEOs are thought to have qualities that motivate the corporations to offer higher compensation to retain them. The median age for Adhikari's sample group was 55 (2015).

Compensation Differential Between CEO and Corporate Executive

Research indicates that CEOs positively impact firm performance; public opinion indicates that there is growing sentiment that the CEOs are overpaid. Large compensation packages decrease the compensation available to the shareholders. Several researchers have noted that CEOs can set their own pay (Cianci, 2011). Powerful CEOs influence the board of directors into paying them whatever compensation they want to receive (Cianci, 2011). The purpose of this study is to determine how changes in the governance environment has affected executive compensation. The results suggest that the mission of SOX to alter the governance – compensation relation has not been successful (Cianci, 2011). SOX stipulates that each

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member of the audit committee be a Board of Director member and be independent. The incentives of independent directors are assumed to be more compatible with the interests of the shareholders (Cianci, 2011). Post-SOX companies have been found to be implementing changes that should continue to strengthen the monitoring ability of the boards. The Boards of Directors are larger and more independent post-SOX. The lack of relation between committee memberships and board seats supports the improved independence. Research continues to provide evidence that executives with greater power receive greater pay (Cianci, 2011). Research also supports higher executive compensation when the board is considered weak and dependent rather than strong and independent (Cianci, 2011). CEO compensation is collected from Execucomp database. Results from this study indicate that CEO dominance has increased and CEO compensation has increased at a greater rate post-SOX than pre-SOX (Cianci, 2011).

Powerful CEOs

Independent directors have been reported to increase firm value (Jiraporn, 2016). The primary focus of a dominant director is profit. The firm makes money and increases the firm self-worth and this increases the value and power of the director. Board independence has also been shown to increase firm transparency (Jiraporn, 2016). A less dominant director is team driven and provides direction rather than dominance. Costs and profits are made to be a common goal, rather than a dictated result. More independent boards lead to less powerful CEOs. The power is distributed rather than monopolized. Less powerful CEOs are less likely to take advantage of shareholders. The less powerful CEO

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wants the company to be prosperous, but not at the expense of the shareholders. Powerful CEOs are found to be inversely related to independent boards (Jiraporn).

Corporate Social Responsibility

Jian and Lee examine the relationship between CEO compensation and corporate social responsibility (CSR). CSR can be viewed as value increasing as well as value decreasing. While value increasing should be considered self-defined, value decreasing should be clarified. Although the CEO may act in a manner that would seem to increase CSR value, he may in actuality be decreasing the value. An increase in one value may create a transfer of value from one interest to another. This can occur when an over-investment in CSR transfers value from shareholders to the community or to employees. Securing personal reputations in the community or nurturing relationships with employees increase the personal value of the individual but do not add value to the company (Jian, 2015). Statistics that are relevant from this study that can be applied to the current research include the mean CEO age of 56 years and the mean CEO tenure of 12.875 years (Jian, 2015).

Internal Audit

The function of the internal auditing team continues to expand seemingly in direct proportion to the increased workload being given to the internal auditors. The internal audit team is expected to improve the organizational effectiveness in the areas of strategic alignment, risk assessment, operational efficiencies, compliance and quality assurance, financial reporting, and responsiveness (Ngah, 2016). Internal audit must play a leading role in assuring strategy is in alignment with the organization’s processes and policies. Risk assessment must include people, processes, technology, and a

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commitment from executive management. Armed with the organization's strategic direction, the internal auditor has the capability to apply basic audit principles to produce results. Public relations nightmares are derived from unresponsiveness. Audit findings cannot be ignored. Compliance issues and customer omplaints must be addressed.

Internal vs. External Auditor

The internal auditor's role in the organization gives him the advantage of familiarity. The internal auditor is familiar with the organization as well as the organizations internal controls. The internal auditor is also familiar with other staff members. The external auditor is at a disadvantage. Although the external auditor is often familiar with the other staff members, he is not a member of the staff. Although he is familiar with the organization's internal controls, he is not a part of them. The internal auditor has an established and visible connection with the organization and the staff. In an experiment created by Burt, the internal and external auditor are set up to retrieve information from a staff member (2016). The retrieval will come after the non-audit staff member voluntarily shares information. It is expected that the staff member will share information with the internal auditor because of familiarity. The experiment results substantiate the expectation and support protecting the interest of the organization (Burt, 2016). Staff members were eager to divulge information to the internal auditor, but did not want the information to go outside the organization. Negative information was withheld from the external auditor in an attempt to improve the organization's system of internal control. The internal auditor is able to obtain more,

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as well as better quality, information about control system weaknesses than the external auditor. The role of the internal auditor benefits the organization because the other employees are familiar with him and comfortable talking with him. The internal auditor is part of the organization and is considered a part of the group. Being part of the group gives him the advantage of hearing unscreened conversation. In-group members have already established a level of trust with other in-group members. The internal auditor has information relayed to him that is of a severe nature as well as information that is of a moderate nature. The external auditor is not informed of severe weaknesses and generally is the recipient of silence as a response (Burt, 2016). This information can be used to determine the strengths and weaknesses of each of the auditors. Internal auditors can be resources for weaknesses that may not otherwise be divulged. The internal auditor can also be present during the questioning process of the external auditor to encourage other staff members to be more vocal. A comparative study to determine organizational protectiveness could also be done to assess propensity of volunteers providing critical information that could be used to adjust the internal control system.

The Creation of Sarbanes – Oxley Act

Considered a milestone in corporate legislation, the SOX Act was created in a sense of urgency at a time that was considered politically and economically volatile (Kecskes, 2016). As multiple corporate scandals shook the trust of the investing public, congress scrambled to intervene. In February 2002 H.R. 3763, Corporate and Auditing Accountability, Responsibility, and Transparency Act of 2002 was introduced in the House (Kecskes, 2016). In April 2002, the Senate received the bill S. 2673, Public Company Accounting Reform and Investor Protection Act of 2002, and referred it to the

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Committee on Banking, Housing, and Urban Affairs (Kecskes, 2016). The speed at which the Act was drafted and pushed through the law-making process indicates the urgency as well as the lack of consideration for potential danger or risk of oversight (Kecskes, 2016). While the focus of the Act was on protecting investors by ensuring accurate and reliable corporate disclosures, behavior such as that leading to the corporate scandals would be subject to penalties that would involve fines, prison sentences, or both. The Act is known worldwide and directly affects companies that are publicly traded in the United States as well as all publicly traded non- United States companies that do business in the United States. The Act has been subjected to a great deal of criticism, primarily related to the "hastiness and unprofessionalism of the legislation" (Kecskes, 2016). Primary critiques include: The Act repeats provisions that are already included in other laws, the approved Act also contained "duplicate provisions on sentencing", and the cost of compliance with the Act disproportionately encumbers smaller companies (Kecskes, 2016). Criticism aside, the Act was received well by the investors and provided a means of dealing with the issues that led to the corporate scandals that could not have been addressed without the aid of legislative intervention (Kecskes, 2016).

Accounting Regulations

Many studies have been done to determine how regulations affect accounting decisions. A primary focus of these studies has been the Sarbanes – Oxley Act. The SOX Act is credited with two primary goals. The first was to create a "quasi-public institution" that would oversee and regulate auditing. This was accomplished with the creation of the Public Company Accounting Oversight Board. The second was to enlist

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auditing teams more extensively in the task of enforcing existing laws against corporate theft and fraud (Kozloski, 2016). This is being accomplished through the implementation of the SOX Act. While it is generally known that the SOX Act was passed on July 30, 2002, it is not commonly known that the Act has been enacted over a period of time. Many studies done over the first post-SOX period do not include the effects of the second post-SOX period. The results will accurately reflect the data for the one period, but will underestimate the results for the two periods combined (Kozloski, 2016). Although the SOX Act has been amended to, it has remained primarily unchanged since its enactment (Kozloski, 2016). In a lawsuit in 2010, the PCAOB was challenged and successfully defended its constitutionality.

Anti-Corruption

A recent investigation by the International Consortium of Investigative Journalists uncovered money being secretly moved to offshore companies (Morrison, 2016). This revelation was derived from more than 11 million emails, documents, and client records that were leaked from a Panama based law firm known as Mossack Fonseca (Morrison, 2016). With the probability of corruption so near, it is important for organizations to establish and implement programs of comprehensive anti-corruption compliance (Morrison, 2016). Internal auditors can use the anti-corruption maturity model, developed at Carnegie Mellon University, to determine the degree the organization is at risk as well as to determine if resources should be allocated to reduce corruption risk. The anti-corruption maturity model measures control strengths on a scale. The scale has multiple levels of activity ranking, but the size is not as relevant as the alignment with the proper risk profile (Morrison, 2016). Corruption related controls should be grouped into sections that are divided by types of risks. Auditors rate each

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control. As the controls become more complex they should be moved to higher levels of the model. The process of evaluation continues until all of the organization controls have been valued (Morrison, 2016). The maximum score that can be achieved is 68.

