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## Ability To Cope With The Increased Costs of Complying With The Sarbanes-Oxley Act of 2002

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**ABILITY TO COPE WITH THE INCREASED COSTS  
OF COMPLYING WITH THE  
SARBANES-OXLEY ACT OF 2002**

A Research Paper  
Presented to the Graduate Faculty of  
the Department of Occupational and Technical Studies  
at Old Dominion University

In Partial Fulfillment  
of the Requirements for the  
Master of Science in Occupational and Technical Studies

By:

Debra B. Cline

May 2004

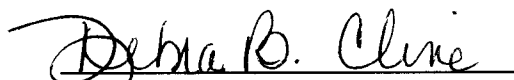
## APPROVAL PAGE

This research paper was prepared by Debra B. Cline under the direction of Dr. John M. Ritz in OTED 636, Problems in Occupational and Technical Studies. It was submitted to the Graduate Program Director as partial fulfillment of the requirements for the Degree of Master of Science in Occupational and Technical Studies.

APPROVAL BY: John M. Ritz DATE: 4-19-04  
Dr. John M. Ritz,  
Advisor and Graduate  
Program Director

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Debra B. Cline

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## **CHAPTER I**

### **INTRODUCTION**

During the past two years, several accounting and management scandals have occurred within major companies that undermined investor confidence in corporations and others involved in capital markets (PriceWaterhouseCoopers, 2003). Thus, the Sarbanes-Oxley Act of 2002 (SarbOx) was established in response to these scandals. SarbOx consists of many new requirements and responsibilities geared toward the Directors and Audit Committees of small businesses, which trade stock on the NASDAQ, American Stock Exchange (AMEX), or New York Stock Exchange (NYSE). The requirements have been put in place with the intent to reduce fraud and failures and improve reliability of corporate reporting.

SarbOx is now the topic of conversation for many members of Boards of Directors, Audit Committees, and other individuals in today's corporate world. The costs related to complying with SarbOx is one of the major issues that publicly traded small businesses and community banks are having to face.

First Century Bank, N.A., is only one of many businesses experiencing the increased costs involved with adhering to good governance and complying with SarbOx. Therefore, First Century Bank, N.A., as well as other publicly traded businesses, will have to determine the cost of SarbOx versus the impact, expense, and ability of de-registration.

### **STATEMENT OF THE PROBLEM**

The purpose of this study was to determine the impact on small

businesses and the ability to cope with the increased costs of complying with the Sarbanes-Oxley Act of 2002.

### **RESEARCH GOALS**

To research this problem, the following questions were established:

- 1) What are the major areas of costs for small businesses related to the Sarbanes-Oxley Act?
- 2) Did every small business incur these costs?
- 3) Did every small business incur costs in each major area?
- 4) Did any of the small businesses go private or de-register as a result of the costs of the Sarbanes-Oxley Act?
- 5) Did the implementation of the Sarbanes-Oxley Act restore shareholder confidence?

### **BACKGROUND AND SIGNIFICANCE**

First Century Bankshares, Inc., and its wholly owned subsidiary, First Century Bank, N.A., is a small community bank with current assets of approximately \$370,000,000.00. First Century Bank, N.A., is headquartered in Bluefield, West Virginia, and provides financial services from eleven locations and two states (Virginia and West Virginia). The holding company's Board of Directors is comprised of fourteen Board Members. The bank's Board of Directors is comprised of fifteen members and the Audit Committee of First Century Bank, N.A., consists of three members. While the above three members do serve on both Boards of Directors, they are required to be independent. First Century Bankshares' common stock is not traded on any stock exchange,

however, quotations may be received through Over the Counter Bulletin Board making First Century Bank susceptible to complying with the Sarbanes-Oxley Act of 2002.

According to Ronald Hypes, Chief Financial Officer and Comptroller for First Century Bank, N.A., the bank will experience a 40 to 50 percent increase in Internal Audit Department fees and other related costs in complying with SarbOx. Many other banks and small businesses are also experiencing these costs. Stephen Wilson, President and CEO of Lebanon Citizens National Bank, stated, "We separated things out and it's costing us a lot of money. And I don't see where I'm getting a lot more value. But we did it" (ABA Banking Journal, 2003, p.18).

This study sought to determine the major areas of costs small businesses encountered while complying with the Sarbanes-Oxley Act of 2002 and to discover if management would consider de-registering the company's stock because the cost benefit analysis is not positive.

### **LIMITATIONS**

This study was based on the following limitations:

1. The information available on small businesses addressed within this study.
2. The affect of SarbOx on all companies impacted by the Act.
3. The companies reviewed were defined as small businesses, however, this study did not conform to any additional size or line of business demographics.

