

# Where We Stand With Sarbox

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When Enron and WorldCom collapsed under the weight of questionable accounting practices, shareholders, investors and employees spent many a sleepless night wondering if they'd ever see their money again. It is these same shareholders, investors and employees that lawmakers were looking to protect when they passed the Sarbanes-Oxley Act in 2002.

In the wake of the accounting scandals, Sarbanes-Oxley, or Sarbox as it's called, seemed like a good idea. Toughen accounting standards and financial reporting rules and improve corporate governance and oversight, in order to restore shareholder and investor confidence in publicly-traded companies.

But like many of the ideas that come out of Washington, this one had both unforeseen costs and consequences, and subsequently, many companies that were quick to embrace the new accounting reforms are now discovering that compliance comes with a mighty hefty price tag. Corporations were finding it difficult to institute enterprise wide changes that aligned with the onerous oversight and reporting requirements. Often, organizations were distracted by compliance and failed to recognize the other advantages of the post-Enron world.

So with Sarbox firmly ensconced in our corporate consciousness, where do we stand today and what have we learned?

Compliance with Sarbanes-Oxley is much more complicated and expensive than anyone ever anticipated. According to AMR Research, U.S. companies were expected to spend \$6.1 billion in 2005 in order to comply with Sarbanes-Oxley. Additionally, the Securities and Exchange Commission estimates that companies collectively spend 5.4 million staff hours each year implementing Section 404 – the section of the law that regulates financial reporting. As you can imagine, senior-level executives in publicly-held companies are not pleased with these results.

In a May 2005 Deloitte and Touche "Section 404 CFO Roundtable," 83 percent of Chief Financial Officers surveyed believed that the cost of Sarbox compliance far outweighed any benefits to their organizations. The CFO's were also concerned that the costs of compliance were having a direct and immediate negative impact on both their bottom line and shareholder value, whereas the benefits of Sarbanes-Oxley compliance wouldn't be seen for years to come. If ever.

Furthermore, the promises of vague, intangible future benefits like "renewed investor confidence" and "improved operating efficiencies" don't sit well with bottom-line oriented CEO's and CFO's whose performance is being measured by shareholders and investors on a quarter-by-quarter basis.

And it's not just CEO's and CFO's of publicly-traded companies who are getting nervous. Privately-held companies and even non-profits are being held to the same rigorous accounting standards as large, publicly-held corporations.

Banks, investors and insurance companies are now requiring that smaller, privately-held companies abide by the same institutional financial reporting rules and regulations as larger publicly-held companies. Large, publicly-traded companies are also requiring that their business partners, both public and private, comply with Sarbox provisions as a condition of doing business.

With their backs pushed to the wall, private companies are complying. In a 2004 survey by Baruch College in N.Y. and Financial Executives International, 60 percent of companies with revenues less than \$25 million were complying, or were planning to comply with some Sarbox provisions.

So it appears that whether you're a large publicly-held multi-national conglomerate, or a small privately-held hometown business, Sarbanes-Oxley will be the new standard by which you're measured and held accountable.

But are the costs of Sarbanes-Oxley compliance too steep for many companies to bear? That remains to be seen. But what is known is that first-year compliance has taken a toll on the bottom-line results of many companies, both large and small, with little or nothing to show for it.

If this trend continues, where compliance costs continue to rise, and stiff penalties for non-compliance are aggressively enforced, accounting and legal fees will continue to increase while diluting bottom-line profits. The result? Both shareholder and investor value will continue to decline.

A law that was designed to protect shareholders and investors from losing their money could possibly have exactly the opposite effect. Unfortunately this could mean a lot more sleepless nights, both for shareholders and senior-level executives. Richard A. Hall is founder and President/CEO of LexTech, Inc., a legal information consulting company. Mr. Hall has a unique breadth of experience which has enabled him to meld technology and sophisticated statistical analysis to produce a technology driven analytical model of the practice of law. As a busy civil trial attorney, he was responsible for the design and implementation of a LAN based litigation database and fully automated document production system for a mid-sized civil defense firm. He developed a task based billing model built on extensive statistical analysis of hundreds of litigated civil matters. In 1994, Mr. Hall invented linguistic modeling software which automatically reads, applies budget codes, budget codes and analyzes legal bill content. He also served as California

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