Financial Analysts

Section 404 of the Sarbanes – Oxley Act was enacted in 2002, but internal control reporting requirements continue to change. Accelerated filers were not obligated to comply until November 2004. Compliance for non-accelerated filers was delayed more than three times and eventually eliminated when the Dodd-Frank Act was passed in 2010 (Clinton, 2014). When the Jumpstart Our Business Startups Act was signed into law in April 2012 it allowed “emerging growth companies” to delay compliance for up to five years after they went public (Clinton, 2014). Research projects that have been completed suggest that firms with lack of internal control have less reliable financial reporting and greater information uncertainty. These qualities can impede the forecasting process of analysts. Ineffective internal control also creates uncertainty for the user of the financial statements. Analysts tend to perceive the costs of following firms with material weaknesses outweigh the benefits of covering the firms. Analysts’ coverage is found to be influenced by firm-specific factors. Material weaknesses in internal control over financial reporting are the only deficiencies that require public disclosure (Clinton, 2014). The testing results show analyst forecasts are found to be more accurate for larger firms. Analysts forecasts are less accurate for firms reporting losses (Clinton, 2014).

Analyzing Section 404

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Sarbanes-Oxley came at a time when investor confidence needed to be restored. "Without investor confidence, investment in the markets decrease, market values fall and the economy will slow into a depressive bear-market state" (Franklin, 2016). Mr. Franklin cites the history of the market after the scandals of Enron and WorldCom as examples to support his statement. Financial reporting must improve as regulation increases, as technology advances, and as the public continues to find ways to scrutinize corporate operations and finances. The task of internal control comes with the burden of considerable expense. Compliance with Section 404 involves the integration of internal controls and the staff to implement them. The staff involves internal as well as external auditing teams. Analysis provided by Mr. Franklin indicates that the costs related to the first three years of compliance for auditing fees are substantial for all public companies. The larger the company, the more substantial the audit fees being paid. The average spent on the first year of SOX implementation for audit fees for large companies was $3 million (Franklin, 2016). While additional staff was being hired to handle daily activities, existing staff was being shifted from daily functions to assisting in compliance assurance with the Section 404 guidelines. Early intentions of management were to keep internal auditing teams focused on internal control duties until they could delegate the duties to the individual department managers (Franklin, 2016). After successfully delegating the duties, the auditing teams could return to their prior tasks and ensure that the managers were maintaining internal controls. Companies expected to exert thousands of man hours to design, implement, and establish compliant activities in their first SOX year (Franklin, 2016). Costs to implement compliance were financially related as well as growth related. Resources that could

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have been used to develop or expand were used to ensure implementation was being accomplished. Although companies were working to ensure compliance, they were also working to salvage expenditures. Lack of knowledge and experience resulted in audits that did not produce intended results. In 2005, three years after the enactment of the Act, the PCAOB provided additional guidance on how to implement an internal control audit that was cost effective and would produce the intended results (Franklin, 2016). The compliance requirements of Section 404 are reviewed and it is determined that smaller companies will “face a significant challenge to comply” with the Act (Franklin, 2016). The costs were considered to be so burdensome, that companies were choosing to “de-list” or list only on foreign exchanges to escape inclusion under the Act. International companies were also subject to compliance with the SOX Act Section 404. Auditing fees recorded by foreign firms rose an average of 74 percent (Franklin, 2016). Auditing fees and compliance were related to the severity of the material weaknesses in controls. If the material weaknesses in controls were addressed and under control the audit fees would reach a plateau. If the material weaknesses in controls were not addressed and not under control the audit fees would continue to rise (Franklin, 2016).

General Literature Summary

With the implementation of the SOX Act came factors that affected how the Act was received (Lehmann, 2010, Prawitt, 2012). The Act was drafted, signed, and implemented; with little to no positive reinforcement or guidance (Taylor, 2005, Townsend, 2014, Weber, 2011). This legislation was intended to produce two immediate responses. The first was awe from the public. The market would be secure. The government was attempting to clean up the corporate act (Jasso, 2009). The

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second was expected from the corporations. Auditing and responsibility were on the agenda. It would be the responsibility of the company heads to ensure that the financial information being reported was accurate and a fair assessment of the company's current financial position (Grumet, 2007, Gupta, 2013). Many of the articles referenced have some form of application to the implementation of the SOX Act. Internal control discussed by Lehmann is imperative. If the company does not have proper control and their finances are not being accurately reflected within the company, their financial statements will also reflect inaccurate information for those statements produced for viewing outside the company. The relevance of the audits and control measures expressed in more than one of the articles encapsulates the purpose of the legislation. Legislation was created and implemented with a primary intent of securing the public interest to ensure that the trade market would not feel any long-lasting effects. The SOX Act has started the concept of corporate control and ethical reporting, but revisions are necessary to address unanticipated side effects that could ultimately destroy a smaller portion of the trade market the Act was developed to protect. Research of these side effects as well as the effect of the need for auditors and auditing staff is an area that has limited exposed review.

Ms. Miller (2015), takes the position that internal control is recommended not only to accommodate legislation, but as an effective means of cleaning up and maintaining a corporation's internal control environment. She advocates that a corporation could be putting themselves in a position of exposure to liability if they practice weak internal control measures. Ms. Miller cites five components as

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imperative parts of an effective internal control system: control environment, risk assessment, control activities, information and communication, and monitoring.

Internal controls are a critical part of the auditing field. Calderon, Wang, and Conrad (2012) cite many studies related to the examination of material weakness issues. Auditors have cited the most popular material weaknesses as accounting documentation, policy, or procedures (Calderon, 2012). These material weaknesses have been noted as the most reported for over ten consecutive years. Year-end adjustments have consistently been noted as the second material weakness for the same time period. These weaknesses lead to misrepresentation of financial statements. Reports viewed by investors must reflect accurate information for the investor to be able to accurately assess the financial position of the corporation as well as for the investor to be able to assess the integrity of the reports' preparing team.

Report preparing teams are established through guidelines issued by the Securities Exchange Commission. Ms. Martin (2015) addresses the issues related to responsibility and liability that are undertaken by the Chief Compliance Officers (CCO) in her article, "Compliance Officers". There is a fine line between acting in the capacity of a director and acting in the capacity of a supervisor. Although some of the job skills seem to overlap, acting in the capacity of a supervisor opens the CCO up for claims of liability to be made against him. These claims are not directed at the corporation, but directed at the individual. The new legislation directed at ensuring compliance from corporations has also generated a need for larger compliance departments. The compliance field has exploded with career opportunities for the individual that is trained to undertake this position that requires an understanding of compliance and risk. The

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development of a compliance program must include someone that can direct as well as enforce. Companies must hire staff that will implement plans which are "clear, fair, and contain reliable disciplinary procedures" (Martin, 2015, p. 187). The CCO should be able to enforce as well as motivate with or without incentives. Ms. Martin believes that incentives should be used as a means of motivation as well as a means of reward.

The influence of management on outside auditor selection is an external issue that is addressed in the paper written by Dan Dhaliwal, Phillip Lamoreaux, Clive Lennox, and Landon Mauler (2015). The SOX Act is very specific in directing the selection of this auditing team. The auditors are to be selected by the corporate auditing committee. Dhaliwal and others completed research that resulted in strong evidence indicating that management continues to be a strong influence, if not the choice selector, of this auditing team responsible for the external auditing. Including management in the auditor selection can create situations that result in conflicts of interest. It is difficult to anticipate a report that is unbiased when the person responsible for the draft is biased by the individual(s) who hired them.

Along the same thought of managerial influence, Peter Hahn and Meziane Lasfer drafted a document concerning the impact of foreign directors related to frequency of attendance at board meetings (2015). The key element of the document is the relation between the foreign director, the lack of attendance at board meetings, and the lack of authority that is given to the foreign director primarily because he is an unknown factor. Those who do attend the board meetings are given a limited respect for their positions as directors. Hahn and others believe that this is yet another method that management uses to influence as well as control decisions made by the board.

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Tammy Whitehouse, a frequent contributor to Accounting and Auditing, brings to the auditing community's attention what can be learned from the auditing reports produced. The reports focus on negative findings. Although the reports are supposed to point out deficiencies and concerns, it is hoped that future reports can also include a form of guidance with expanded information. The information currently cites the deficiencies. The information that could additionally be cited would include causes of negative findings; questions that could lead to answers to help resolve, understand, and correct the deficiencies; and an assessment of what the negative findings could mean for the corporation on a short-term basis as well as on a long-term basis.

Ms. Whitehouse addresses the issues related to auditing rule changes that are on the horizon in an article she contributed in 2016, "Auditing world: Focus on ICFR; Big rule changes". Although the original draft of the SOX Act was out and implemented in 2002, fourteen years later there are still sections that will be required to be integrated into the corporate auditing process. Most specifically, Ms. Whitehouse cites revenue recognition, transparency of leases, impairment of financial assets, and the classification and measurement of financial instruments (Whitehouse, 2016). The recorded declining volume of restatements indicates that the SOX Act is working, and the auditors will now be called on to substantiate the testing methods used to evaluate control with evidence.

Board independence is an issue that is under the scrutiny of the public. As an investing public, there are concerns related to truthful reporting and accurate information being expressed in the financial statements. Valenti theorizes that the strength and independence of the board directly affects the power and expertise of the

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members. The implementation of the SOX Act required the corporations to include a financial expert on their boards. Another issue addressed because of the implementation of the SOX Act was the separation of the CEO and the chair position of the board. Their issues were addressed by most companies by appointing a CPA or CFO to their boards (Valenti, 2007).

