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The New Age of Accounting Regulation in Canada and the United States

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Abstract

This paper reviews major differences between the accounting regulatory systems in Canada and the United States. In the U.S., the Sarbanes-Oxley Act of 2002 governs responsibilities of management, auditors, and Boards of Directors related to internal control over financial reporting. In Canada, a series of Multilateral Instruments under provincial jurisdiction serves similar objectives. As compared to the U.S., the Canadian system is more decentralized and principles-based, allowing a greater degree of responsibility to the accounting profession for standard setting and oversight. The Canadian approach has resulted in weaker regulation, slower implementation, and greater influence by the accounting profession. These findings imply that accounting regulations should be tailored to fit the political and institutional structures of the adopting country.

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The New Age of Accounting Regulation in Canada and the United States: Divergent Paths or Parallel Tracks? [1]

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The New Age of Accounting Regulation in Canada and the United States: Divergent Paths or Parallel Tracks?

Introduction

Prominent business scandals in the early 2000's, such as those involving Enron and WorldCom, resulted in loss of confidence in the business community and the accounting profession. The Sarbanes-Oxley Act (SOX) (US Congress, 2002) was a major US regulatory response in order to improve corporate governance and to regain corporate credibility and investor confidence. Canadian companies that trade on US stock exchanges and Canadian subsidiaries of US companies must also comply with SOX. In addition, Canadian securities regulators introduced similar requirements for Canadian public companies (Canadian Securities Administrators (CSA), 2005a, 2005b, 2005c, 2005d, 2006). Furthermore, some private companies and public and non-profit organizations have also strengthened their internal control to enhance their reputations as responsible and credible organizations.

The Sarbanes-Oxley Act is one of the best known accounting regulations. It governs the responsibilities of management, auditors, and Boards of Directors in ensuring effective control over financial reporting by public companies. The Act established the Public Company Accounting Oversight Board (PCAOB) with broad powers to regulate auditing and auditors: for example, to set auditing standards, to enforce compliance with the Act, to investigate violations, and to impose sanctions (PCAOB, 2004). The most extensive requirements of SOX are those in Section 404, which requires senior management to establish and maintain adequate internal control over financial reporting, assess the effectiveness of control, and certify and report the conclusions of these assessments. In addition, it requires independent auditors to certify and report on the adequacy of management's internal control assessments.The Canadian regulations are similar to SOX, but notable differences also exist. Securities regulation in Canada falls under provincial jurisdiction under the Canadian Constitution.[1] The Canadian Securities Administrators (CSA) worked with provincial administrators and legislators to enact regulations stipulated in the revised Multilateral Instrument, MI 52-109, now effective in all provinces (CSA, 2006). In contrast to SOX, reporting can be done in conjunction with management discussion and analysis (MD&A) in the financial statements, and separate reports are not required. In addition, auditor certification of management control assessments is not required at all (CSA, 2005c, 2006). Although the Canadian regulations are somewhat weaker than SOX, once fully implemented, they require equal effort on the part of management to implement internal control and systems, and to assess and report control effectiveness.

As neighbouring countries with similar history, language, and culture, Canada and the US could be expected to have very similar regulations and approaches to regulation. Although this may be true to a degree, significant differences are found in accounting regulation in the two countries. This paper reviews the major differences and their implications for the major players. It specifically uses the recent and extensive regulation of internal control over financial reporting required by SOX and by Canadian regulations as the main example. It contributes to the accounting literature and practice by highlighting that different approaches have been used, and are useful, in accounting regulation and standard setting in different jurisdictions. These

experiences can help other jurisdictions implement and improve their regulations, systems, and processes, as well as aid academics to refine theory in this relatively new and under-researched area. Specific areas examined include: theories of accounting regulation; major regulators of accounting; differences in major accounting regulations; differences in roles for boards of directors, management, and auditors; and differences in accounting regulation strategies. However, it should be noted that these regulations are complex in both countries and involve both accounting and legal professions, as well as multiple levels of government and other agencies. Therefore, a full discussion of the regulations is not possible; nonetheless, some key examples are provided to highlight such complexities.

