Sarbanes-Oxley Five Years Later: Hero or Villian by Charles W. Murdock

Article Abstract:

Sarbanes-Oxley was enacted as the culmination of the outcry against the corporate scandals that came to light in the early 2000s. The mantra "business is good, government is bad" was temporarily reversed as investors lost billions of dollars and employees lost their retirement benefits. Government was called upon to act, and the notion that the market solves all problems was disabused when it was clear that the market was also duped by companies such as Enron.

However, it did not take long for the pendulum to begin to swing back as business railed against the costs of compliance with Sarbanes-Oxley. While compliance initially was projected to result in very modest costs, the actual costs mushroomed, arguably because of the over reaction of the accounting profession. Calls for the repeal of Sarbanes-Oxley began to be heard. Accordingly, five years after its adoption, this article reviews the legislation and its impact, and concludes that its benefits far outweigh its burdens.

In particular, it analyzes two high profile examples of corporate corruption, the complicity of the accounting profession, and the supineness of boards of directors who failed to fulfill their oversight responsibility. It also analyzes the requirement that management certify the accuracy of financial statements and the efficacy of internal controls, and that auditors attest to the operation of internal controls, and concludes that these requirements are essential to an efficient functioning of the securities markets. The controversy over the costs of these provisions is a red herring since these are costs that have been inappropriately imposed by the accounting profession and not by the legislation itself. Recent rules adopted by the SEC should alleviate this problem.

The article concludes that the policy behind the Sarbanes-Oxley is essential for the proper functioning of efficient capital markets and that business, instead of bemoaning the Sarbanes-Oxley legislation, should adopt a new mantra "Why Not Tell the Truth."