Current Reviews Related to Auditing Education

Implementation of the Sarbanes – Oxley Act has expanded the need for additional education for the student that wants to enter the field of accounting in an auditing position. Consideration has been given by educators and auditing professionals for the need to add courses to better prepare auditors with respect to the demands required by the new legislation (Blouch,2016). Current curriculum course lists are limited with respect to the inclusion of classes on how to handle the new legislation. Sarbanes – Oxley requirements are currently being taught through the process of substituting prior class material and instruction with the details of the Act and information needed by the student to make them aware of the legislation and how it was implemented as well as how the Act has empowered the PCAOB to enforce the regulatory legislation. Educators will need to work with professionals that are currently using the SOX guidelines in the capacity as auditors to assess the need for additional courses. To prepare the student for the entry level positions available in auditing the student will ultimately need to be knowledgeable with the prior standards of auditing as well as with the current regulatory demands of the Sarbanes – Oxley Act. Blouch (2016) remarks that the auditing educational programs will gradually expand to include additional classes that are specifically focused on educating the accounting student that

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is focused on entering the field in auditing with the details related to the SOX Act. The expansion is expected to include not only education on the law and
how it has and will continue to be implemented, but also case history that has had time to develop since the implementation of the Act. The student will be able to review case information to develop their own understanding of the Act and the expectations of legislation at the time the Act was drafted (Blouch, 2016).

Current Assessments of Internal Control Deficiencies

Audit deficiencies, as evaluated by Calderon (2016), are listed in Table 1. These deficiencies are noted in reports disclosed by the Public Company Accounting Oversight Board (PCAOB). Calderon (2016) believes the PCAOB as well as the auditors in the accounting profession would benefit if they understood the “dynamics” that prevent this phase of the regulatory process from succeeding. The reports are meant as a form of assessment as well as critique. Calderon (2016) also notes that auditors tend not to acknowledge the criticisms or advice from the reports. The apparent, blatant disregard to address the deficiency creates the same situation(s) because the same processes are being used and the results remain unchanged. The incorporation of the new legislation is critical in all of the accounting processes. But the focus of internal controls must be placed in the specialized area of auditing. This focus must also include overlapping communication between management, internal auditors, and external auditors.

The primary deficiencies noted in the reports related to internal controls (as depicted in Table 1) are affiliated with design issues, testing issues, and information technology. Correcting the designing and testing deficiencies are the responsibility of

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both the external and internal auditors. The controls should be managed and implemented by management, internal auditors, and external auditors. Information technology should be part of multiple management areas such as: "the office of the CEO, the offices of management team leaders, the offices of vice – presidents, etc." (Masli, 2016). Ideally, each of these positions will hold unique IT responsibilities that will work in combination with one another or collectively as a group.

Current Status of PCAOB and Rule Making Process

The creation of the PCAOB came with the implementation of the Sarbanes – Oxley Act. This regulatory unit was entrusted with the duty of ensuring there would be a uniform approach and responsibility for corporations to report their financial positions (Franzel, 2016). At the onset of the creation of this unit, it was met with opposition. The accounting professionals were now responsible for ensuring compliance from their clients as well as complying with federal guidelines to ensure financial reports were being accurately reported and financial responsibility was being acknowledged. The PCAOB is credited for the higher quality of financial reports that are being produced with respect to responsibility and accuracy. The PCAOB is responsible only to the Security Exchange Commission; but is able to ensure enforcement of the regulations through the judicial system of the United States.

The rule making process is regulated by the Security Exchange Commission. To ensure the SEC would be able to enforce the new legislation, Congress gave them additional oversight power (Kimbell, 2017). In addition to the oversight power given to the SEC, Congress also established at the same time the nonprofit entity noted above, Public Company Accounting Oversight Board (PCAOB). Although the

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PCAOB does not have any power to create rules, this unit does have the power to draft rules for submission to the SEC. This unit is a governing unit used to enforce the legislation implemented. “The PCAOB is responsible for establishing the specific requirements for internal control attestation, including audits of internal controls over financial reporting by external auditors, and for establishing controls for evaluation and classification of internal control error” (Kimbell, 2017).

The initial resentment implied by the auditing sector of the accounting community was disruptive to the implementation of the SOX Act. The Act was interpreted by many as a means of government control over another sector. The benefits of the Act for the community were overlooked at this time primarily because the probable financial effects on corporations were given primary focus. As deadlines drew near, and responsibility for financial reporting was imminent, the auditing sector began to experience the financial windfall that resulted from the implementation of the Act. External as well as internal auditing usage was increased based on the requirements of the Act. The PCAOB is currently selectively reviewing cases. The volume of compliance deficiencies grows as cases continue to be reviewed, but the volume of cases to be reviewed is declining as the corporations acknowledge the legislation and implement strong structures of internal and external control (Stefaniak, 2017).

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Chapter 3: Research Method

The purpose of case study is to understand one person or one situation. This research addressed the implementation of the Sarbanes – Oxley Act of 2002. The law was enacted to create enforceable legislation that would provide transparency and accuracy in corporate financial statements. The primary focus of this study was the effects of the implementation of the law as they are related to increased audit controls and the costs required to implement these controls. Other factors such as controlling corporate fraud and greed were only evaluated as they apply to the implementation of internal and external audit controls. The lack of internal controls was a significant factor in the scandals concerning Enron and WorldCom. The lack of external controls was evident in the involvement of a prominent accounting firm that found themselves facing charges from the federal prosecutor. These convictions were ultimately overturned, but the scandal created a disgraceful situation that ultimately ended with the firm voluntarily giving up their licenses to practice as Certified Public Accountants in the United States.

Methods of data collection for this research included obtaining documented interviews of corporate officials as well as any other appropriate written documents and audiovisual material. Written or recorded personal interviews of corporate officials and staff as well as outside auditing teams was also considered as a supporting form of data collection for the research but personal contacts did not occur. Archived data was abundantly available and this form of resource was not pursued. Analysis of data using this method would have been done by categorizing data into groups of commonalities. From this point an overall assessment would have been drawn.

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The form of quantitative method that fit this research the best was a correlational study. A correlation study can be used to identify the negative correlation between the expenditures by those that were required to adapt to the new implementations and the resulting net income. A correlation study could also identify the positive correlation between the expenditures by those that were required to adapt to the new implementations and the increase in auditing staff. Other variables that were considered in this correlational study were the companies that were not public and therefore not required to adapt to the SOX Act implementations or expenditures associated with the Act.

Quantitative studies are designed to yield information that can be summarized through statistical analysis. The numerical result of this form of study is advantageous only in the respect that it drives the researcher to formulate a plausible solution based on interpretation of the statistical data. The numerical data must be used to supplement this type of research, not govern it.

Population

The population of the study consisted of publicly traded corporations. The estimated size of the population to produce results that reflect true characteristics of the entire population was between 40 and 50 corporations. The population of this group in its entirety is approximately 3,500. Forty to fifty corporations represent 1 % of this group volume, and 10 % of the Fortune 500 group. Population characteristics included being a publicly traded corporation, gross revenue equal to or more than one million dollars, and currently having an active Chief Executive Officer and Chief Financial Officer on the Board of Directors. Using corporations from several forms of industry from this specific characteristic group allowed a representative group to be created that

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can be used to provide a result that can be used and applied to multiple business types. The actual sample size the research started with included 92 corporations. The sampling frame originated with Fortune 500 companies. The samples were selected on a random basis to produce the first sample group of 92 companies based on the position of the company in an alphabetical list.

Sample

The research included quantitative method studies. A quantitative selection was made and derived from the volume of participants required based on suggested proposals from prior research documents. All data was collected, evaluated, and assessed from historical and current market information and references were retrieved specifically for this research project.

Materials

Archived data was predominantly used. This data was collected using libraries or online websites that included individual company websites. Companies were not contacted unless updated copies of recent financial statements were not unobtainable by accessing the company website or Internet research. No personal interviews were conducted. Interviews that were archived and retrievable were used for supplemental information.

Operational Definition of Variables (Quantitative/Mixed Studies Only)

Social value

Integrity involves trust in the management of the corporation. Social value is measured by the financial involvement the public is willing to contribute to the corporation. A decline in social value can create financial hardships for the

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corporation to endure, as well as create situations of corporate bankruptcy. This variable can be measured in the financial market by credit worthiness as well as market share price. Credit worthiness can be derived from current creditors as well as public evaluators such as Dun and Bradstreet. The market share price will reflect the demand the public has for the company; the lower the price, the lower the public interest which indicates a lack of trust in the corporate ability to sustain profitability. The social value will be used in the analysis of factors related to the responsibility acknowledged by the Corporate Executive Officers, specifically the Chief Executive Officer with respect to the responsibility of financial reporting acknowledgement. The primary factors of cost, implementation, public perception and trust, board responsibility and acceptance, and specifically Section 404 of the Sarbanes – Oxley Act were considered independently as well as in combinations. The relevance of the relationships leads to a clear indication that the factors are independently relevant as well as inter-related.

Audit cost

This cost is both external and internal. This cost was measured by financial statement reportings, vendor payment records, interviews with corporate and audit staff, as well as audit records. The values derived from these reports was used to assess implication of cost factors, efficiency of expenditures over periods of time, as well as need for additional staff for compliance of implementation. The factor of cost is specifically related to the costs of implementation. These costs include (but are not limited to):

Developing an internal and external control structure;

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Training staff (including board members) to comply with legislation requirements and standards;

Establishing an audit committee, and additional audits required per legislation.

