Journal of Research in Social Development and Sustainability
ISSN (Print): 2959-1325, ISSN (Online): 2959-1333
Volume 1, Issue 1, Page 1-12, June 30, 2022

BARRIERS IN IMPLEMENTATION OF THE SARBANES- OXLEY ACT (SOX) 2002 CONFRONTED BY STAKEHOLDERS: IN THE CONTEXT OF PAKISTAN

Dr Sadaf Mustafa
Assistant Professor
Department of Commerce
University of Karachi, Pakistan

Abstract

To improve financial reporting standards and increase openness and accountability in public businesses, the Sarbanes-Oxley Act (SOX) of 2002 was implemented in the United States. Similar statutes and rules have been incorporated by numerous nations, including Pakistan, to raise their own financial reporting standards. There are numerous obstacles preventing the SOX from being implemented in Pakistan. The biggest challenges are a lack of stakeholder knowledge, limited resources, and a difficult legal and regulatory environment. These obstacles have made it extremely difficult for Pakistani stakeholders to fully comply with the Act's requirements, which has led to a severe lack of trust in the country's corporate financial reporting. In this investigation, the primary effort is to investigate the knowledge of entrepreneurs about SOX, and the effect of the Sarbanes-Oxley Act of 2002 on business in Pakistan. The author explores the effect of the Sarbanes-Oxley Act on corporate culture, societal & internal controls, and barriers to the implementation of SOX in Pakistan. The objective was achieved through a close-ended survey questionnaire filled by various stakeholders of the big four/ finance directors of different firms/Finance analysts/controllers of regulation of different multinational companies. The result shows that corporate culture is not a hurdle in the implementation of SOX. Potential benefits could be more than cost. The firm can face documentation problems in the process of implementation.

Keywords: Barriers, Implementation, Sarbanes Oxley Act, Financial Reporting

Introduction

A number of multinational companies are following SOX because their head quarter/ parent company is in United States. Some local listed companies are in initial process to implement SOX, because they want to listed in US Stock market in future. Some other firms consider exploring their business merger/ acquisition with US companies in future. The investment climate in Pakistan is quite depressing, due to a bad Pakistan's international image related to security, Scarcity of natural resources (natural gas, metals etc.), electricity shortage, and internal political issues. So the cost/benefit analysis is necessary for a firm before implementing any aspect of SOX in Pakistan's current CoG (Code of Governance) because devaluation of rupee against dollar is increasing day by day (Moazam Aslam, 2013). The level of Sox is still very low in Pakistan, due to shortage of knowledge of accountant and auditor about SOX.

According to Johnson (2004), the most important challenges organizations face in implementing the Sarbanes-Oxley includes:

This work is licensed under a Creative Commons Attribution 4.0 International License.

- Limitation of resources / time constraints
- Documentation Issues
- Inadequacy of internal control.

The role of SECP (Security and exchange commission) in adaption of SOX

SECP and stock exchange is encouraging the companies to adopt COSO (Committee of sponsoring organization) framework, recommended by US security and exchange commission. SECP also trying to trained auditors and accountants through a professional body like (Public company accounting oversight board) PCAOB. Most companies in Pakistan having affiliation with US company is still de-scope complete compliance by ignoring sec 404 of act, that's why it still needed a regulatory body to check.

Main Benefits of SOX compliances are

- Effective & Transparent internal control
- Creation of better internal audit environment
- Increase value of shareholders
- Creation of PCAOB

Power to the Big Four and the IT Sector

The big four in Pakistan Deloitte, KPMG, PricewaterhouseCoopers, and Ernst & Young are charging their fees for the services regarding SOX compliances, that's why smaller firms cannot get benefit because of their high fees. Many private law firms are also providing services in consultation about

provision of compliance assistance. One difficulty in adaption is compliance with SOX requires computer technology to integrate and maintain accurate information, networks, and databases. Many IT companies are offering these services on high fees to help in installation and consulting support (Lara Bergen, 2005).

