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The Sarbanes-Oxley Act (sox) was enacted in July 2002 to restore investors’ confidence in the financial market and close loopholes that allowed public companies to defend investors. The act had a profound effect on corporate governance in the U.S. The Sarbanes-Oxley Act requires public companies to strengthen audit committees, perform internal controls tests, strengthen disclosure and also make directors and officers personally liable for accuracy of financial statements. The Sarbanes-Oxley Act also establishes strict criminal penalties for securities fraud and changes how public accounting firms operate. The Sarbanes-Oxley Act helps to provide more securities against fraudulent activities in most accounting firms.

The Sarbanes-Oxley Act changes management’s responsibility for financial reporting significantly. The act requires that top managers personally certify the accuracy of financial reports. If a top manager knowingly or willfully makes a false certification he can face 10 to20 years in prison. If the company is forced to make a required accounting restatement due to managements’ misconduct, top managers can be required to give up their bonuses or profits made from selling the company’s stock. The Sarbanes-Oxley Act significantly strengthens the disclosure requirement. Public companies are required to disclose any material off- balance sheet arrangement, such as operating leases and special purposes entities. The company is also required to disclose any pro forma statement and how they would look under the generally accepted accounting principles (GAAP). Insiders must report their stock transactions to the Securities and Exchange Commission (SEC), within two business days as well.

The Sarbanes-Oxley Act has encouraged companies to make their financial reporting more efficient centralized and automated. Finally, the Sarbanes-Oxley Act established the Public Company Oversight Board , which promulgates standards for public accountants, limits their Conflicts of interest and requires lead audit partner rotation every five years for the same public company.