4. The population was limited to small businesses and banks within the Bluefield Region in Virginia and West Virginia.

### **ASSUMPTIONS**

This study was based on the following assumptions:

1. All small businesses are complying with the Sarbanes-Oxley Act of 2002.
2. Complying with the Sarbanes-Oxley Act will cause a loss in profits.

### **PROCEDURES**

For this study, the researcher conducted a review of literature specifically related to the Sarbanes-Oxley Act of 2002 and consulted with the First Century Bank, N.A., Chief Financial Officer, Auditor and Senior Vice President. To determine the major areas of costs for small businesses, the researcher then developed and administered a survey to owners and executives of small businesses. Upon receipt of the surveys, the information was compared to determine the costs, major areas of costs, and if any businesses went private or de-registered due to the costs.

### **DEFINITION OF TERMS**

The terms used in this study are defined as follows:

**Audit Committee-** The Audit Committee assists the Board of Directors in fulfilling its oversight responsibilities, as well as reviewing the financial reporting process, the system of internal control, the audit process, and the company's process for monitoring compliance (PriceWaterhouseCoopers, 2002).

**Board of Directors-** A committee, which provides governance, guidance, and

oversight to management. The Board has a major role in defining what it expects in integrity and ethical values, and can confirm its expectations through its oversight activities. The Board is involved pervasively in internal control (PriceWaterhouseCoopers, 2002, p. 5).

**De-registering-** Removing the company's stock from AMEX, NASDAQ, or NYSE in order to trade publicly via Pink Sheets or Bulletin Board. This helps with decreasing the costs related to time and money.

**Independent Committee Member-** The independent committee member must be an "affiliated person" of the company. They may not accept, directly or indirectly, any consulting, advisory, or other compensation fee from the company other than in his or her capacity as a member of the Audit Committee, Board of Directors, or other Board Committee (PriceWaterhouseCoopers, 2002, p. 19).

**Private Corporation-** A corporation owned by less than 300 shareholders with shares in the open market.

**Public Corporation-** A corporation having either common or preferred stock shares available to an individual in the open market (AMEX, NASDAQ, or NYSE).

**Sarbanes-Oxley Act of 2002-** Protects investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws.

## **SUMMARY AND OVERVIEW**

Chapter I was an introduction to the Sarbanes-Oxley Act of 2002 and presented the major issue of costs for small businesses in complying with the Act. The problem statement, research goals, and background and significance provided a rationale for the study. The procedures section explained how the

study would be executed.

Chapter II, Review of Literature, provides a summary of the Sarbanes-Oxley Act and information relating to its major area of costs for small businesses. Chapter III, Methods and Procedures, explains how the study was conducted. In Chapter IV the findings are compiled and presented. Chapter V finalizes the study with the summary, conclusions, and recommendations.

## **CHAPTER II**

### **REVIEW OF LITERATURE**

The purpose of this chapter was to review literature related to the topic and goals of the research study. Contained within this chapter were sections explaining the Sarbanes-Oxley Act of 2002 and the major areas of costs for small businesses complying with SarbOx. The review of literature also focused on de-registering or taking a company private as a result of the costs and its effect on investor confidence.

#### **Sarbanes-Oxley: A Brief Overview**

A series of accounting and management scandals in some of America's most well known companies such as Enron and WorldCom have occurred over the past two years. It is believed that these scandals within major companies have undermined investor confidence in corporations and others serving the capital markets (PriceWaterhouseCoopers, 2003).

The Sarbanes-Oxley Act is a government regulation put in place with the intent of improving the accuracy and reliability of corporate reporting, as well as consumer confidence. Therefore, the law applies in general to publicly held companies, their Boards of Directors, and Audit Committees.

Although all sections of the Sarbanes-Oxley Act are important and contribute to the costs of compliance, Sections 302 and 404 are two of the most critical statutes, as well as considerable factors contributing to the rising costs in complying with SarbOx. Records show that, "EMC Corporation will have spent more than \$1,000,000.00 and thousands of man-hours complying with two of the

main statutes in the Sarbanes-Oxley Act of 2002-Section 404, related to internal controls; and Section 302, mandating CEO and CFO certification of quarterly financial statements” (Nyberg, 2003, <http://www.cfo./article?.article=10546>). See Figure 1 and 2 for a summary of these sections.

**Figure 1. Summary of Sections 302 and 404 of SarbOx**

**Section 302: Corporate Responsibility For Financial Reports.**

The CEO and CFO of each issuer shall prepare a statement to accompany the audit report to certify the “appropriateness of the financial statements and disclosures contained in the periodic report, and that those financial statements and disclosures fairly present, in all material respects, the operations and financial condition of the issuer.” A violation of this section must be knowing and intentional to give rise to liability.