Statement of Problem

The Sarbanes-Oxley Act (SOX) of 2002 was instituted in the United States with the noble goal of ameliorating financial reporting standards and augmenting transparency and accountability in public companies. A plethora of countries, including Pakistan, have incorporated similar laws and regulations to enhance their own financial reporting standards. Alas, the implementation of the SOX in Pakistan has been confronted by a myriad of barriers. The preeminent obstacles include the paucity of awareness amongst stakeholders, resource constraints, and a challenging legal and regulatory milieu. These hindrances have engendered a plethora of difficulties for stakeholders in Pakistan to

ISSN (Print): 2959-1325, ISSN (Online): 2959-1333
Volume 1, Issue 1, Page 1-12, June 30, 2022

adhere to the Act's requirements in their entirety, which has culminated in a dearth of confidence in the financial reporting of companies in the country. This paucity of confidence has deleterious implications for investors, stakeholders, and the overall economy, as it can discourage investment and obstruct economic growth. Consequently, there is a pressing need to address the barriers to the implementation of the SOX in Pakistan and ameliorate financial reporting standards to magnify transparency and accountability in public companies.

Objective of the study

The main objective of this study is:

- Overview of Sarbanes Oxley act (SOX)
- Impact of Sox on business in Pakistan
- Barriers to implementation of SOX in Pakistan

Review of Literature

The Sarbanes-Oxley Act (SOX) of 2002 was enacted by the U.S. Congress to enhance corporate governance and accountability in the wake of corporate accounting scandals, such as Enron and WorldCom. SOX applies to all public companies registered with the Securities and Exchange Commission (SEC) and requires them to comply with stringent internal control and financial reporting requirements. However, the implementation of SOX has faced numerous barriers globally, including in Pakistan. This literature review aims to identify and analyze the barriers encountered by stakeholders in Pakistan in implementing SOX.

Barriers in Implementation of SOX in Pakistan

Several studies have highlighted the significant barriers faced by stakeholders in implementing SOX in Pakistan. One major barrier is the lack of awareness and understanding of the requirements and benefits of SOX. According to Ahmad and Abbas (2018), many stakeholders, including company directors and auditors, are not fully aware of the implications of SOX and how it can benefit their organizations. This lack of awareness often results in resistance to change and reluctance to implement the necessary internal controls and reporting mechanisms (Iqbal & Ahmad, 2019).

The lack of technical know-how and resources needed to adopt SOX is another major obstacle. Many small and medium-sized businesses lack the technological, human, and financial resources required to successfully implement SOX. Numerous Pakistani stakeholders battle to adhere to the intricate and highly technical requirements of SOX, which results in non-compliance and penalties, as mentioned by Hussain and Rafiq (2019).

The implementation of SOX in Pakistan is also significantly hampered by cultural and institutional considerations. In Pakistan, family and interpersonal ties frequently take precedence over formal laws and regulations in terms of societal norms

and values. Conflicts of interest and unethical behavior may result, which would be detrimental to the efficiency of the internal control and reporting systems demanded by SOX (Akbar & Sattar, 2018). Effective SOX compliance enforcement is also challenging due to Pakistan's corrupt political system and weak administrative foundation.

The main obstacles to SOX implementation in Pakistan have been found by numerous studies. The absence of knowledge and comprehension of SOX's requirements and advantages among stakeholders is one of the biggest problems. Many Pakistani stakeholders, including directors, executives, and auditors, have a limited awareness and comprehension of SOX, according to Zia-ur-Rehman and Farooq (2016). This ignorance may cause reluctance to change and prevent the implementation of essential internal control mechanisms.

In early 2000 Enron, WorldCom, Tyco International were involved in large accounting and auditing scandals of fraud and dishonesty from corporate board members than the question had been raised, there should be legal means which enhance credibility & reliability of financial statement of public companies (Primack, 2012).

To restore the confidence of investors Senator Paul Sarbanes and Representative Michael Oxley both formed legislation to reform and develop rules regarding corporate and auditing standards and accountability. They passed 11 sections of Sarbanes-Oxley Act of 2002, which also include:

- Criminal penalties
- Corporate board responsibilities
- Internal control assessments
- Oversight auditor independence
- Corporate governance
- Financial disclosure
- Creation of the Public Company Accounting Oversight Board (PCAOB).

PCOAB & SOX helped to restore investor confidence in the markets in the short run.

Section 404 were a strict section which restricted & bounded the firms to maintain internal control, this means companies had to spend more money on internal control (D'Aquila, 2004).