Theories and Strategies of Accounting Regulation and Standard Setting

The justification of and the strategies for enacting accounting regulations and setting accounting standards are similar to those for other legislation and regulations. Gaffikin (2005) argued that accounting regulations cannot be considered in isolation but need to be viewed within the broader legal frameworks and systems for different countries. Regulation can arise from three primary sources: market, governmental legislators and regulators, and the accounting profession.[2] In some cases, more or less independent agencies, for example SEC and PCAOB in the US and the Canadian Public Accountability Board (CPAB) and the Auditing and Assurance Standards Oversight Council (AASOC) in Canada, have also been established to carry out various regulatory and enforcement activities. The relative strengths and powers of these parties can vary in different countries, depending on the prevailing economic, social, political, and ideological conditions, and the existing institutions and systems (Puxty, Willmott, Cooper, and Lowe, 1987). Consequently, the approaches taken and the regulations themselves are expected to vary among different countries even with advanced market-based economies.

Regulation has often been justified using the concept of *information asymmetry*, based on economic principles (Gaffikin, 2005).[3] One form of information asymmetry, called adverse selection, implies that some parties to a business transaction have internal information that other parties do not have. As such, they may have an unfair advantage and can take action for their own personal economic benefit (Scott, 2006). Regulation that prohibits certain actions and activities, or requires disclosure of them, presumably helps level the playing field for all parties. For example, securities regulations to prevent insider trading by corporate executives further this objective. Another form of information asymmetry, called moral hazard, is based on the premise that the parties to a business transaction, whose actions cannot be observed by other parties, can shirk their duties (Scott, 2006). For example, as shareholders cannot directly observe the actions of corporate executives in managing the corporation on their behalf, executives can neglect to take action that is in the best interests of shareholders. In these situations, incentive contracts can be designed to promote desired behaviours, and measures, such as the net income and share price, used to assess managerial effort. However, as both can be manipulated by management, regulation may still be required to minimize opportunities for and to detect manipulation.

It has also been argued that theories based on economic principles can provide only limited explanations for regulation, and that regulation is as much, if not more, a political activity as an economic activity (Scott, 2006). Three politically-motivated theories are *public interest theory*, *interest group theory*, and *institutional theory*. Public interest theory posits that regulation is

required to protect public interests, given imperfect market mechanisms, and that regulators operate to maximize social welfare. Market forces are unable to adequately control the amount and type of regulation and accounting information supplied and demanded, as both are public goods.[4] The providers may be reluctant to produce appropriate information and the users unable or unwilling to pay the true cost of information (Scott, 2006). In addition, the "public" is not a homogeneous group with uniform interests and demands for regulation (Gaffikin, 2005), and such interests can change over time (Day, 2001). Instead, it consists of groups of individuals with common interests, but interests that are different from, and often conflicting with, those of other groups (Baker, 2005). The interest group theory posits that special interest groups lobby the regulators for their own benefit (Van Lent, 1997). Furthermore, regulatory bodies, standard setters, and accounting firms themselves are special interest groups with their own power positions and interests in mind (Hirshleifer, 1976; Puro, 1984; Rahman, Ng, and Tower, 1994; Scott, 2006).[5] Therefore, determining the right type and amount of regulation is difficult, if not impossible, and regulations often represent majority consensus or compromises among conflicting interests, instead of ideal or optimum solutions. Furthermore, Day (2001) and Gilfedder and Ó hÓgartaigh (2001) described the lack of user participation and the overrepresentation of large preparers of financial statements and accounting firms in setting accounting standards. Although the interest group theory may be more appropriate than the public interest theory for describing accounting regulation and standard setting (Scott, 2006), it is not sufficient in itself, without considering the broader social context (Tinker, 1984; Gaffikin, 2005). The institutional theory, which posits that regulation is shaped more by social and organizational settings than by individual or group interests (Baldwin and Cave, 1999; Tinker, 1984), may be more useful for explaining recent developments in accounting regulation.

Countries have adopted different strategies or approaches to accounting regulation and setting standards. Baldwin and Cave (1999) identified eight strategies of regulation, with four being possibly applicable to accounting regulation: command-and-control regulation, self-regulation, incentives-based regulation, and disclosure regulation. In the command-and-control strategy, the regulator establishes acceptable activities, rules, procedures, and standards; enforces compliance; and imposes penalties for violations. The regulation of securities markets in the US by SEC exhibits strong characteristics of this strategy. Self-regulation relies on professional bodies to establish rules, procedures, and standards for their members, and to develop systems for monitoring and enforcing them. This is a typical strategy for setting accounting standards in many countries, Canada being a good example. Incentives-based regulation provides financial or non-financial incentives to achieve desired policy objectives on a voluntary compliance basis without excessive rules. Providing tax credits, guidelines, and other support mechanisms to encourage voluntary adoption of desirable activities are examples of this strategy. Penalties for non-compliance with securities regulations can also serve as negative incentives and promote compliance. Disclosure regulation strategy involves requirements for the disclosure of certain information, for example, extensive disclosures of financial and operational information under the securities regulations. Each strategy poses specific strengths and weaknesses, from the perspectives of different stakeholders, which must be carefully balanced by the regulator.