**Section 404: Management Assessment Of Internal Controls.**

Requires each annual report of an issuer to contain an “internal control report,” which,

- (1) state the responsibility of management for establishing and maintaining an adequate internal control structure and procedures for financial reporting; and
- (2) contain an assessment, as of the end of the issuer’s fiscal year, of the effectiveness of the internal control structure and procedures of the issuer for financial reporting.

Each issuer’s auditor shall attest to, and report on, the assessment made by the management of the issuer. An attestation made under this section shall be in accordance with standards for attestation engagements issued or adopted by the Board of Directors. An attestation engagement shall not be the subject of a separate engagement.

Taken from the website <http://www.aicpa.org/info/Sarbanes-Oxley2002.asp>



## Figure 2. Implications of SarbOx

**Auditors Report to the Audit Committee**-Auditors will report to and be overseen by a company's audit committee, not management.

**Audit Committees Must Approve All Services**-Audit Committees must pre-approve all services (both audit and non-audit services not specifically prohibited) provided by its auditor.

**Audit Reports Must Contain Description of Internal Controls Testing**-The regulatory board will also issue or adopt standards that will require every audit report to attest to the assessment made by management on the company's internal control structures, including a specific notation about any significant defects or material noncompliance found on the basis of such testing.

**Failure to Maintain Workpapers**-It is now a felony with penalties of up to 10 years to willfully fail to maintain "all audit or review workpapers" for at least five years. The SEC will establish a rule covering the retention of audit records and the Board will issue standards that compel auditors to keep other documentation for seven years.

Taken from the website <http://www.aicpa.org/info/Sarbanes-Oxley2002.asp>

These compliance requirements, as well as others outlined in the Sarbanes-Oxley Act, are geared toward improving corporate disclosures and governance. "Yet, the compliance requirements and costs far outweigh the benefits" (Telberg, 2003, <https://www.cpa2biz.com/News/Telberg/CPAs+Chafe+at+SOX + Burdens.htm>).

Fines are also excessive for misinforming or not complying with the act. Therefore, in order to avoid these penalties, corporate clients are paying up to 30 to 40 percent more in fees to ensure they receive accurate and timely information concerning the final rulings (Telberg, 2003, <https://www.cpa2biz.com/News/Telberg/Top+10+Surprises+Sarbanes+Oxley+Act>). This could be one reason why SarbOx has only been in existence for approximately 14 months, yet Chief Financial Officers continue to tally the compliance costs.

## Major Areas of Costs

The increased costs occurring for small businesses are attributed to several factors, including legal counsel costs, internal control documentation, new technology, staff additions, and training. “By rapidly legislating a whole set of processes, this law has become a windfall for auditors and lawyers and a time drain on overburdened finance departments” (Nyberg, 2003, <http://www.cfo.com/article?.article=10546>).

“The Sarbanes-Oxley Act is so dense with rules, and the penalties for breaking them so severe, managers are turning to lawyers and auditors for expert advice on practically everything” (*USA Today*, 2003, p. 2B). Businesses are incurring increased costs from legal counsel and consulting fees as attorneys are called in for legal advice regarding corporate governance and compliance and consulting firms are obtained to provide individual assessments of the project and assist in the application of new software. As a provision with SarbOx, an Audit Committee can retain counsel at its discretion without prior permission of the company’s Board of Directors or its management staff. This section of SarbOx does not preclude the Audit Committee from questioning either the company’s internal counsel or regular outside counsel.

A company’s internal control structure and documentation process used to comply with Sections 302 and 404 are critical parts of the SarbOx and related costs. As the internal controls are documented, each area is reviewed for weaknesses. An example would include documentation of the internal control structure, which must first start with a review of each financial statement section.

As each area is reviewed, documentation on each entry (either debit or credit) is examined for who prepares it, who controls it, and who reconciles it. If the segregation is not noted, an internal control weakness has occurred. As the areas are identified, the company must implement new procedures to ensure that stronger internal controls are executed and documented. Without correcting weaknesses, Section 404 has not been attested to for quarterly or annual financial statements. These procedures take a tremendous amount of man-hours, as well as the cost of software programs to assist in the procedures.

Updating the company's compliance system in order to meet new requirements of SarbOx is an area where technology costs escalate. Many corporations are purchasing software and information technology consulting packages in order to assure compliance to this section of SarbOx. For example, flow-charting software has been recommended by accounting firms for the quickest way of documenting and noting internal control weaknesses.

Additional costs also come from hiring or expanding the audit staff in order to ensure closer attention to compliance. This can include either paying overtime for man-hours used, hiring additional staff, or external consulting for documenting the internal control structure. Companies can also expect to spend money on training to ensure current employees are educated on effective internal control structure and compliance software and attend seminars and audit committee schools in order to meet year-end and quarterly audit requirements. The need for training will continue to occur for employees and Audit Committee members as new interpretations of SarbOx are brought into practice.