Data Collection, Processing, and Analysis

Data was collected from resources available to the public. The resources that were collected are corporate financial statements as well as statements related to the individuals that make up the board of directors. The information that was collected spanned a period of five or more years. Publicly traded companies that do not have five years or more of established financial information could not be used. The information was reviewed as processed for each company and applied to the questions proposed in the hypothesis. Answers were accumulated and reviewed to produce an overall result that could be applied to all publicly traded companies with a reasonable percent of error included. This information was collected from libraries, companies, and Internet sites that post pdf files of original documents. Results were derived from comparisons of financial statements within the company, as well as comparing lists of board members for successive years within the company. No practical comparisons were made between two different companies. Overall results were determined for each industry type as well as overall result for all companies regardless of industry type. The researcher collected, processed, and analyzed data. The calculations for sample size, confidence level, and confidence interval were determined by using an online computer program. By providing Confidence Level, Confidence Interval, and the Population available the program generated a sample size that was adequate for the Confidence Level and Confidence Interval given to accumulate what was needed to

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achieve credible and significant results for that bracket. The stronger your intended Confidence Interval, the higher the sample size required to produce a result that would continue to grow in acknowledged credibility and significance. The larger the sample size, the surer you can be that the answer(s) reflect the population you are assessing.

The sample size used to apply to the company list, using the selection process noted above, consisted of ninety-six companies being selected for the financial statement statistical analysis. From this list, eight companies were eliminated because they were listed multiple times based on stock classifications. Four companies were listed three times based on different stock classifications. Although stock classifications are relevant for investment purposes, for the purpose of this research multiple stock classifications simply refer to the same company financial documents providing separate line listings for the same company multiple times. Specific data was obtained from each company for evaluation in this research. Additional considerations for sample size are noted in Table 3: Coordinating Sample Size and Confidence Interval. History of executive board member tenure was retrieved from company websites as well as from annual documents filed with the Security Exchange Commission. Financial statements for periods prior to implementation of the SOX Act and periods after implementation of the SOX Act were retrieved to evaluate changes in expenses for administrative purposes. The administrative expense category was used to promote consistency. Expenses were subdivided into many different account names with several of the companies. All companies used the title Administrative Expenses for the category heading classification. This category included additional auditing expenses incurred and additional expenses for the extra payroll incurred for additional staff needed for the implementation of newly developed

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permanent control measures. The classification of expenses includes all of the relevant expenses needed for evaluative purposes for this research. Using the P-value as shown in Table 4, the increased expenses are found to be relevant to the focus of this research. P-value noted is equal to .00001 and the result is considered to be significant if the value is less than or equal to .05. The factor analysis table, Table 5, reflects the significance of the factors that were used in the determination and collection of the research data. Chief Executive turnover was evaluated with a P-value result of less than .0001. Administrative Expenses were evaluated with a P-value result of .0254. P-values that reflect results less than .05 are considered to be significant and support the alternative hypothesis for the research project being evaluated. For this research, the factors considered were all found to be related or supportive of each other as well as related or supportive of the alternative hypotheses. Results that are independently supported as well as support other factors are found to provide a more realistic analysis for the sample that is indicative for the larger population. P-values have been determined through Chi^2 analysis, One-Way ANOVA, and Cronbach Alpha. In each of these analyses or tests the P-value has reflected a significant result indicating support for the alternative hypotheses. Results from One-Way ANOVA Calculator are depicted in Table 6. This statistical calculation was used to illustrate the correlation and relevant significance of the expenses pre- SOX, post-SOX, and net increases between the two periods. Although the ANOVA summary of calculations reflects a significant difference between groups (F (2, 261) = 6.18014, p = .002386); it also reflects a significant result with the p-value less than .05. The factors used in this research were selected for relevance as well as significance. The p-values that were calculated from each of the statistical methods that were used further supported the

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alternative hypotheses of this research indicating positive relationships between the legislation and the costs of implementation, the legislation and the levels of public trust, and the legislation and the level of board responsibility. Each factor carries its own weight with respect to significance. The primary factors of cost, implementation, public perception and trust, board responsibility and acceptance, and specifically Section 404 of the Sarbanes – Oxley Act were considered independently as well as in combinations. The relevance of the relationships leads to a clear indication that the factors are independently relevant as well as inter-related. Further research to determine clear thresholds of relevance should be considered for additional evaluative purposes. The factor of cost is specifically related to the costs of implementation. These costs include (but are not limited to):

Developing an internal and external control structure;

Training staff (including board members) to comply with legislation requirements and standards;

Establishing an audit committee, and additional audits required per legislation.

The factor of implementation is exclusively related to establishing practices as required by law to ensure that the corporation is acting in a legal capacity with respect to financial reporting. The factor of public perception and trust is evaluated based on the market share price of the corporate stock. It is assumed that the value of the stock will rise if the stock is in demand, and the value of the stock will decline if the stock is not in demand. If the public perceives the corporation to be in a state of financial risk the stock will not be in demand. If the public perceives the corporation to be a safe investment the stock will be in demand. The factor of board responsibility and acceptance is also

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measured by the level of implementation of the legislation. The corporate boards that accept the responsibility for the actions they are legally bound to comply with will have the support of their investors and employees. The corporate boards that do not accept the responsibility for the actions required by legislation will create a situation of chaos, turnover, and possible disruption in daily business practices. The factor of Section 404 of the Sarbanes – Oxley Act is the element of the legislation that requires assessment of adequacy and effectiveness of internal controls and procedures. This assessment must be written, published, and included with annual reports. This assessment must be done by corporate executive officer as well as the corporate registered accounting firm.

While each of these factors carry a significant impact independently, the combination of any two factors also carries significant weight and should be given relevant consideration. You can use an exploratory factor analysis to test a new scale, and then move on to confirmatory factor analysis to validate the factor structure in a new sample such as hypothesis testing to determine 'goodness of fit' with the values.

Assumptions

It is assumed that the corporation is publicly traded if the corporation is listed on the NYSE. It was assumed that all corporations meet or exceed one million dollars in gross revenues if they were included in the research study. This volume of revenue was verified by financial statements retrieved from company websites and / or retrieved from SEC file documents. It is assumed that each included company has a board of directors

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with an actively participating Chief Executive Officer and an actively participating Chief Financial Officer.

Limitations

The primary limitations are related to financial statement reporting accuracy. Based on current regulations it is anticipated that this type of reporting will be governed by law. All data that will be collected will have been published and available to the public for their review. A secondary limitation, still within the financial statement group, is the description used for reporting individual expenses. Although the expense of the most concern is those expenses paid for accounting purposes, many corporations do not report each expense item independently but rather in a group. For purposes of evaluation, the group the accounting expenses were reported in was used for each company included in the research sample. The expenses for the financial purposes were consistently grouped together to mitigate an extreme effect thereby reducing a threat to the validity of the overall results.

Delimitations

Choices made to narrow the scope of publicly traded companies include: five years of active business, up to and including the current year; gross revenue equal to or more than one million dollars; and an active board of directors. Five years of active business was required to establish a baseline for expenses and a determination of an increase or decrease in expenditures. Gross revenue threshold was required to accommodate the requirements stipulated in the Sarbanes – Oxley Act. An active board of directors was required to determine employment stability within the

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executive board members and the affect the financial reporting responsibility had on the level of implementation.

Ethical Assurances

No informed consent procedures were needed. Data collected was retrieved from archived sources. Data collected was obtained from public sources and no confidentiality measures were needed. Data collected had been submitted to public sources and was retrievable without solicitation necessary.

Summary

The creation of the Act was not intended to create a safety net for the executive, but to create a sense of security for the investor (Lenn, 2012). The Act was quickly created and implemented at a time when the U.S. needed to show that there would be no tolerance for incidents or scandals similar to that of Enron and WorldCom (Grumet, 2007). Assessing the implementation of the financial disclosure and reporting portion of the SOX Act allowed an assessment of corporate transparency and accountability. This provided a means to show how the Act has affected the public-sector factors that include the investor, the capital markets, and the economy; as well as the professional sector factors that include accountants, auditors, and corporate executives and board members. Based on these assessments, accounting methods and practices can be adjusted to ensure that the professional sector is compliant with the legislation requirements while the public sector is protected to prevent economic depressions and stock market crashes. Costs related to initial implementation should not be considered ongoing factors; costs related to continued use should be budgeted as an ongoing factor. As corporations continue to utilize their developed control teams, it is expected

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that their costs for these teams will decline or remain constant. Information that has been referenced prior indicated that the factor of cost declined after the internal and external control teams were trained and implemented.

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Chapter 4: Findings

While there are many studies that are researching factors of implementation and analyzing the effects of the Act with respect to the reception of and influence on the public investors (Dah, 2014; Davidson, 2012; Fogel, 2015; Gage, 2015; Litvak, 2014); little research is being directed toward the corporation and reception of and influence on the internal control structure. The purpose of this study was to evaluate how the cost of implementing the Act to ensure corporate compliance has affected the profitability of the firm, the board member stability of the firm, as well as the internal and external control structures of the firm over the period of time from original implementation to established implementation. The primary focus of the results of the impact this legislation has had on the investor has generated other effects that are directly related to the corporate methods being used to implement the Act. These effects contribute to the results that are being achieved and should be acknowledged as factors rather than being overlooked. The period of time that is being evaluated was expected to differ based on the size of the corporation and the staff responsible for conforming to the legislation. The Act has had several amendments to provide corporations more time to deal with the implementation deadline. One significant section within the Act requires the implementation of a stronger internal control and auditing structure. Section 404 mandates this implementation to be established by all publicly-traded companies. Internal controls and procedures are required for financial reporting. These controls and procedures must include documentation as well as testing and maintenance of the controls and procedures to guarantee they are consistently effective. The level of

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implementation of the requirements of this section can be measured by the reduction of corporate fraud incidents.