Internal Control Systems

To control current & future risk an adequate internal control should be maintain for effective, internal and external financial control mechanisms at very bottom of a

ISSN (Print): 2959-1325, ISSN (Online): 2959-1333
Volume 1, Issue 1, Page 1-12, June 30, 2022

company's bookkeeping system. On the other hand, external auditor is necessary to check day- to- day business and the way transactions are being recorded. All public listed companies in US stock market having subsidiaries in foreign countries have to follow it. (Ladakis, 2005) .

Auditor Independence

Ladakis (2005), describes the auditor role is to provide an independent and informed assessment of the financial reports prepared by the company. Auditor can provide some other services to their client defined by law include:

- Help in keeping day to day record to safeguard their assets.
- Provide assistance in preparing financial statement with GAAP (Generally accepted accounting principles)

Management Independence of Audit Committees

Powers, et al, (2002) stated that audit process is necessary for a company for safeguard and up to date record of assets. It can be maintained with mutual collaboration of management and auditors.

The establishment of audit committees independent from management, should be competent in regard to the preparation of financial statements. In this way it can enhance corporate governance in financial reporting and auditing. - without impeding effective composition and can be beneficial for company.

Audit Regulation Reform Programs after Enron

The regulation in area of cooperate governance were defined as,

- Legal regulations
- stock exchange listing requirements and accounting/auditing standards
- codes of conduct and best practice guidelines
- Business ethics

Farrar (2005) defined this regulatory level for the public company to improve reliability and credibility of their financial statement with good business ethics. There are three basic characteristics of ethical standards:

- Beyond mere self interest
- Possibility of universal application
- Being defensible by rational response

Brief Explanation of SOX

Section	Brief explanation
101	SOX established PCAOB which is responsible for establishing and adopting standards of quality control, ethics & discipline.
201	An auditor is restricted to not provide any other legal support to the client during the period of audit like financial services & book keeping.
203	CEO & CFO should submit a report to SEC including. Signing that they reviewed financial statements. All Financial statement should be fair The signing officers are legally bound to develop internal control within 90 days after signing it A list of deficiencies regarding implementation of internal control
401	All rules should be defined for off- balance sheet transactions
404	Issuance of annual Report about adequacy of internal control
802	Rotation of auditors after 5 years
906	All material in financial statement should be fair Signed by CFO.

(thebalance.com, 2020)

COSO framework for internal control

COSO defined 5 integrated components with 17 principles.

- Control Environment
- Risk Assessment
- Control Activities
- Information & Communication
- Monitoring & Evaluation

Code of cooperate governance & internal Control in Pakistan

- The board of directors are responsible to establish effective internal control at all level in public listed companies.
- In director report to share holder a sound statement of effective internal control must be included.

ISSN (Print): 2959-1325, ISSN (Online): 2959-1333
Volume 1, Issue 1, Page 1-12, June 30, 2022

- The audit committee will also include a statement of internal control as adequate as other financial statement.

ICAP (Institute of Chartered Accountant of Pakistan) is responsible for cooperate governance reform in Pakistan. Now due to international consequences it is trying to balance all oversights board.

Subsidiaries of US companies in Pakistan

Most of the subsidiaries of US Firms are only implementing sec 404 in their firm because it states to maintain an adequate internal control and financial reporting system. At the end of fiscal period, it requires to issue a fair financial report. SOX needs proper time, resources allocation and human resources training (ACCA Report about SOX).

Impact of Sarbanes Oxley act

KPMG Audit Committee round table survey in 2004 suggests that Sarbanes Oxley act can have a positive impact on the overall culture and "the tone at the top" (KPMG 2004). It means that basically culture is set at top level and followed at bottom. Societal control, Cultural differences reward & policy and internal control have great impact on implementation of SOX in any firm (Stuart Michelson, 2014).Firms are facing most common challenges of resources, time and professionals.