The basic strategies or approaches to accounting regulation and accounting standard setting have been categorized as either the Anglo-American approach or the continental approach. The Anglo-American approach is characterized by:

> [A] strong accounting profession, a somewhat limited role of government, the importance of securities markets for raising equity capital, and an emphasis upon the *true and fair* view of audited financial statements [emphasis original] (Wolk, Tearney, and Dodd (2001), p. 715).[6]

On the other hand, the continental approach relies on a relatively weak accounting profession, strong governmental influence on accounting regulation, and emphasis on debt financing instead of equity capital. Major characteristics of the Anglo-American approach are evident, for example, in the US, UK, Canada, and Australia; whereas the continental approach is dominant in France, Germany, and Japan (Wolk et al., 2001).[7] Major characteristics of the continental model are also exhibited in Italy, Spain, and Greece (Di Pietra, McLeay, and Riccaboni, 2001; Blake and Amat Salas, 2001; Ballas, Hevas, and Neal, 2001). In particular, Di Pietra et al. (2001) described Italian accounting regulation to be firmly political and legislative. However, there has been significant convergence of the two approaches during the past few years in response to the globalization of business and capital markets. For example, greater private-sector and professional influence in setting accounting standards has been noted in France and Austria, two continental countries, bringing them closer to the Anglo-American approach (Merkl-Davies, 2004; Colasse and Standish, 2004). While income manipulation or "creative accounting" has traditionally been associated with the Anglo-American model, Blake and Amat Salas (2001) provided examples of it also in Spain, with a more continental approach. On the other hand, greater legislative and regulatory control has emerged in the US and Canada, as is demonstrated in this paper, moving them somewhat closer to the continental model.[8] Nonetheless, this paper presents evidence that this classification may be too simplistic and that significant differences also persist between the standards and standard-setting approaches within the Anglo-American group, namely Canada and the US.

Accounting Regulators in Canada and the US

Both legislators and professional accounting bodies play important roles, although in somewhat different capacities and proportions, in establishing and overseeing accounting regulations in Canada and the US. The roles of major regulatory agencies are discussed in this section and summarized in Table 1.

[Table 1]

In both Canada and the US, professional accounting bodies serve important functions in establishing and regulating accounting standards. In Canada, the Canadian Institute of Chartered Accountants (CICA), through its three boards, conducts research into current business issues and sets accounting, auditing, and assurance standards. The Accounting Standards Board (AcSB) sets accounting and reporting standards for profit-oriented and non-profit organizations. The Public Sector Accounting Standards Boards (PSAB) sets accounting and reporting standards for federal, provincial, and local governments and boards. The Auditing and Assurance Standards Board (AASB) sets auditing and assurance standards for all sectors. In the US, the Financial Accounting Standards Board (FASB) has a mission similar to that of CICA. FASB establishes and improves financial accounting and reporting standards for the private sector and the federal

government, and provides guidance and education to issuers, auditors, and users of financial information. The Governmental Accounting Standards Board (GASB) serves the same role for state and local governments. The Financial Accounting Standards Advisory Council (FASAC) advises FASB on technical issues, project priorities, selection and organization of task forces, and other relevant matters. The Financial Accounting Foundation (FAF) oversees and funds activities of FASB and GASB, and selects members of both Boards and their advisory councils. However, setting accounting standards in the US has not historically been completely independent of the influence of the Securities and Exchange Commission (SEC). As expressed by Zeff (1995):

> The SEC's accounting staff has kept a close watch over the issues, agendas, priorities, and the tentative positions of the [accounting] standard setter, and has not been reluctant to intervene with its views … (Zeff, 1995, p. 56).
>
> Without question, the agendas of the successive [accounting] standard setters and many of their pronouncements have been powerfully shaped by the signals emanating from the SEC (Zeff, 1995, p. 61).