Compliance with this objective has created other effects and recorded results that have provided data that was compiled and assessed to determine effectiveness related to ethics, market failure and success, as well as how the legal system has been given additional authority to deal with the corporations; specifically dealing with those that do not comply with legislation requirements. Insight gained from this research can be useful for auditing professionals seeking to establish benchmarks as well as for governing bodies such as the Public Company Accounting Oversight Board and the U.S. Department of Justice to set thresholds for precedents.

Results

Resource documents were retrieved from company websites, library databases, and government databases. The documents were catalogued based on relevant material and statistical information that was gathered from each. The material was handled in a consistent and secure manner to maintain the integrity and consistency needed in the development of research results. All relevant material was evaluated and summarized. Points and counterpoints were reviewed and evaluated for inclusion as items of support or opposition. Spreadsheets were utilized as templates for the collection of volume data as well as resources for the drafting of comparative graphs for result interpretation. Only publicly traded companies listed on the NASDAQ list were used. Only companies that were required to comply with the Sarbanes – Oxley Act and the additional reforms implemented were considered for inclusion in this research. Section 404 of the Sarbanes – Oxley Act lists guidelines that dictate the requirements for publicly traded companies

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that must comply. The companies that were used were also companies that had financial history before and after the implementation of the Sarbanes – Oxley Act. Companies that did not have financial history prior could not be used because of the lack of available comparative information.

Companies were selected from the NASDAQ listing on a consistent but random basis. The first selection consisted of three companies per every hundred and were selected based on the company placement in the NASDAQ list. The numbered position the company was listed in was selected prior to obtaining the list to remove as much bias as possible. An additional three companies per every hundred were selected for inclusion in the same manner for two purposes. The first purpose was to have a secondary set available should the first set have too many names removed because of conditions that were established. The second purpose was to build a larger sample with respect to the overall question of administrative costs increasing or decreasing. The same position within each hundred names was used, a similar selection process is depicted in the table labeled Table 2. The company that was listed in the noted position was then evaluated for inclusion in the research process based on the requirements noted prior: financial history before and after the implementation of the Sarbanes – Oxley Act.

Resource documents were collected from company websites as well as retrieved from the Security Exchange Commission bank of annual reports that are posted for public review. Company financial history was also retrieved from the library databases of Northcentral University, University of Michigan – Flint, Baker College – Flint; as well as local library databases from the libraries located in Flint, Michigan; Clio,

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Michigan; and Kosciusko, Mississippi. Resource documents included financial statements for all companies included in statistical computations as well as any material related to board member history and the development of internal and external controls that are being used to ensure corporate compliance of Section 404. Interviews and any direct additional information were not sought from any specific corporation. Research resources were comprised entirely of financial histories and board member histories retrieved from company websites, government websites, and educational and public library databases. General information related to implementation of Sarbanes -Oxley Act was retrieved in media as well as written form. Media forms were confirmed with a written source. Media forms obtained included clips posted on the Internet in audio as well as video form. Transcripts for these forms of reference material were used to support the accuracy of information referenced from these sources.

Evaluation of Findings

Q1. What is the relationship between the corporate declared cost of complying with Section 404 of the Sarbanes – Oxley Act and the level of implementation of control methods and delegation of board member responsibility.

$H1_0$. The implementation of the Sarbanes – Oxley Act, specifically Section 404, is unrelated to any additional financial burden companies may be experiencing including internal or external costs of operation.

$H1_a$. The implementation of the Sarbanes – Oxley Act, specifically Section 404, is related to additional financial burden companies may be experiencing including internal or external costs of operation.

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The relative significance of the results for the first question posed in the research clearly indicted by the "p-value" calculated rejects the acceptance of the null hypothesis in favor of supporting the alternative hypothesis. Pre- and Post-SOX expenses along with recognized expenditures in implementing the SOX legislation and reforms as they occurred are sufficiently documented and provide results that reflect a direct correlation between the expenses incurred and the legal requirements that had to be accommodated at the time these expenditures were noted. Both the chi-square test and the one-way ANOVA provided "p-values" to support the acceptance of the alternative hypothesis as well as reject the null hypothesis.

Question two is addressed by the correlation of expenses as reported in the correlation tests.

Q1a. What correlations can be made between the cost of compliance and the level of implementation?

$H1_{0.}$ As the level of implementation of the Sarbanes – Oxley Act increases, specifically Section 404, the financial burden companies may be experiencing including internal or external costs of operation remains the same.

$H1_{a.}$ As the level of implementation of the Sarbanes – Oxley Act increases, specifically Section 404, the financial burden companies may be experiencing including internal or external costs of operation increases.

As implementation becomes an obligation as required by legislation, reports of expenses are reflectively increasing within the administrative expense category. The

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correlation of expenses and the supporting test values, specifically the p-value, substantiate and support the acceptance of the alternative hypothesis for Question number 1a and reject the null hypothesis. Although several of the companies did reflect a decrease in expenses related to administrative issues, this was not the norm and the preponderance of companies reflected an increase in administrative expenses. Question three is uniquely answered by the statistical test that provided a Cronbach Alpha of .6203.

Q1b. What correlations can be made between the cost of compliance and the level of board responsibility and trust?

$H1_{0.}$ As the cost of implementation of the Sarbanes – Oxley Act increases, specifically Section 404, the level of board responsibility and public trust remains the same.

$H1_{a.}$ As the cost of implementation of the Sarbanes – Oxley Act increases, specifically Section 404, the level of board responsibility and public trust increases.

This statistic favors the rejection of the alternative and the acceptance of the null. The best result of the Cronbach Alpha for supporting the alternative would be a result of .70 or higher. This test also provided a t-value of 5.2 and a p-value of $< .0001$. The p-value contradicts the rejection of the alternative hypothesis. A P-value that is less than .05 indicates strong evidence supporting the alternative hypothesis. This is indicative of a strong relationship between Chief Executive Officer tenure and company stability with respect to ongoing investor faith and financial stability during a time when the company

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is maintaining a positive bottom line while paying to accommodate new mandatory legislative financial requirements.

Summary

The results obtained through statistical development were both supportive to existing ideals expressed through many literature pieces reviewed during this research and supportive to the new situations. Cost continues to be the primary consideration, both in past assessments as well as in future analysis. The development of an internal control system is a necessary action for the cost of implementation of legislation related to financial reporting of the corporation to become manageable. In addition, the development of a relationship between internal and external auditing controls is imperative to ensure that this expense is beneficial to the corporation rather than simply an additional cost to bring down the company's net income as well as creating a burden to the human resource department with constant turnover in staff and continuous cycles of training. The development of internal and external controls in publicly traded companies has also promoted the development of tenure among the executive board members. The information collected to produce the relative statistical analysis between the demands of implementing the Sarbanes – Oxley Act and the turnover rate produced an analysis opportunity for tenure of the executive board members and the increases in their pay based on the level of responsibility they are required to acknowledge. Although smaller companies do not reflect substantial amounts of salary increases during the biggest phase of the implementation of the Act, the overall trend of salary increases applied to all company sizes. Most companies were willing to pay their chief

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executives more to keep them rather than take the risk of losing them. The level of increased responsibility and knowledge the chief executive officers and chief financial officers are expected to have with respect to financial reporting is evident in the letters of acknowledgement that must come from them that must be included with the corporate year-end financial statement bundle. Ignorance is no longer an acceptable justification for inaccurate reporting of financial information.

The development of these new situations goes beyond the hypothetical indicating that there are correlations between the development of financial control expenses and the higher level of ownership for those that have become responsible for not only handling the receipt and disbursement of the funds to manage these expenses, but being able to responsibly provide an accurate financial report. As the board members, specifically the Chief Executive Officer and Chief Financial Officer, are becoming more involved in how the finances are handled and more importantly how they are reported, it is imperative that the correlations between costs and implementation as well as costs and ownership of responsible reporting are made more obvious for internal as well as external developments to continue in the accounting field communities. This is an implied conclusion with a recommended action for response to follow that has already affected the auditing sector of accounting with a strong impact. The original expenditures for the development of internal and external controls and the training required for the staff members that are responsible for the implementation of these new programs are beginning to level out for the bigger corporations. The control measures are becoming more routine and established and the initial expenditure budgeted to ensure implementation by the declared legislation date are now a permanent part of the budget

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to ensure the continued success of the internal control teams as well as the development of communication between the internal control teams and external control teams. As internal control teams continue to grow stronger, the residual effects will either support or hamper the effects and efforts of the external control teams. Conflicts between the external and internal control teams could adversely affect the development and growth of the auditing sector as a whole. Continual monitoring and strategic adjustments will need to continue to ensure these teams continue to work together.