## De-registering or Taking a Company Private

In a July article titled, "Though Stock Is Publicly Held, Firms Adopt Private Mentality," the *Wall Street Journal* wrote, "At a time when tougher corporate-disclosure laws are making it more and more difficult for publicly traded companies, de-registering could become even more attractive" (<http://www.upenn.edu?researchatpenn/article.php?715&bus>). According to an article in *USA Today* (2003, p. A3), there has been a percent increase in the past year in companies going private and it suggests that the increased costs of complying with SarbOx are a factor.

Being a private company has not always been the trend. In fact, for the past 10-years, public is where companies have wanted to be, due to financial and growth opportunities. But, the implementation of Sarbanes-Oxley has created stricter standards, regulatory concerns and additional requirements for officers and directors in public companies, not to mention the costs involved in remaining public and complying to the new regulations. Therefore, many companies are now considering de-registering or taking the company private. The process of de-registering or taking a company private generally lowers the company's filing requirements making them unobligated to disclose sensitive information and unsusceptible to SEC filings. In fact, taking a company private is an increasingly popular strategy. "These deals now make up 17 percent of all public takeovers. Up from virtually zero just 10 years ago" (Bohnen & Rosenblatt, 2003, <http://www.bizJournals.com/boston/stories/2003/06/16/editorial4.html>).

Taking a company private, however, is not necessarily an easy task either

and it also has its costs. Therefore, companies have to weigh their options, consider the costs of taking a company private, and determine if they should remain public and endure the burdens of filings, regulations, and liabilities that drive up the cost of complying to SarbOx.

### **Investor Confidence**

A major purpose of the Sarbanes-Oxley Act is to re-establish investor confidence in capital markets. Requiring certification of financial statements, disclosure control and procedures is a way of doing this. "A concern is that Sarbanes-Oxley is costly and that this is having a negative impact on corporate behavior" (Shelby, 2003, <http://banki.../index.cfm?FuseAction=Hearings.Testimony&TestimonyID=337&HearingID=6>). Thus, they are choosing to take their companies private. With publicly held companies going private, it is possible that there will be less financial and business information available to shareholders causing a decrease in investor confidence in capital markets. The Sarbanes-Oxley Act, to a degree, appears to be contributing to investors regaining confidence in the market. But, it is going to take more than a law to fully regain investor confidence. "It will take demonstrated commitment to transparency, accountability, and integrity to fully regain public trust" (Yoon, 2003, <http://www.cfo.com/article/1,5309,9081,00.html?f=related>).

### **Summary**

Chapter II provided information on the Sarbanes-Oxley Act of 2002 and major areas of costs related to implementation of government compliance. The information found indicated that small businesses were experiencing increased

costs related to Sarbanes-Oxley. It also discussed the prospect of businesses de-registering or going private as a result of the increased costs of complying with the law and the effect of SarbOx on investor confidence.

Chapter III will discuss the procedures employed that will determine the impact and ability for small businesses to cope with the costs of complying with the Sarbanes-Oxley Act. The instrument design, population, methods of data collection, and statistical analysis will be discussed in this chapter.

## **CHAPTER III**

### **METHODS AND PROCEDURES**

The focus of this study was the ability for small businesses to cope with the increased costs of complying with the Sarbanes-Oxley Act of 2002. The information presented in this chapter addresses the purpose and research goals of the study. In response to this problem, the following research goals were established: to determine the major areas of costs for small businesses related to the Sarbanes-Oxley Act; to find out if small businesses incurred costs in each of the major areas; to determine if any of the small businesses de-registered or took the company private as a result of the costs; and, to conclude if implementation of the Sarbanes-Oxley Act has restored shareholder confidence. Chapter III also identifies the population, as well as provides information regarding the instrument design, the methods and procedures used to gather the data collected, analysis of data, and summary.

#### **POPULATION**

In order to collect the information needed to address the research goals, the population used was public companies within the Bluefield Region of Virginia and West Virginia. The population consisted of 25 publicly traded small businesses. The Chief Financial Officer of each company served as the targeted population.

#### **INSTRUMENT DESIGN**

The researcher developed an instrument consisting of questions regarding the costs of complying with the Sarbanes-Oxley Act. The researcher also

consulted with the Senior Vice President and Auditor of First Century Bank, N.A., in order to solicit additional questions that would need to be addressed and/or suggestions for improving the survey instrument. The survey instrument was based on the study's research goals. It focused on increased costs, the major areas of those costs, companies de-registering or going private, and shareholder confidence in relation to complying with SarbOx and was designed to collect this information. The survey instrument consisted of ten closed-form questions with yes/no answers, five of those questions had fill in slots for percentages of cost increases. A sample of the survey is found in Appendix A of this study.

