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THE MAIN GOVERNANCE ASPECT OF THE SARBANES-OXLEY ACT

The Sarbanes-Oxley act (SOX) was enacted in July 2002 to restore investor’s confidence in the financial market and close loopholes that allowed public companies to defraud inventors. The act also establishes stricter criminal penalties for fraud and changes on how public companies operate. It introduced major changes to the regulation of corporate governance and financial practice. It is named after Senator Paul Sarbanes and Representative Michael Oxley, who were the main architects, and it set a number of non-negotiable deadlines for compliance.

The direct effect of the Sarbanes-Oxley act on corporate governance is the strengthening of public companies audit committees and they receive wide leverage in overseeing the top managements accounting decisions. The audit committee members must be independent of management and gain new responsibilities such as approving numerous audit and non-audit services, selecting and overseeing external auditors, and handling complaints regarding the managements accounting practices.

Its primary emphasis was to enhance the quality and transparency of corporate disclosure and force changes in the auditing of publicly traded companies. These objectives were achieved in a number of ways by the passing of the Sarbanes-Oxley act. The corporate governance guideline of the (SOA) includes;

1. An increase in the direct responsibility of senior corporate manager for the quality of their company’s financial reports and disclosures
2. An increase in the audit committee’s independence from the company and its responsibility the company’s auditors.
3. Limitations on the types and nature of services that auditors can provide to a publicly traded, audit client.
4. The creation of an independent board to oversee auditing practices regarding publicly traded companies.

The Sarbanes-Oxley act changes management’s responsibility for financial reporting significantly. The top managers personally have to certify the accuracy of financial reports. If the top manager knowingly makes a false certification he may be sentenced to 10-20 years imprisonment. Due to managers misconduct the company may be asked to make an accounting restatement, other top managers may be required to give up their bonuses or profits made from the sales of companies stocks. If the director is convicted of his actions he may be asked not to serve the same role in a public company as punishment.

Finally the act also created an overseeing board “public company accounting oversight board”, and it communicates standards for public accountants to help limit their conflict s of interest and it also requires that the lead auditor has to be rotated every five years for the same public company.