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Chapter 5: Implications, Recommendations, and Conclusions

Implications

Question One

Relationship between the corporate declared cost of complying with Section 404 and the level of implementation of control methods and delegation of board member responsibility. The results derived from the statistics and analysis supported the alternative hypothesis: the implementation of the Sarbanes – Oxley Act, Section 404, is related to additional financial burden companies may be experiencing including external and internal costs of operation. The results also rejected the null hypothesis: the implementation of the Sarbanes – Oxley Act, Section 404, is unrelated to any additional financial burden companies may be experiencing including external and internal costs of operation. Costs to consider to implement the legislation by the amended legislation deadlines include additional staff, possibly additional equipment, and additional outside staff to perform external control tasks. Fees being paid for accounting, auditing, and outside professional fees escalated during the primary time when legislation called for implementation of the Act and professed to initiate sending out penalties for those that did not comply within the deadline given. Outside auditing teams are required to review and give a stamp of approval on the financial reports before they can be submitted to the federal agencies. Companies were now responsible for obtaining an external accounting firm or accountant to substantiate the validity of their financial reports as well as hiring an internal team to ensure and develop a strong internal control network that included the Chief Executive Officer and the Chief Financial Officer. The cost was an obvious reported expenditure and the administrative expense account

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increased as quickly as the costs were being billed to the company. In addition to the added expense of additional staff, additional responsibilities had been handed to the Chief Executive Officer. Ignorance is no longer an excuse for not understanding what is being reported by your accounting staff. The implementation of the Act made it the legal responsibility of the Chief Executive Officer to ensure that he is knowledgeable about the financial reports he is ultimately responsible for signing and filing with the SEC as well as providing to the investing public for their review. To maintain continuity with the company, Chief Executive Officers were encouraged to remain with the company. Part of the administrative expenses that increased included the salaries of executive board members. Another statistic that supported the longevity of the Chief Executive Officer was the low rate of turnover. One of the reasons that this position was not in a state of turmoil from constant changes was the primary ownership. Throughout the process of collecting data, it was discovered that many of the companies listed on NASDAQ are smaller companies (with respect to employee volume) that are publicly traded, but a substantial volume of the stock is privately owned stock. The chief Executive officer of these companies is usually part of or related to the company originating team that has had the company passed on to him; or the shares of the company transferred to him from a predecessor.

Question Two

Correlation(s) between the cost of compliance and the level of implementation. The results derived from the statistics and analysis supported the alternative hypothesis: as the level of implementation of the Sarbanes – Oxley Act, Section 404, increases, the financial burden companies may be experiencing including internal and

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external costs of operation also increase. These results also rejected the null hypothesis: as the level of implementation of the Sarbanes – Oxley Act, Section 404, increases, the financial burden companies may be experiencing including internal and external costs of operation remain the same. These results were derived from Chi^2 statistics as well as ANOVA statistics. As the data was being compiled, prior to statistical assessment, the comparison of categorical expenses from pre- and post- SOX implementation with respect to administrative expenses was an obviously greater amount for the majority of companies for the post-SOX accounting period. The difference was consistently larger for a substantial amount of the companies, noticeably larger for many companies, and smaller for a few companies. It is relevant to note that the expenses that were posted for the administrative category did not continue to grow for all companies, many of the larger companies stabilized and the expenses leveled off and remained similar for several years after their obligations to implement internal and external controls for accounting were met. This could be the result of many factors, but the isolation of expenses in the administrative area allows the expenses that are related to the implementation of the legislation such as additional staff and training to be lumped together thus giving the opportunity to compare similar expenditures that would normally fall into the same category. The expenditures were unsurprisingly higher based on the status of the company with respect to business sales volume and business wealth. The level of implementation the companies were responsible for was also based on business sales volume. Many of the smaller businesses opted out of the higher levels of internal control and continue to pay to "patch the hole" instead of fixing it. In the short term the smaller businesses are saving money, in the long term this method will

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cost them more than simply implementing a solid structure that works in the beginning. With either scenario, the costs of operation are predominantly increasing as noted in the alternative hypothesis.

Question Three

Correlation(s) between the cost of compliance and the level of board responsibility and public trust. The results derived from the statistics and analysis supported the alternative hypothesis: as the level of implementation of the Sarbanes – Oxley Act, Section 404, increases, the level of board responsibility and public trust increase. These results also rejected the null hypothesis: as the level of implementation of the Sarbanes – Oxley Act, Section 404, increases, the level of board responsibility and public trust remain the same. Although the results supported the alternative hypothesis, the data collected was not as obvious in providing a supportive result in the raw form. The three factors together support the alternative hypothesis as the cost of compliance increases the level of board responsibility for written financial reports also increases. As these two factors were increasing, so was the market share price of the publicly traded company increasing. As the investing public appeared to take a renewed interest in publicly traded companies, the stock values increased providing support for the trade market as well as the economy in general.

Discussion

The scandals that evolved from the incidents similar to that of Enron and WorldCom created "stock market scares" of impending market crashes or economic depression (Grumet, 2007). In an effort to head off a stock market crash and/ or the associated economic depression, the Act was quickly drafted and implemented.

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United States Congress used their legislative powers to show a unified congressional front that would not stand for or show any tolerance of incidents such as those and put corporations on notice that they would be held accountable for accurate and ethical financial reporting or be faced with legal consequences that included fines and possible penitentiary sentences. The Sarbanes – Oxley Act is considered one of the fastest pieces of legislation to be drafted and signed into law in one of the shortest periods of time. Following the implementation of the financial disclosure and the reporting portion of the SOX Act a sense of corporate transparency and accountability was created. This renewed sense provided a means to show the investor, the capital markets, and the economy that corporations can be controlled and can deliver accountability in the form of ethical and accurate financial reports.

The literary consensus that the burden of the cost inhibited many companies from implementing the Act sooner is supported by a preponderance of data that reflects exactly that. The cost of adding staff for the purpose of an internal control team, the additional cost of training the extra staff, and the extra fees connected to external requirements and additional professional fees substantially support all of the alternative hypotheses. Although a small portion of the available companies listed on the NASDAQ corporate list were used, the data collected from these companies was collected in a random way and provided results that could be representative of any of the other companies on the list.

The original interest in the Act was developed at a time that the Accountants and Auditors seemed to be benefiting from the “required” external audit needed for the

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financial statements to be released. What had been a yearly, reasonable audit with respect to time and money had turned into a golden opportunity goose. Popular opinion among accounting professionals was antagonistic toward the group that was now going to “monitor” their activity to some degree (PCAOB). The communication between groups has evolved to a better position. There is a mutual understanding about the expectations of the PCAOB among corporations as well as the auditing teams. While the level of expenses being paid was reasonably easy to ascertain, the longevity of the Chief Financial Officer was moderately easy to acquire, there were other factors that needed to be pursued that were not. The direct connection between expenses and implementation is easily attributable to the enactment of the legislation. Stock prices are also an item that can be retrieved as needed to substantiate the potential economic crisis that was averted. Information that is not easily acquired, if at all, is the information related to the ethical education and application of those in a position to use it. This information is un-retrievable from a database or Internet search engine. This information would be most likely attained through a personal interview or survey. This type of information could prove to be very helpful with respect to the development of control crews. The establishment of an ethical standard is an important detail that should be addressed and included in the implementation of a control team that is expected to act in a proprietorial manner that is in the best interest of the company. This is one item that should have been included as well as more developed within the Sarbanes – Oxley Act.

Another area that has not received a great deal of research or active attention is the legal power that has been established through the enactment of the Public Company Accounting Oversight Board. As this is a new area and the judicial system has not been

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used by exercising their authority in the capacity they could have, there is limited information available for or against the power they have. This is currently an extremely gray area. Very little reporting has been done in favor or against the control measures this panel has available to them to use to ensure compliance with the legislation. New cases will establish precedents as well as need to be used to set precedents for future trials. The detailed case information can also be used to educate future accountants. Prior controversy between management accountants and financial accountants should also be evaluated to determine what basis each has when attempting to represent their group at a disadvantage when addressing the Public Company Accounting Oversight Board. While the level of support from the general public has appeared to be flourishing, based on market transactions and the corporate stock prices; the level of support from the accounting-auditing sector appears to have been scaled back. Auditors, initially supportive of the implementation and the additional fees that they can charge, must now also consider the additional responsibility they are being required to handle by acknowledging established procedures, protocols, and implementations that have been developed with the sole intent of ensuring compliance with legislation.

Another factor that should be given a great deal of consideration is the development of a string of classes related to ethics, ethical standards, and how they go together for future auditing students as well as any student interested in getting education in a field related to finance. The accounting field in general respects the ethical factors involved in making choices, the relevant question for this group is are they impelled to make their choices with ethics as a consideration. Does the factor of ethics supersede the factor of financial gain? This is an area that is currently

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speculative, no significant research has been done on this topic. As well as no significant research has been done on the topic of creating a subsidiary curriculum of ethical classes. The development and establishment of this curriculum could be added to all of the financial programs currently available for all of the colleges that offer you a chance to “make a difference”.

Recommendations

The scope of this study involved three specific areas of interest: cost, implementation, and responsibility related to Sarbanes – Oxley Act. A broadened exploration of this research would illuminate in greater detail the legal responsibility that is attached as well as the legal expectations you may have to deal with if you find yourself fighting the judicial system. The legal ramifications of this Act are extremely cumbersome as well as difficult to assess because of little to no prior history. A more thorough understanding of these legal guidelines would further illuminate how fraud and fraudulent reporting is handled. Additional studies, or a follow-up study could be conducted on fraud incidents and how these incidents have been handled in and/or out of the court system. These incidents of fraud could also be used to develop a required course plan to be included in the curriculum for college business students. Ethics is an issue that is often overlooked as a teachable subject. Ethics are an imperative factor in the development of internal controls in a business. Corporations do not want to have among their staff an individual that is not trustworthy or is capable of performing a fraudulent act.