### **METHODS OF DATA COLLECTION**

Data collection consisted of a survey instrument distributed to 25 representatives of small public companies. The purpose of the survey was to evaluate the major areas of costs for small businesses, conclude if small businesses incurred costs in each of the major areas, determine if any small businesses de-registered or took the company private due to those costs, and if shareholder confidence is being restored due to the implementation of the Sarbanes-Oxley Act.

The survey instruments were mailed through the United States Postal Service along with a cover letter and a self-addressed, stamped envelope. Each of the Chief Financial Officers was asked to respond within a two-week period. After the two-week period expired, a follow-up letter, as well as another survey instrument was mailed to those representatives who had not yet responded. Upon receipt of all executed surveys, the identification reference sheet was



destroyed in order to ensure the confidentiality of those surveyed. For a copy of the cover letter and follow-up letter, see Appendices B and C.

### **STATISTICAL ANALYSIS**

The data collected from the survey of small businesses was tabulated and analyzed using mean statistics for the closed-form questions and percentiles for the percentage responses to determine:

1. If costs were incurred by every company in each major area.
2. Area with highest percentage of costs.
3. Did any of the small businesses de-register or go private as a result of the increased costs of SarbOx.
4. Whether shareholder confidence is being restored.

The results will be used to show the major areas of costs, the area with the largest costs, if any businesses de-registered or went private due to the costs and if a restoration of shareholder confidence has been noted.

### **SUMMARY**

Chapter III showed the methods and procedures used to collect the pertinent data to address the research goals and purpose of the study. The data collected allowed the researcher to determine a small company's ability to cope with the costs of complying with the Sarbanes-Oxley Act of 2002. The results from the methods and procedures established in this chapter will be presented in Chapter IV.

## **CHAPTER IV**

### **FINDINGS**

Chapter IV will present the data gathered for this research study. The problem addressed in this study was the ability for small businesses to cope with the increased costs of complying with the Sarbanes-Oxley Act of 2002. Data was collected through a survey instrument distributed to public companies within the Bluefield Region of Virginia and West Virginia. The survey instrument consisted of ten closed-form questions. Five of the ten questions asked for increased percentages. The purpose of the survey was to obtain information pertaining to the five research goals of the study. Approximately two-weeks after the initial mailing, follow-up letters and copies of the survey instrument were mailed to those individuals who had not responded. A total of 23 responses were received, representing 92% of the population.

### **SURVEY RESPONSES**

Questions 1 through 10 furnished yes/no responses to questions that would provide the necessary information to answer the research goals. Responses are summarized in tables for these questions.

Question 1 asked each of the representatives if their company was classified as a small public corporation as of July 2002. A total of 23, 100% of representatives, responded that their company was classified as a public company as of July 2002. The responses are summarized in Table 1.

<b>TABLE 1. Question 1</b>			
	<b>Response</b>	<b>Frequencies</b>	<b>Mean</b>
Was your company classified as a small public corporation as of July 2002?	Yes	23	100.00
	No	0	0.00

Question 2 asked if companies incurred costs related to complying with the Sarbanes-Oxley Act of 2002. One-hundred percent of the representatives answered yes to this question. The responses are summarized in Table 2.

<b>TABLE 2. Question 2</b>			
	<b>Response</b>	<b>Frequencies</b>	<b>Mean</b>
Has your company incurred costs as related to complying with the Sarbanes-Oxley Act of 2002?	Yes	23	100.00
	No	0	0.00

Question 3 asked representatives if their companies have gone private due to the costs associated to complying with the Sarbanes-Oxley Act of 2002. Question 4 asked companies if they had de-registered due to the costs associated to complying with the Sarbanes-Oxley Act of 2002. A total of 3 companies have gone private due to the costs associated with complying to the Sarbanes-Oxley Act of 2002. The same 3 companies have also de-registered due to the costs associated with complying to the Sarbanes-Oxley Act of 2002. A total of 20 companies remain public. The responses are summarized in Table 3.

<b>TABLE 3. Questions 3 &amp; 4</b>			
Has your company gone private and/or de-registered due to the costs associated to complying with the Sarbanes-Oxley Act of 2002?	<b>Response</b>	<b>Frequencies</b>	<b>Mean</b>
	Yes	3	8.7
	No	20	91.3

Questions 5 through 9 asked the respondents if their companies experienced an increase in legal, internal control documentation, technology, staff addition, or training costs related to complying with the Sarbanes-Oxley Act of 2002. If their answer was yes, they were also asked to provide the percentage of increase experienced. These individual percentages are provided in Appendix D. Most companies experienced some increased costs in each area. A majority of the companies responded that they experienced increases in costs related to internal control documentation and training. Many of the companies, 69.5%, also experienced an increase in legal costs. However, very few companies, 26.1%, experienced an increase in staff addition costs. Table 4 summarizes the responses.