In the US, the SEC regulates and oversees securities markets and enforces securities legislation, notably the Sarbanes-Oxley Act (SOX) (2002).[9] SOX has been considered to be "the most significant piece of securities legislation since the 1930s" (Whitestone, 2005, p. 382), notably since the Securities Act (US Congress, 1933) and the Securities Exchange Act (US Congress, 1934). The Public Company Accounting Oversight Board (PCAOB) was created under SOX as an oversight agency. Its major mandate is inspecting and registering public accounting firms that prepare audit reports for public companies. PCAOB can establish, adopt, or modify auditing, quality control, ethics, independence, and other standards for public company audits. However, these standards must be approved by SEC (SEC, 2007). PCAOB enforces compliance with SOX, its own rules, professional standards, and securities laws relating to the preparation and issuance of audit reports and the related obligations and liabilities of accountants. It is also charged with investigating registered companies for potential violations of applicable rules relating to audits and imposing sanctions for violations. In order to facilitate reporting and enforcement, particularly in smaller companies, SEC recently agreed to coordinate the enforcement of some key areas of SOX with PCAOB (SEC, 2007).

In Canada, securities regulation is within provincial jurisdiction.[10] Securities regulators from each province have joined to form the Canadian Securities Administrators (CSA). CSA is primarily responsible for developing a harmonized approach to securities regulation across Canada.[11] Oversight functions similar to those of PCAOB are handled by several different oversight agencies. The Canadian Public Accountability Board (CPAB) is an independent non-profit organization, established in 2002 by CSA, CICA, and the Office of the Superintendent of Financial Institutions (OSFI). Under CPAB, CA firms engaged in public company audits must undergo more frequent and rigorous inspections, implement new Canadian auditor independence rules, adopt second partner reviews of all public company audits, and establish new quality control standards. The Accounting Standards Oversight Council (AcSOC) oversees activities of the Accounting Standards Board (AcSB) and the Public Sector Accounting Board (PSAB). In addition, the Auditing and Assurance Standards Oversight Council (AASOC) was established in

2002 to oversee the activities of the Auditing and Assurance Standards Board (AASB). AASOC provides input, strategic direction, and user perspective into setting auditing and assurance standards. At the provincial level, the Province of Ontario has played a leading role in securities regulation (Cox, 2004), and created the Public Accountants Council (PAC) in 2005 to set standards for public accounting and to certify that professional accounting bodies in Ontario meet these standards.

In summary, accounting regulation and oversight in the US tend to be more centralized, emphasizing the role of SEC and PCAOB. On the other hand, the Canadian system relies on both professional and legislative approaches. CPAB is funded by accounting firms and it is not subject to any regulatory oversight. In addition, a disproportionately large number of CPAB members are accountants, resulting in some questioning of its independence (Pritchard and Puri, 2006). CICA and its boards also play key roles both in standard-setting and oversight functions. Even on the legislative and enforcement front, a great deal of voluntary collaboration is necessary among the provinces to reach a national-level consensus and to enact uniform legislation for each province. Pritchard and Puri (2006) concluded that Canada relies largely on self-regulation, whereas the US relies almost exclusively on government regulation. Considering the fragmented regulatory system in Canada, Whitestone (2005) argued that it is difficult for regulators to pursue fraud charges and for individual investors to take legal action against companies.

Accounting Regulations in Canada and the US

Canadian accounting regulations for internal control over financial reporting bear some marked similarities to SOX, as they were modelled after SOX, but notable differences also exist. In addition, the regulations in both countries are still a work in progress after several years of planning and implementation. The major differences in the structure of the relevant Canadian and US regulations are outlined in Table 2.

[Table 2]

In the US, the Sarbanes-Oxley Act (SOX) provides the legislative basis for internal control regulation. It establishes the responsibilities of management, auditors, and Boards of Directors for effective control over financial reporting by public companies. The most extensive requirements of SOX are those found in Section 404, which require senior management (CEO and CFO) to establish and maintain adequate internal control over financial reporting, assess the effectiveness of internal control, and certify and report the conclusions of these assessments. In addition, it requires independent auditors to certify and report on the adequacy of management's internal control assessments. While SOX is US legislation, Canadian and other foreign companies that trade on US stock exchanges must also comply with these regulations. Large US companies ('accelerated' filers with market value of common equity of at least $75 million), have already had to comply with both management and auditor certification requirements for fiscal years ending after November 14, 2004 (SEC, 2004). The compliance deadlines for small US companies and for foreign companies have been extended several times (SEC, 2005). According to the latest announcement (SEC, 2006), small US and foreign companies ('non-accelerated' filers with market value of less than $75 million) have to comply for fiscal years

ending after December 14, 2007 for management certification and December 14, 2008 for auditor certification. Large foreign companies have to comply for fiscal years ending after July 14, 2006 for management certification, and July 14, 2006 (if market value is at least $700 million) or July 14, 2007 (if market value is between $75 and $700 millions) for auditor certification. All new US and foreign public companies have to comply commencing for the second year of their operations.