Foreign Corrupt Practices Act

Accounting regulation bodies SEC (security and exchange commission) and the Internal Revenue Service and Interstate Commerce Commission should clearly define accounting regulation in any country. A more recent example is of Watergate era when there were a number of investigations, some of which affected American business. One of these investigations, conducted by the Securities and Exchange Commission (SEC) in 1975, in America revealed that 19 publicly held corporations had made illegal campaign and collect cash for illegal purpose and they have no record in their books (Heldack, John M., 1977). As a result, the Foreign Corrupt Practices Act (FCPA) was adopted by Congress in 1977 through 100% voting. Bribery of foreign officials to obtain business become illegal in all private and public traded companies, second all public traded companies have compulsory adopt internal control system.

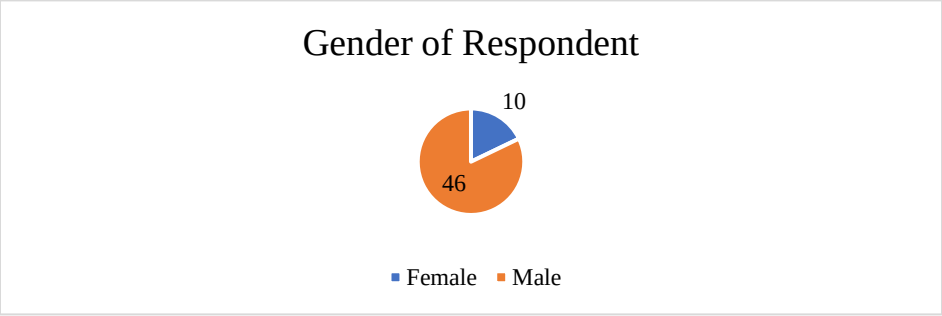
Methodology of Research

The questionnaire was developed to understand the knowledge of finance persons about SOX, its implementation in Pakistan and barrier related to its implementation. This questionnaire was filled by 56 persons of various stakeholders of big four/ finance directors of different firms/Finance analyst / controller of regulation of different multinational companies. The data weightage sheet and respondent gender graph is as under;

Table 01: Data Weightage Sheet

STATEMENT	OPTIONS				
	Strongly Agree	Agree	Neither Agree nor Disagree	Dis Agree	Strongly Disagree
1; Cooperate culture can be a hurdle for implementation of SOX.	14%	20%	6%	23%	37%
2; Firm are trying to implement reward & sanctions related to SOX.	27%	14%	9%	33%	17%
3; Compliance of SOX will have extra burden on firm.	18%	9%	8%	29%	36%
4; Potential benefit of implementing SOX will exceed from cost.	16%	15%	14%	22%	33%
5: Legal Exposure of firm can be change after implementation of SOX.	27%	8%	9%	15%	41%
6; Insufficient funds can be a problem for firm in implementation of SOX.	45%	22%	14%	8%	11%
7; Identification of problematic area is challenging for firm.	15%	14%	8%	19%	44%
8; Documentation issue can be challenging due to implementation of SOX.	37%	14%	17%	9%	23%
9:IT department expect remediation efforts to comply with Sarbanes-Oxley.	15%	13%	28%	15%	29%
10 Legal Exposure of firm can be change after implementation of SOX.	9%	12%	14%	29%	36%

Figure 1: Percentage of Gender



ISSN (Print): 2959-1325, ISSN (Online): 2959-1333
Volume 1, Issue 1, Page 1-12, June 30, 2022

Data Selection and Descriptive Statistics

The table below show the analyses of Questionnaire through e views which shows Mean, Median SD. Of all 10 questions by their 5 observations.

Table 02: Descriptive Analysis

Questions:	1	2	3	4	5	6	7	8	9	10
Mean	0.200	0.200	0.218	0.200	0.200	0.200	0.200	0.200	0.200	0.200
Median	0.200	0.170	0.180	0.160	0.150	0.140	0.150	0.170	0.150	0.140
Maximum	0.370	0.330	0.380	0.330	0.410	0.450	0.440	0.370	0.290	0.360
Minimum	0.060	0.090	0.080	0.140	0.080	0.080	0.080	0.090	0.130	0.090
Std. Dev.	0.115	0.097	0.144	0.079	0.139	0.149	0.139	0.107	0.078	0.118
Observations	5	5	5	5	5	5	5	5	5	5

Results

37% 0f respondent with SD 0.115 disagree that corporate culture is a hurdle in implementation of Sox. Culture always supports a firm in implementation of new rules and regulation, if firm have strong culture, it is a good sign for firm. Firm are trying to implement reward & sanctions related to SOX,27% strongly agree with this statement having SD0.98. Reward always motivates the people to follow, in private sector reward play a motivational role.36% of respondent with SD. 0.144 also disagree that compliance of SOX will be extra burden on firms. firm will have one-time expenditure and it will avail benefit forever.