<b>TABLE 4. Questions 5-9</b>			
Has your company experienced an increase in legal, internal control documentation, technology, staff additions and/or training costs related to complying with the Sarbanes-Oxley Act of 2002?			
<b>Area if Cost</b>	<b>Response</b>	<b>Frequencies</b>	<b>Percentage</b>
Legal	Yes	16	69.5
	No	7	30.5
Internal Control	Yes	19	82.6

Documentation	No	4	17.4
Technology	Yes	10	43.5
	No	13	56.5
Staff Addition	Yes	6	26.1
	No	17	73.9
Training Costs	Yes	18	78.3
	No	5	21.7

Question 10 asked respondents did they feel the implementation of the Sarbanes-Oxley Act restored shareholder confidence in their company. All 23 representatives responded that they did not feel that the Sarbanes-Oxley Act has restored shareholder confidence. However, some of the respondents wrote comments such as they felt that shareholder confidence was never lost, was never an issue, or had no impact. One respondent commented that their shareholder confidence was always positive. A summary of responses is shown in Table 5.

	<b>Response</b>	<b>Frequencies</b>	<b>Mean</b>
Do you feel the implementation of the Sarbanes-Oxley Act restored shareholder confidence in your company?	Yes	23	100.00
	No	0	0.00

### **SUMMARY**

The survey instrument was used to collect information in relation to the research goals established for this study. Data were obtained to determine the

major areas of costs and if costs were incurred in each of the major areas, if any small businesses de-registered or took the company private, and if shareholder confidence has been restored. A summary of the findings, conclusions reached, and recommendations as a result of the data gathered and analyzed is presented in Chapter V.

## **CHAPTER V**

### **SUMMARY, CONCLUSIONS, AND RECOMMENDATIONS**

The purpose of this chapter was to report the summary, conclusions, and recommendations of this study. A summary of this research project will be presented in order to provide a description of the problem, research goals, as well as the methods and procedures used in the study. An answer to the research problem will be provided based on data collected. Recommendations will also be presented based on the information gathered from the survey instrument.

#### **SUMMARY**

The problem of this study was to determine the ability for small businesses to cope with the increased costs of complying with the Sarbanes-Oxley Act of 2002. Research goals were established based on the problem. The research goals addressed in this study were to determine the major areas of costs for small businesses; to find out if small businesses incurred costs in each of the major areas; to identify if any small businesses de-registered or took the company private as a result of those costs; and, to conclude if implementation of the Sarbanes-Oxley Act of 2002 has restored shareholder confidence.

A review of literature was conducted in order to provide a brief overview of the Sarbanes-Oxley Act of 2002. Other sections of the literature review focused on determining the major areas of costs for small businesses complying to the Sarbanes-Oxley Act, as well as de-registering or taking a company private and investor confidence.

Upon completion of the review of literature, an instrument was developed

and distributed to the Chief Executive Officers of 25 publicly traded small businesses within the Bluefield Region of Virginia and West Virginia. The survey was used to collect data and provide answers to the research goals outlined in the study. Based on the review of literature and results of the survey, conclusions and recommendations were made.

### **CONCLUSIONS**

The purpose of this study was to determine the cost and impact of complying to the Sarbanes-Oxley of 2002 for small businesses such as First Century Bank, N.A. The first three goals were obtained by a combination of the review of literature and data collected by the survey instrument. The first goal of the study was to determine the major areas of costs for small businesses related to the Sarbanes-Oxley Act. The researcher conducted a review of literature, which established that the major areas of costs for small businesses related to the Sarbanes-Oxley Act are legal, internal control documentation, technology, staff addition, and training. The second goal addresses if every small business incurred these costs. Question 2 of the survey instrument clearly indicated with a 100% response that small businesses have incurred costs related to complying with the Sarbanes-Oxley Act. Goal three was to find out if every small business incurred costs in each of the major areas. Questions 5 through 9 revealed that several of the businesses have incurred some costs in each of the major areas, however, not every small business has incurred costs in each of the major areas. A majority of small businesses have incurred legal, internal control documentation, and training costs.



The fourth goal of the research study was to determine if any of the small businesses went private or de-registered as a result of the costs of the Sarbanes-Oxley Act. This goal was answered by asking survey respondents if their companies had gone private and/or de-registered due to the costs associated with complying with the Sarbanes-Oxley Act of 2002. Responses to Questions 3 and 4 of the survey indicated that 3 out of 23 companies have gone private and/or de-registered since the implementation of the Sarbanes-Oxley Act of 2002 indicating that costs are an issue for small businesses.