The main Canadian regulations for internal control over financial reporting are articulated in Multilateral Instrument 52-109, applicable to all publicly listed Canadian companies in all provinces, except investment funds and companies that comply with similar certification requirements under SOX (CSA, 2004a, 2006).[12] After considerable collaboration among provincial legislators and the Canadian Securities Administrators (CSA), the instrument was ratified in all jurisdictions. Consistent with SOX, it calls for management certification of the design and operating effectiveness of internal control over financial reporting. The design certification requirements become effective for years ending after June 29, 2006, and the effectiveness certification requirements are proposed for years ending after June 29, 2008 (CSA, 2006, 2007a). Such reporting can be accomplished as a component of management discussion and analysis (MD&A) in financial statements, as compared to a separate component in annual reports that is required for SOX. Contrary to SOX, auditor certification of management control assessments is not required at all in the revised MI 52-109 (although it had initially been proposed in MI 52-111) (CSA, 2005c, 2006). In its guidance-providing role, CICA has also issued guidelines to help small companies implement internal control requirements, following similar previously released guidelines intended for management and directors (Goodfellow and Willis, 2007, 2006a, 2006b).

Although the ink was barely dry on the above-discussed US and Canadian regulations, proposals for further modifications have already been presented in both countries.[13] In the US, PCAOB released the Audit Standard No. 5 to replace the Standard No. 2 (PCAOB, 2007). The new standard aims to streamline audits of internal control over financial reporting by focusing on the most important controls and by eliminating unnecessary audit procedures and details, and to scale audits based on company size. There is still also a possibility for further compliance extensions for small US and foreign companies, depending on the availability of appropriate and timely guidance. In Canada, standards addressing public accountants' responsibilities in conducting audits of internal control over financial reporting, which are based on agreed-upon procedures with no assurance provided, were adopted in the *Assurance Handbook* in April 2007 and became effective May 1, 2007 (CICA, 2006).[14] The Auditing and Assurance Standards Board (AASB) also plans to revise the Canadian auditing standards based on the new US standard. This example illustrates that Canada has often waited for US outcomes before embarking on its own regulatory and standard-setting initiatives.

It is obvious that the regulation of internal control over financial reporting is here to stay in both countries. At the same time, these regulatory systems continue very much to be a work in progress, subject to ongoing refinement and possibly increasingly stringent requirements, as more experience is acquired. The regulatory system in Canada relies on provincial collaboration, as compared to the more centralized system in the US, and setting auditing standards in Canada is primarily the responsibility of the accounting profession, as opposed to being the responsibility of a federal regulatory agency in the US. In addition, the Canadian standard-setting approach in

general is more principles-based than the US approach, which tends to be more rules-based, although PCAOB claims the Audit Standard No. 5 to be more principles-based than the Standard No. 2. Due to these factors, significant differences in regulations and standards could be expected. Canada has generally adopted a 'wait-and-see' approach and mirrored its regulations and standards on those of the US. Two notable differences in the Canadian requirements are the more streamlined reporting requirements and the lack of auditor certification requirement for management's control assessments. These differences result in greater responsibility by the management of Canadian companies for internal control over financial reporting.

Responsibilities of Management, Auditors, and Boards of Directors

In implementing internal control regulations, the Boards of Directors and their audit committees, management, and auditors play important roles. Such roles vary in the US and Canadian systems. The main responsibilities of the three parties are discussed in this section and summarized in Table 3.

[Table 3]

In the Sarbanes-Oxley Act (SOX), Section 301 establishes requirements relating to the audit committee's responsibilities. It covers issues such as selecting, compensating, retaining, and overseeing independent audit firms; ensuring the independence of audit committee members; establishing procedures for handling confidential and anonymous complaints regarding accounting, internal control, and auditing; and engaging advisors. In addition, Section 201 specifies non-audit services that would impair auditor independence; Section 202 deals with the pre-approval of audit and non-audit services by the audit committee and the disclosure of audit fees; and Section 203 limits the term of contracts for audit services to no more than five consecutive years. Furthermore, Section 406 requires a company to disclose whether it has adopted a code of ethics that applies to the company's principal executive officer, principal financial officer, principal accounting officer, and controller, and if not, to explain why. As a final example, Section 303 prohibits officers and directors, and persons acting under their direction, from taking actions to fraudulently influence, coerce, manipulate or mislead the auditor for the purpose of rendering the financial statements materially misleading.