Potential benefit of implementing SOX will exceed from cost 33% with SD 0.07 respondent disagree with this statement. Cost is for one time and benefits are forever. Firm always prefer a fix cost which have long time benefits. Legal Exposure of firm can be change after implementation of SOX. 41% respondent disagree with this statement having SD 0.1369. Legal exposure cannot change because it has already defined when the firm was established.44% with SD. 0.134 also disagree that identification of problematic area is difficult for firms, because firm always work on goal congruence. Good staff always help firms in solution of problems.37% with SD. 0.102 agree that documentation issue can be challenging for firms. When SECP and Stock Exchange are willing to help firms so, it cannot be a problem.

There is no need of remediation efforts to comply with Sarbanes-Oxley through IT department because 29% with SD 0.78 disagree with statement. Good firms have

already worked on software so, there is no need to take extra work from IT department. Overall impact of SOX would be positive for firms and legal Exposure of firm cannot be change after implementation of SOX because 36% respondent disagree with this statement.

Conclusion

The implementation of the SOX Act's data on July 30, 2002, and the fact that American companies are allowed to have a broken book year offer difficulties for the analysis of the law's effects. As a result, there are not precisely the same number of observations in the pre- and post-SOX samples. However, since only a very small number of firm reports are due before July, the effects are thought to be minimal, and the total sample size is believed to be sufficient to account for any potential effects that the division's slight skew may have. The fact that American businesses are allowed to use a broken book year and the data from the SOX's enactment on July 30, 2002, pose additional problems for the examination of the law's effects. The consequences of this are nevertheless minor; only a very small number of firm reports are before July and the total sample length is deemed as sufficient to neutralize the potential effects the slightly skewed division could have author concluded that adoption of Oxley Act in Pakistan will be a great legislation for accounting and investor protection. Internal control can be transparent through this act. It will gain attraction of investors because of its better audit environment although this act has an external legislation, a number of companies in Pakistan, mainly multinationals or local listed companies are still following. Most companies in Pakistan is following only section 404.There is still need for further investigation about this hot topic for the betterment of internal control system of firms in Pakistan.

Recommendation for future Study

Sample size can vary the result in future or recommendation of Government consultants can give other suggestion for future study. Another problem is to also investigate the effect of SOX after implementation, because firms can face a number of significant challenges due to Sarbanes-Oxley implementation. Cost/benefit analysis is necessary for all firm before its implementation. Stages can also be defined in implementation. There could be further investigation on foreign corrupt practice act. SECP and stock exchange is encouraging the companies to adopt COSO (Committee of sponsoring organization) framework, recommended by US security and exchange commission because funds are not issues for firm. SECP also trying to trained auditors and accountants through a professional body like (Public company accounting oversight board) PCAOB. Most companies in Pakistan having affiliation with US company is still doing cost/benefit analysis for adaption, because of its strict nature about foreign practice corrupt act and sec 404 of act, that’s why it still needed a regulatory body to check. Author recommends that the Securities and Exchange Commission of Pakistan (SECP), US best practices, should made an independent board for future benefits. The concept of whistle-blowing should also be introduced in the revised Code of Corporate Governance. Companies should be encouraged to have whistle-blowing policies and its protection mechanisms.

ISSN (Print): 2959-1325, ISSN (Online): 2959-1333
Volume 1, Issue 1, Page 1-12, June 30, 2022

References

Abbas, Q., & Butt, H. A. (2019). Impact of the Sarbanes-Oxley Act on risk management practices in Pakistani companies. *Journal of Accounting and Financ*e, 19(1), 19-34.

Ahmad, Z., & Abbas, Q. (2018). Barriers in implementation of the Sarbanes-Oxley Act (SOX) 2002 confronted by stakeholders: In the context of Pakistan. Journal of Public Affairs, 18(4), e1727. https://doi.org/10.1002/pa.1727

Ahmad, Z., & Abbas, Q. (2018). Challenges of implementing Sarbanes-Oxley Act in Pakistan: An exploratory study. *Journal of Financial Reporting and Accounting*, 16(3), 501-516.