Goal five was to determine if the implementation of the Sarbanes-Oxley Act has restored shareholder confidence. Again, a combination of the review of literature and survey instrument was used to obtain this goal. Question 10 of the survey instrument asked representatives if they felt the implementation of the Sarbanes-Oxley Act restored shareholder confidence in their company. The review of literature revealed that a major purpose of SarbOx is to restore investor confidence. However, a 100% response from representatives indicates that businesses do not feel the Sarbanes-Oxley Act has restored shareholder confidence. This result shows that it is going to take more than the implementation of this Act to regain shareholder confidence.

### **RECOMMENDATIONS**

Based on the research conducted, the researcher recommends the following actions. The recommendations focus on two areas: taking a company private and/or de-registering and costs.

**Taking a company private and/or de-registering:** Small public businesses

should consider taking their company private and/or de-registering. There are advantages and disadvantages to taking the company private and/or de-registering. Taking the company private may lower the company's filing requirements, regulations, and liabilities, which in turn lowers the costs of complying with the Sarbanes-Oxley Act of 2002. However, taking a company private also has its costs and may hinder financial growth opportunities.

Additional research is also recommended in this area.

**Costs:** Small businesses should monitor their costs in relation to the implementation of SarbOx. Being aware of the major areas of costs, developing a budget, and planning for the increased expenses in these major areas will help small businesses to cope with the increased costs of complying with the Sarbanes-Oxley Act of 2002.

**Advertising:** Small businesses should consider advertising their compliance with the Sarbanes-Oxley Act. This would make investors aware of the Act. Investors would also need to be educated on the requirements of complying with SarbOx. This would build trust with the company.

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## APPENDICES

**Appendix A: Survey Instrument**

**Appendix B: Cover Letter**

**Appendix C: Follow-up Letter**

**Appendix D: Results of Individuals Percentages**

## APPENDIX A

### ABILITY OF SMALL BUSINESSES TO COPE WITH THE INCREASED COSTS OF COMPLYING WITH THE SARBANES-OXLEY ACT OF 2002

#### Survey Instrument

All information gathered from this survey will be used for the completion of a research study conducted as part of the Master's of Science in Occupational and Technical Studies at Old Dominion University (ODU) Norfolk, Virginia.

Information gathered from this study will be used to determine the major areas of costs of complying with the Sarbanes-Oxley Act of 2002, the ability for small businesses to cope with those increased costs and if any companies de-registered or went private due to the costs.

#### **Instructions:**

Please answer every survey question by circling yes or no. For questions 5-9, if your company experienced an increase in costs, please fill in the percentage amount.

Return the survey in the self-addressed, stamped envelope provided for your convenience.

A number has been typed in the bottom right hand corner of each survey in order to keep track of who has completed the survey. Upon receipt of all surveys, this information will be destroyed. All answers and comments made on this survey will remain completely anonymous. The study will not contain any company names.

Thank you for your assistance in completing this survey.

**Please respond to each question below by circling "Yes" or "No". For questions 5-9, if the answer is "Yes", please fill in the percentage of increase your company experienced.**

1. Was your company classified as a small public corporation as of July 2002?

Yes No

2. Has your company incurred costs as related to complying with the Sarbanes-Oxley Act of 2002?

Yes No

3. Has your company gone private due to the costs associated to complying with the Sarbanes-Oxley Act of 2002?

Yes No

4. Has your company de-registered due to the costs associated to complying with the Sarbanes-Oxley Act of 2002?

Yes No

5. Has your company experienced an increase in legal costs related to complying with the Sarbanes-Oxley Act of 2002?

Yes No

If yes, what percentage of increase \_\_\_\_\_

6. Has your company experienced an increase in internal control documentation costs related to complying with the Sarbanes-Oxley Act of 2002?

Yes No

If yes, what percentage of increase \_\_\_\_\_

7. Has your company experienced an increase in technology costs related to complying with the Sarbanes-Oxley Act of 2002?

Yes No

If yes, what percentage of increase \_\_\_\_\_

8. Has your company experienced an increase in staff addition costs related to complying with the Sarbanes-Oxley Act of 2002?

Yes No

If yes, what percentage of increase\_\_\_\_\_

9. Has your company experienced an increase in training costs related to complying with the Sarbanes-Oxley Act of 2002?

Yes No

If yes, what percentage of increase\_\_\_\_\_

10. Do you feel the implementation of the Sarbanes-Oxley Act restored shareholder confidence in your company?

Yes No



**APPENDIX B**

Date:

Name

Company

Address

City, State, Zip

Dear \_\_\_\_\_ :

I am currently working on my Master's of Science Degree in Occupational and Technical Studies majoring in Business and Industry Training. As part of the degree program, I am conducting a study. The focus of this study is the ability for small businesses to cope with the increased costs of complying with the Sarbanes-Oxley Act of 2002.

