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THE MEAN GOVERNANCE OF THE SARBANES-OXLEY

The Sarbanes-oxley act of 2002 enacted July 30, 2002 also known as the ‘public company reform and investor protection Act’ and ‘corporate and auditing accountability, responsibility and transparency Act’ and more commonly called Sarbanes-Oxley, Sarbox or sox, is a united state federal law that set new or expanded requirement for all U.S public company boards, management and public accounting firms. A number of provisions of the Act also apply to privately held companies, such as the willful destruction of evidence to impede federal investigation.

The bill, which contains eleven sections, was enacted as a reaction to a number of major corporate and accounting scandals, including Enron and Worldcom. The sections of the bills cover responsibilities of a public corporation’s board of directors, adds criminal penalties for certain misconducts, and requires the securities and exchange commission to create regulations to define how public corporate are to comply with the law.

The corporate governance, as defined by shleifer and Vishny (1997), refers to the ways in which investors ensure that they will receive maximum investment. Fundamental components of effective governance structure include managerial ownwrship, size and composition of the board of directors, CEO and directors compensation schemes, audit controls, and external market for control ( keasey and wright, 1997). In general, effective governance controls agency conflicts between management and investors in two ways, first, the free-cash flow problem of a firm can be reduced through dividend policy, stock repurchases, capital structure decisions, and investment in long term projects. Second, the likehood of management entrenchment can be reduced, thus strengthening shareholders rights.

One direct effect of the Sarbanes oxley act on corporate governance is the strengthening of public companies audit committees. The audit committee receives 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.