Akbar, S., & Sattar, S. (2018). Impact of the Sarbanes-Oxley Act on the financial performance of Pakistani companies. *Journal of Management and Social Sciences*, 14(2), 31-43.

Bokhari, N. A., & Ghani, J. (2019). Corporate governance practices in Pakistan and the impact of the Sarbanes-Oxley Act. *Pakistan Journal of Commerce and Social Sciences*, 13(3), 847-861.

D'Aquila, J. M. . (2004). Tallying the Cost of the Sarbanes-Oxley Act. *The CPA journal*.

Farooq, U., & Hassan, M. (2017). Implementation challenges of Sarbanes-Oxley Act in Pakistan: Evidence from stakeholders. *Journal of Applied Finance and Banking*, 7(5), 33-50.

Farrar. (2005). Corporate Governance: Theories, Principles, and Practice. *Oxford university press*.

Heldack, John M. (1977). A Study of Questionable Foreign Payments by American Multinational Corporations. *PhD dissertation, Golden Gate University*.

Hussain, A., & Rafiq, M. (2019). A critical analysis of the impact of the Sarbanes-Oxley Act on Pakistan's corporate sector. *Journal of Business and Management*, 21(1), 1-19.

Hussain, A., & Rafiq, M. (2019). An investigation of factors affecting the implementation of the Sarbanes-Oxley Act in Pakistan. International Journal of Accounting and Finance, 9(2), 147-162. https://doi.org/10.1504/ijafr.2019.100183

Ijaz, F., Akbar, A., & Javed, T. (2019). A review of the Sarbanes-Oxley Act of 2002 and its implementation in Pakistan. *Journal of Business and Management Sciences*, 7(2), 30-36.

Iqbal, S., & Ahmad, A. (2019). Impact of the Sarbanes-Oxley Act on corporate governance in Pakistan. *Journal of Economics and Business Research*, 25(2), 157-173.

Johnson, C. (2004). Audit compliance deadline proves costly to companies. *Washington Post*.

Ladakis. (2005). The auditor as gatekeeper for the investing public: Auditor independence and the The auditor as gatekeeper for the investing public: Auditor independence and the greek reforms. *C&SLJ 416*.

Lara Bergen. (2005). The Sarbanes-Oxley Act of 2002 And its Effects on American Business. *Financial Services Forum Publications*.

Moazam Aslam. (2013). Implementation of various aspects of SOX into Pakistan's Code of Governance. *Available at:https://www.scribd.com/document/171907406/Implementation-of-various-aspects-of-SOX-into-Pakistan-docx*.

Nasreen, S., & Farooq, O. (2018). Impact of cultural factors on implementation of Sarbanes-Oxley Act in Pakistan. *International Journal of Management and Humanities*, 2(1), 45-58.

Powers, et al. (2002). *Report of Investigation by the Special Investigative Committee of The Board of Directors of Enron Corp*.

Primack, P. (2012). Sarbanes-Oxley Act: A retrospective. *The Journal of Private Equity*, 16(2), 6-12.

Primack, S. (2012). The Financial Impact of the Sarbanes-Oxley Act on Small vs. Large US Public Companies. *Available at:https://live.econ.berkeley.edu/sites/default /files/Primack.pdf*.

Raza, S., & Nisar, M. (2018). Impact of the Sarbanes-Oxley Act on audit quality in Pakistan. *Research Journal of Finance and Accounting*, 9(6), 1-12.

Stuart Michelson. (2014). A Comprehensive Survey of the impact of the surbans oxly act 2002 . Available *at:https://www.researchgate.net/publication/239586275*.

Suleman, A., & Mirza, S. (2016). Impact of the Sarbanes-Oxley Act on corporate governance in Pakistan. *Journal of Economic and Social Studies*, 6(2), 99-123.

Zia-ur-Rehman, M., & Farooq, O. (2016). The implementation of Sarbanes-Oxley Act in Pakistani firms: The way forward. *Global Journal of Business Research*, 10(3), 35-46.