The results received from the analysis of the collected data supports all alternative hypothesis of this research. Gradual implementation of the Sarbanes – Oxley

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Act allowed many of the corporations an opportunity to spread out the costs to establish an internal and external control team over several years. The costs related to the implementation are significantly related to auditing. While the Act has guidelines that must be adhered to based on the significant volume of costs, recommendations for gradual implementations of the Act is advantageous from a financial perspective. Legal perspective may outweigh the financial perspective and implementation may need to occur at a faster pace, but internal control team members should be given a more relevant consideration than external control team members. Internal control team members are more invested in the company. External control team members are often contracted staff such as external auditors and have no vested interest in any one particular company.

Relevant policy and procedure protocol should include ethical evaluations as well as a thorough discussion on what is legally expected from team members. Break downs of levels of responsibility and legal obligations should be clearly understood. Costs required to implement the SOX Act may or may not be manageable. What must be manageable are the team members you contract or hire to protect the financial interests of the company. Team members should be responsible for attending regular training sessions that include ethics as part of their ongoing training and update sessions. These sessions may be quarterly, or annually, but should be set up on a consistent scheduling cycle to ensure that all the employees are onboard with all of the laws the corporation is responsible to abide by as well as all of the corporate policies established to comply with legislation and to ensure the corporation will grow financially.

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Ethics classes are currently optional. This applies at high school as well as college level. Colleges currently do not require the inclusion of an Ethics program in any of their degree programs. Some programs currently have two or three classes that are required that are of an Ethics nature, but the programs do not specify a defined Ethics curriculum. Many of the current business programs will allow the Ethics classes to be substituted with another elective. Based on historical events, this researcher recommends two Ethics classes be included in the Degree Curriculum requirements for all business degrees.

Conclusions

The enactment of the Sarbanes – Oxley Act created a platform to ensure that corporate America would be held accountable if they deviated from what is considered to most to be the normal business path, pursuing a positive company growth and a positive cash flow. This Act came with positive aspects as well as negative aspects. The most notable negative aspect is that the implementation of the Act was not cost effective for most for the first two years, and for many for the first five years. After this time, the establishment of internal and external controls have been considered worth the investment. The control measures established have in essence paid for themselves and have provided a security type safety net for the company for the future. Research results show that the costs of implementation were excessive for many for the first two years, but after that time the costs were recognized as part of the expenditures for the period as the Act required staff structure changes. Auditing practices changed, auditing staff was added, and the general corporate culture of how auditing was handled was altered. Year-end audits of the past lacked the all-encompassing, comprehensive detail

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that is needed to comply with the new legislation. Unfortunately, the accounting firms were put in a position as an external means of control and were overwhelmed with the volume of audits they had to complete. Just as any other business entity would do, the auditors raised their audit prices. Some auditors raised their prices to five times the price they had charged the previous year. Although the Act does include some guidelines for judges to use to penalize those that do not comply with the Act by the declared deadlines, to date these guidelines are used very little. The results of the analysis clearly support the relationship between costs and level of implementation. The results supported the relationships between all three factors: cost, implementation, and responsibility. As cost rose, the level of implementation and responsibility also rose. Chief Executive Officers were less likely to leave their current employer if they had a sound internal and external control team.

The establishment of an ethical standard is an important key to establishing a consistent ethical benchmark. Ethics is one factor that is imperative to the development of a trusting relationship. Currently there are no mandatory requirements to include Ethics as part of a college degree curriculum. This subject should be required in all business degree programs. Many students are unaware how Ethics could benefit them. Ethics is currently an elective category. If the student does not want to take an Ethics class, that is his option. The results from this research can be used to establish a correlation between the costs of implementation and the level of implementation. The stronger companies spent more in staff, training, and equipment then the smaller companies. The stronger the level of implementation, the less likely an incidence of fraud will occur. The stronger the level of implementation, the stronger the internal and

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external control teams are. The stronger the control teams are, the lower the costs will be.

The Next Step(s)

The next step(s) to address the issues of looking out for the investor, the economy, and the corporation should be to ensure that the Act and its Amendments are being implemented. The drafting and implementation of the Act were handled at a rapid rate. This assessment can be arrived at by acknowledging the Amendments to the Act that followed at a more leisurely rate. Again, the legislative body was attempting to protect the investors, the economy, and the corporations. The creation, or drafting, of the Act was imperative. The implementation of the Act was less of an imperative maneuver and more of a persuasive maneuver. The Act specifically called for certain conditions to be arrived at by certain deadlines. These conditions included the establishment of internal controls, external controls, and financial reporting responsibility by Chief Board Members. Although the deadlines were modified by Amendments, corporations were made aware of the eminent deadlines and informed of the need to perform compliantly or risk fines or possible jail sentences or both. As auditing costs continued to increase, so did the volume of corporate responsibility as well as the levels of internal control measures.

With the established rules in hand, now is the time to ensure that corporations are placing competent, ethical, and capable executives in places of power and management. This is also the time to ensure that new business professionals are being educated with the knowledge they need to succeed in the new corporate world. Figure 5 depicts a current Board of Directors scenario. Figure 6 depicts a suggested Board of

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Directors scenario. Although key elements can be found in both figures, it is an obvious expansion to include committees under the different departments responsible to key positions. As depicted in the expanded diagram, Figure 6, the auditing committee is responsible for reporting back to the Executive Board. This is a control measure to help prevent issues of fraud. Established committees are responsible for reporting back to their leaders. Each committee is responsible to one vice – president, except the auditing committee. This method helps promote diminished volumes of fraud. Figure 5 is the most common form of Board of Directors. At the head of the board, and the position considered to be the most relevant is that of the President or Chief Executive Officer. It is the intention of the Act to make this Officer responsible for ensuring financial accuracy of the financial reports of the corporation as they are given to the public. The next tier of Officers reflects an even distribution of power. This level has the Vice – President, the Treasurer, and the Secretary. All of these positions are delegated with tasks that are considered important for the ongoing business concern of the corporation, but the level of responsibility and authority are lower than that of the President. Although there are checks and balances in this arrangement, and it is the most common form of officers in smaller organizations, the lack of responsibility that can come with delegation encourages opportunities for fraud and discourages ethical choices.

The configuration in Figure 6 creates more delegation of responsibility and creates more opportunities of making ethical choices. The auditing committee is answerable directly, and only, to the Executive Board. This diminishes the opportunities of collusion. Collusion is the combined effort of two or more to steal. The Chairman of the Board is responsible for the governance of general committees

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related to the functionality of the corporation that include (but are not limited to) legal components, planning components, marketing components, and program components. The financial committee reports back directly to the Treasurer. Each of these committees produces progress reports than can be evaluated at the next Executive Board Member meeting.

Another critical area that must be addressed that is not governed by law is that of ethics. Current graduate programs are lacking the volume of ethics classes that should be considered for inclusion in the development of financial programs of study. As depicted in Table 8, only two classes are called for in most Bachelor Degree Programs and these two classes are often on the elective lists. The names in Table 8 are generic names, but the names represent the general area of education that the subject of ethics is applied. This should not be the case. It should be mandatory for ethics classes to be taught to all Financing Majors in a curriculum block. These blocks are not uncommon for individuals that are taking classes based on a focused program.
Two such focused blocks are depicted in Figure 7. As noted in Table 8, there are no required ethics classes for an Associate's Degree. The Ethics classes may be taken as electives, but they are not required. The Bachelor's Degree programs have similar arrangements. Although the student is required to take elective courses, of which a social science class must be included, a specific ethics class is not required. In addition, the accounting majors are not currently obligated to take additional classes related to the implementation of the Sarbanes – Oxley Act in most Business Colleges. The topic of the legislation is discussed over two or three class periods, but it is not a class by itself. The

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Act with the Amendments could provide topic material for an entire class. This is also material that all future accountants, specifically future auditors will have to be aware of.

The college website snapshots are course curriculum requirements for 1. Computer degree and 2. Accounting degree. As observed in the figure referred to prior, the course curriculums do not include any electives. The focus of the classes is the major program, in the first list the curriculum is focused on computer programming and languages and in the second list the curriculum is focused on accounting skills. Again, the "next step" would be to integrate ethics classes into the required core class structures. To ensure the success of the corporate financial structure and the success of the auditors responsible for verifying that this information is being reported accurately and responsibly, we must challenge ourselves to ensure that we continue to provide the most current information to those that are expected to make decisions based on the information they have. This applies to educational information, ethical information, and legislative information. It should not be unreasonable to assume that advancing business professionals should be able to acquire information from all of these areas during their educational process of attaining their certification and /or degree.

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Types of Audit Deficiencies Related to ICFR and Auditor Type

Types of Audit Deficiencies	Big Four U.S. Auditor	Other Annually Inspected U.S. Auditor	Triennially Inspected U.S. Auditor	Foreign Auditor	Total
Testing of design of controls or operating effectiveness of controls	28	17	20	29	94
Top-down risk-based approach	20	16	10	7	53
IT consideration	23	11	3	3	40
Use of work of others	12	9	5	2	28
Evaluating identified control deficiencies	11	7	0	3	21

Table 1. Types of Audit Deficiencies

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16	1116	2216
32	1132	2232
74	1174	2274
116	1216	2316
132	1232	2332
174	1274	2374
216	1316	2416
232	1332	2432
274	1374	2474
316	1416	2516
332	1432	2532
374	1474	2574
416	1516	2616
432	1532	2632
474	1574	2674
516	1616	2716
532	1632	2732
574	1674	2774
616	1716	2816
632	1732	2832
674	1774	2874
716	1816	2916
732	1832	2932
774	1874	2974
816	1916	3016
832	1932	3032
874	1974	3074
916	2016	3116
932	2032	3132
974	2074	3174
1016	2116	
1032	2132	
1074	2174	

Table 2. NASDAQ company selection process

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Confidence Interval	Sample Size Recommended
5	344
7	185
10	93

Table 3. Coordinating Sample Size and Confidence Interval

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Category		Observed	Expected	Difference	Difference Squared		Difference Squared / Expected
Increased		142	157	-15	225		1.43
Decreased		30	15	15	225		Infinity
DF = 1. Chi^2 value is Infinity. P-value = 0.00001. The result is significant at p=≤0.05.							

