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THE MAIN GOVERNANCE ASPECT OF THE SARBANES-OXLEY ACT

The Sarbanes Oxley act of 2002 enacted 2002 was also known as the public company accounting reform and investor protection act. It was a response to the rash of real and perceived failures in corporate governance and financial disclosure. The Sarbanes-Oxley act changes management responsibility for financial reporting significantly. The act requires that top managers personally certify the accuracy of financial reports. If a top manager knowingly or wilfully makes a false certification, he can face 10 to 20 years in prison. If the company is forced to make a required accounting restatement due to management misconduct, top managers can be required to give up their bonuses or profits made from selling the company’s stock. If the director or officer is convicted of a securities law violation, he can be prohibited from serving in the same role at the public company.

The sarbanes-Oxley act significantly strengthens the disclosure requirement. Public companies are required to disclose any material off-balance sheet arrangements, such as operating leases and special purposes entities. The company is also required to disclose any pro forma statements and how they would look under the Generally Accepted Accounting Principles (GAAAP). 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, centralised, and automated. Even so, some critics feel all these control makes the act expensive to comply with, distracting personnel from the core business and discouraging growth. The act contains eleven titles, or sections, ranging from additional corporate board responsibilities to criminal penalties, and requires the Securities and Exchange Commission (SEC) to implement rulings on requirements to comply with the law. Harvey Pitt, the 26th chairman of SEC, the led the SEC in then adoption of dozens of rules to implement the Sarbanes-oxley act. It created a new, quasi-public agency, the public company accounting oversight board, or PCAOB, charged with overseeing, regulating, inspecting, and discipline accounting firms in their roles as auditors of public companies. The act also covers issues such as auditor independence, corporate governance, internal control assessment, and enhanced financial disclosure. The non-profit arm of financial executives international (FEI), financial executives research foundation (FERF), completed extensive research studies to help support the foundation of the act. It was approved in the house by a vote of 423 in favour 3 opposed, and 8 abstaining and in the senate with a vote of 99 in favour and 1 abstaining. President George W. Bush signed it into a law, stating it included ‘the most far- reaching reforms of forms of American business practices since the time of franklin D. Roosevelt. The era of low standards and false profits is over; no hoard room in America is above or beyond the law.’

Finally, the Sarbanes-oxley act established the public company accounting 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.