As Chief Financial Officer of your company, I feel you will have the knowledge and information necessary to answer questions regarding the Sarbanes-Oxley Act of 2002. Your input is very important because it will help me to obtain the high response rate needed to successfully complete the study and construct my analysis.

I have enclosed a brief survey designed to collect data regarding the major areas of costs, the percentages of increased costs, shareholder confidence, as well as if any small businesses de-registered or went private due to the costs of complying with the Sarbanes-Oxley Act of 2002. Please complete the survey and return it to me in the self-addressed, stamped envelope enclosed for your convenience by \_\_\_\_\_, 2004.

To ensure the privacy of the identity of participants, a number has been typed in the bottom right hand corner of each survey in order to keep track of who has completed the survey. Upon receipt of all surveys, this information will be destroyed. All answers and comments made on this survey will remain completely anonymous. The study will not contain any company names.

Thank you for taking time to complete the enclosed survey. If you have questions or need additional information, you may contact me at 304-324-3240. I look forward to receiving your completed survey soon.

Sincerely,

Debra B. Cline

Enclosure

**APPENDIX C**

Date

Name  
Company  
Address  
City, State, Zip

Dear :

Several weeks ago, you should have received a survey asking for information on the costs related to complying with the Sarbanes-Oxley Act of 2002. The information that you provide will allow me to collect data regarding the major areas of costs, percentages of increased costs, shareholder confidence, as well as if any small business de-registered or went private due to the costs of complying with the Sarbanes-Oxley Act of 2002.

If you have not yet completed the survey, please do so as soon as possible. Also, I have enclosed another copy of the survey in case you did not receive the previously mailed copy. A self-addressed, stamped envelope is also enclosed for your convenience.

Thank you for your assistance in this matter. If you have any questions, please contact me at 304-324-3240.

Sincerely,

Debra B. Cline

Enclosure

## APPENDIX D

Question #5 Legal Costs		Percentage	Question #6 Internal Control Documentation Costs	
1.	Yes	10%	Yes	25%
2.	No		Yes	25%
3.	Yes	50%	Yes	60%
4.	Yes	40%	Yes	30%
5.	Yes	10%	Yes	100%
6.	Yes	5%	Yes	10%
7.	No		No	
8.	Yes	3%	Yes	2%
9.	No		Yes	25%
10.	Yes	10%	No	
11.	No		Yes	2%
12.	Yes	3%	Yes	5%
13.	Yes	5%	Yes	10%
14.	Yes	10%	Yes	10%
15.	Yes	20%	Yes	15%
16.	No		No	
17.	Yes	2%	Yes	20%
18.	Yes	10%	Yes	10%
19.	Yes	15%	Yes	50%
20.	Yes	5%	Yes	10%
21.	Yes	8%	Yes	15%
22.	No		No	
23.	No		Yes	10%
<b>Yes-16</b>			<b>Yes-19</b>	
<b>No-7</b>			<b>No-4</b>	

Question #7 Technology Costs		Percentage	Question #8 Staff Addition Costs		Percentage
1.	Yes	2%	No		
2.	Yes	20%	No		
3.	No		No		
4.	Yes	10%	No		
5.	No		No		
6.	No		Yes		2%
7.	No		No		
8.	Yes	10%	No		
9.	No		Yes		5%
10.	No		No		
11.	No		No		
12.	Yes	10%	No		
13.	Yes	7%	Yes		2%
14.	Yes	5%	Yes		5%
15.	Yes	5%	Yes		5%
16.	No		No		
17.	No		Yes		1%
18.	No		No		
19.	No		No		
20.	Yes	20%	No		
21.	Yes	10%	No		
22.	No		No		
23.	No		No		
<b>Yes-10</b>			<b>Yes-6</b>		
<b>No-13</b>			<b>No-17</b>		

	<b>Question #9 Training Costs</b>	<b>Percentage</b>
1.	Yes	10%
2.	No	
3.	Yes	30%
4.	Yes	10%
5.	Yes	10%
6.	Yes	5%
7.	No	
8.	Yes	3%
9.	Yes	5%
10.	Yes	25%
11.	Yes	1%
12.	No	
13.	No	
14.	Yes	10%
15.	Yes	25%
16.	Yes	2%
17.	Yes	5%
18.	Yes	5%
19.	No	
20.	Yes	5%
21.	Yes	5%
22.	Yes	10%
23.	Yes	5%

**Yes-18**

**No-5**