Table 4. P-value related to change in administration.

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Factor	Items	Statistical Values
CEO Turnover	Yes, No	t=5.2; p<.0001
Administrative Expenses: Pre-SOX Post- SOX	$ from financial statements Prior to 2005 Post 2012	 T value is -2.314508 P value is .025482
Results for statistical values are considered significant and relevant if p-value is <.05.		

Table 5. Factor Analysis Table

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Summary of Data

	Treatments					
	1	2	3	4	5	Total
N	88	88	88			264
ΣX	2258149.16	3383459.32	1125310.16			6766918.64
Mean	25660.7859	38448.4014	12787.6155			25632.2676
ΣX²	2327421306394[illegible]34721389.[illegible]43079708.7328					814219931737.396
Std.Dev.	44823.5684	58824.3166	39530.731			49359.7203

Result Details

Source	*SS*	*df*	*MS*	
Between-treatments	28973048427.7611	2	14486524213.8806	$F = 6.18014$
Within-treatments	611795414065.7741	261	2344043732.0528	
Total	640768462493.5352	263		

The f-ratio value is 6.18014. The p-value is .002386. The result is significant at $p < .05$.

Table 6. Summary of ANOVA calculations

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P-value	Interpretation
P<0.01	Very strong evidence against H0 (null hypothesis). We are looking to support the alternative hypothesis.
P<0.05	Moderate evidence against H0.
P<0.10	Suggestive evidence against H0.
P>0.10	Little or no evidence against H0.

Table 7. P-value interpretation

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Associate Degree Programs	Bachelor Degree Programs
NO Required Ethics classes.	1. Business Ethics
	2. Legal Ethics

Table 8. Suggested College

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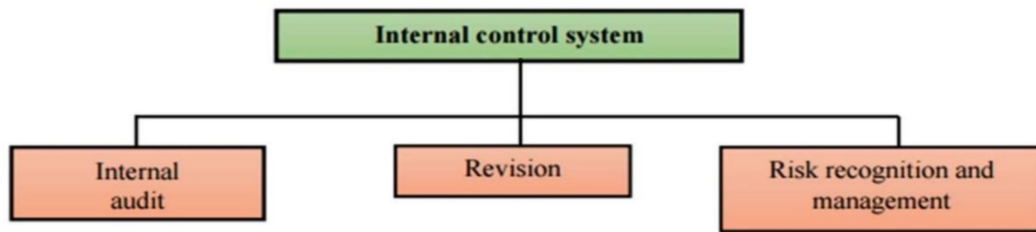

Figure 1. Structure of Internal Control System.

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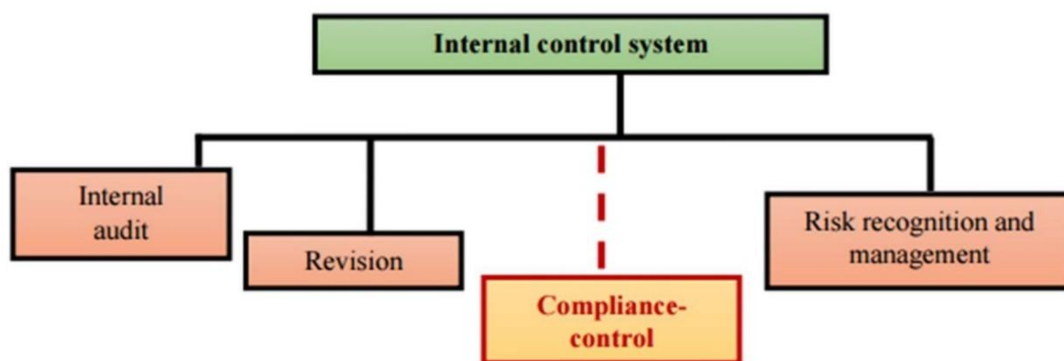

Figure 2. Modified structure of Internal Control System to include Compliance-Control.

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Determining Sample Size

Confidence Level	95%
Confidence Interval	10
Population	*3184*
Sample Size Needed	93

Figure 3. Determining Sample Size.

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Finding Confidence Interval	
Sample Size	93
Confidence Level	95%
Population	3184
Percentage	50

Figure 4. Finding Confidence Interval.

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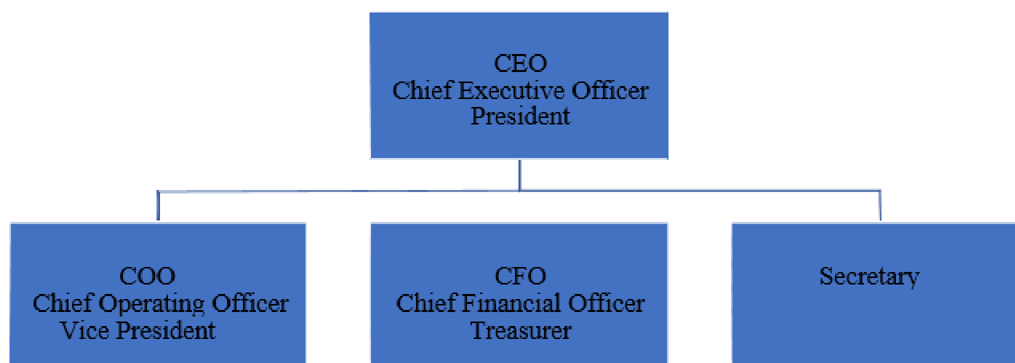

Figure 5. Board of Directors

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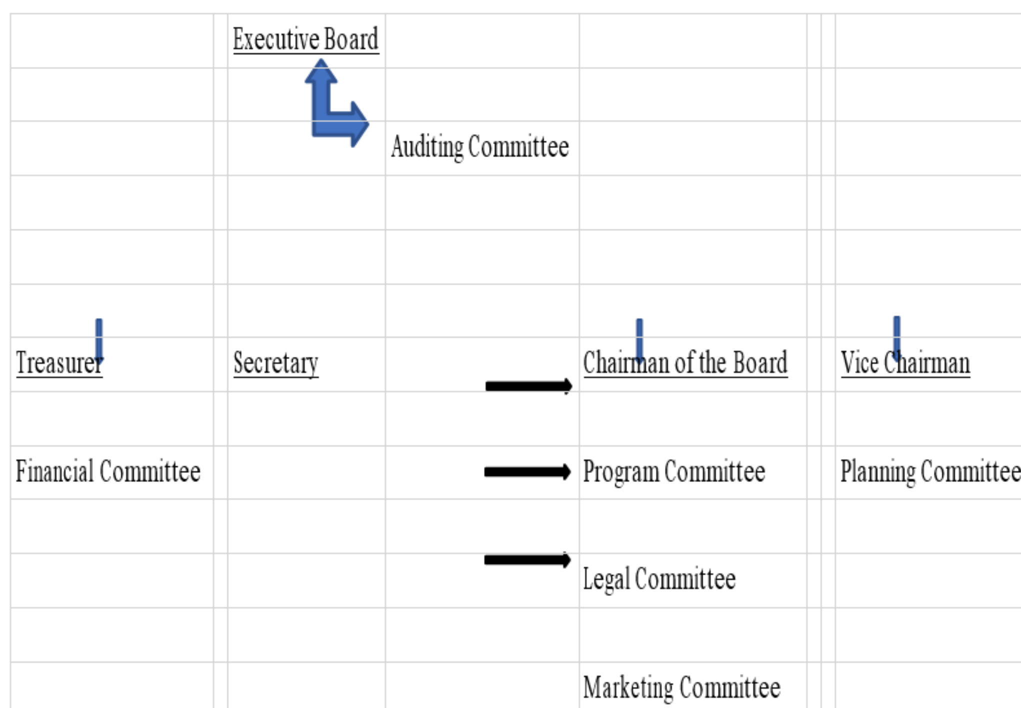

Figure 6. Board of Directors, Suggested

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CIS 422	Database Administration II
CS 241	Java Programming
CS 242	Advanced Java Programming
CS 346	Programming for Security
CS 391	Research in Computer Science
CS 406	Operating System Development
CS 422A	Database Programming I
CS 423	Database Programming II
DMD 131	Introduction to Graphic Imaging
SPN 103	Spanish III
WEB 111B	Introduction to HTML
WEB 121A	World Wide Web Design
WEB 131	Web Development I
WEB 132	Web Development II

AC 114: ACCOUNTING I
AC 116: ACCOUNTING II
AC 239: MANAGERIAL ACCOUNTING
AC 256: FEDERAL TAX
BU 224: MICROECONOMICS
MM 255: BUSINESS MATH AND STATISTICAL MEASURES
MT 140: INTRODUCTION TO MANAGEMENT
MT 217: FINANCE
MT 219: MARKETING
AC 300: INTERMEDIATE ACCOUNTING I
AC 301: INTERMEDIATE ACCOUNTING II
LS 311: BUSINESS LAW
MT 302: ORGANIZATIONAL BEHAVIOR
300/400-LEVEL: MAJOR ELECTIVES

Figure 7. Focused College Class Blocks

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