In Canada, the audit committee's responsibilities are set out in Multilateral Instrument (MI) 52-110 (CSA, 2004b). It is concerned with appointing and overseeing external auditors; reviewing financial statements, MD&A, and earnings press releases before their publication; establishing procedures for handling anonymous complaints on accounting, internal control, and auditing matters; and approving policies aimed at ensuring auditor independence. For example, MI 52-110 requires each public company to have an audit committee with a minimum of three members, to require the external auditor to report directly to the audit committee, and to disclose the names of the audit committee members and whether the members are independent and financially literate. In addition, the National Policy (NP) 58-201 (CSA, 2005b) deals with ensuring integrity of chief officers, establishing a culture of integrity throughout the company, identifying principal risks, and ensuring appropriate systems to manage risks. The Canadian requirements for risk management are interesting in that risk management has typically been considered to be a management function, instead of a governance function, and in that SOX does

not have explicit corresponding requirements. The establishment and enforcement of professional integrity and conduct standards in Canada is primarily the responsibility of CICA (CICA, 2002, 2003, 2006, 2007).

The responsibilities of management are very similar under both the US and Canadian regulatory systems. The Canadian requirements are stipulated in the Multinational Instrument (MI) 52-109 (CSA, 2006) and the US requirements in Sections 302 and 404 of SOX. In both cases, the CEO and the CFO must certify that the financial statements do not contain material misstatements and omissions, that adequate *disclosure control* and *internal control over financial reporting* exist, and that they are responsible for designing and maintaining such controls.[15] They must also evaluate the effectiveness of internal control and report their conclusions, along with any material changes in internal control and their effects. The main difference between the Canadian and the US requirements is that this reporting can be accomplished as part of the management discussion and analysis (MD&A) accompanying financial statements in Canada, whereas separate disclosures in the financial reports are required in the US.

As to the auditor's responsibilities, SOX (Sec. 404) requires a company's auditors to attest to, and report on, the internal control assessments made by management. This attestation is to be made in accordance with standards for attestation engagements issued by PCAOB. The auditor must also report certain matters to the audit committee, including critical accounting policies, alternative accounting treatments the auditor has discussed with management, the ramifications of alternative treatments, and the treatment preferred by the auditor (Sec. 204). There is no audit requirement for management's internal control assessment reports in Canada. However, the *Assurance Handbook* (CICA, 2007, Sec. 5751) establishes standards for auditor communication with the audit committee in general on matters arising from financial statement audits, and the new Section 9110, effective May 1, 2007, addresses public accountants' responsibilities specifically in conducting reviews of internal control over financial reporting and the form and content of such reports (CICA, 2006, 2007).

In summary, the management of public companies in both Canada and the US is responsible for similar core requirements for internal control over financial reporting in that it must establish and maintain proper internal control procedures in order to ensure timely, reliable, and effective financial reporting. Roles of audit committees are also comparable and involve overseeing the external auditor, ensuring the independence of the external auditor and audit committees, and designing appropriate processes for handling confidential complaints.[16] In addition to audit committees, the Boards of Directors of Canadian public companies are required to identify major risks and to establish appropriate risk management strategies and practices. One key difference in the Canadian approach is a significantly reduced formal role for independent auditors, as no certification of management's internal control assessments is required. Another major difference is the significantly more prominent role of professional accounting bodies, that is, CICA and its boards, in setting professional independence and integrity standards in Canada. In the US, these issues are regulated by SOX and the standards set by PCAOB.

Accounting Regulation Strategies in Canada and the US

As discussed in Section 2, various countries have adopted different strategies for accounting regulation. In this section, strategies adopted in Canada and the US are compared and the extent of their usage summarized in Table 4. Baldwin and Cave's (1999) general categorization of regulation strategies is modified, as applicable to accounting regulation. Of the eight strategies identified by Baldwin and Cave, four strategies could apply to accounting regulation: command-and-control regulation, self-regulation, disclosure regulation, and incentives-based regulation. The command-and-control and self-regulation approaches are viewed as opposite core approaches, and the other two can be used to supplement either one. The degree to which these strategies are used in each country is evaluated as extensive, moderate, or minimal, and examples of relevant legislation and regulations are provided. Although this assessment may involve some subjective judgment, it illustrates some interesting contrasts in accounting regulation strategies adopted in the two countries.

[Table 4]

The main strategy of accounting regulation in the US has been the command-and-control strategy. This strategy has been used extensively, for example, through more centralized control over securities regulation granted to SEC by the National Securities Markets Improvement Act (US Congress, 1996), and particularly to SEC and PCAOB by the Sarbanes-Oxley Act of 2002. PCAOB's authority to set auditing standards and to inspect public auditing firms clearly diminishes the self-regulatory authority of the accounting profession. Heavy penalties for non-compliance are another manifestation of the command-and-control strategy. SOX (Sec. 1106) increased maximum penalties in the Securities Exchange Act (US Congress, 1934) for willful provision of false or misleading information by corporate executives; fines for up to $5,000,000, and/or imprisonment for up to 20 years. SOX (Sec. 802 and 807) provides for fines and/or maximum imprisonment for knowingly falsifying documents and for defrauding shareholders for up to 20 and 25 years, respectively. The new sweeping powers of SEC and PCAOB under SOX, along with the rules-based approach to setting standards, demonstrate extensive use of the command-and-control strategy and reduce self-regulation of the accounting profession to a moderate level.

While the command-and-control strategy is also evident in Canada[17], the extent of its use can be characterized as only moderate. Although the Canadian Securities Administrators (CSA) facilitated the development of common provincial regulation—particularly Multilateral Instrument MI 52-109—the provinces and their securities regulators are responsible for enactment and enforcement. MI 52-109 does not address penalties, leaving them to provincial regulators (CSA, 2004a). However, the CSA Staff Notice 57-302 stipulates that companies failing to file internal control assessment certificates in accordance with MI 52-109 may be subject to "cease trade" orders (CSA, 2004c), depending on the jurisdiction.[18] In addition, the Canadian Institute of Chartered Accountants and oversight boards—all heavily staffed by accountants—are primarily responsible for the development and enforcement of auditing standards and rules of professional conduct in Canada, although provincial securities commissions and stock exchanges also have their own rules of conduct. Given the more principles-based approach to setting accounting and auditing standards, the accounting

profession in Canada still has extensive self-regulatory capacity. Therefore, the use of the command-and-control strategy in Canada is considered to be moderate, and the use of self-regulation extensive.

Both countries use disclosure regulation, but the US does so somewhat more extensively than Canada. For example, Multilateral Instrument MI 58-101 requires disclosure of corporate governance practices established in National Policy NP 58-201 (CSA, 2005b, 2005e), and Multilateral Instrument MI 52-110 requires disclosure of education, experience, independence, and financial literacy of audit committee members (CSA, 2004b). Similar issues are addressed in Sections 406 and 407 of SOX. Section 406 requires disclosure of whether companies have adopted a code of ethics applicable to chief executive and financial officers and controllers, and if not, to explain why not. Section 407 requires disclosure of whether the audit committee has at least one financial expert and whether this member is independent. In addition, Section 202 requires disclosure of audit and non-audit services performed by the auditor. Non-audit services must have been pre-approved by the audit committee. Furthermore, the Section 404 core disclosure requirements for internal control over financial reporting are stronger than those in MI 52-109, as auditor certification of management's control assessments is not required in Canada. Therefore, the use of disclosure regulation is classified as moderate in Canada and moderate-extensive in the US.

As regulators in both countries have used the first three strategies at least moderately, they have not relied extensively on incentives-based regulation. An example of non-financial incentives to help companies implement new regulations in Canada is a series of guidance documents by CICA, specifically targeted to managers, directors, and small businesses. Some financial relief associated with duplicate compliance requirements is provided to Canadian companies complying with SOX, as they may file US documents with Canadian regulators. Penalties, as negative incentives, are intended to promote compliance by imposing significant negative financial consequences or threat of imprisonment for non-compliance. Such "heavy-handed" methods are more characteristic of the command-and-control strategy than the incentives-based strategy. Neither country provides financial rewards to help implement regulations and to encourage compliance. Most companies have, at significant cost, used services of consulting companies to implement the necessary regulatory requirements. The financial burden has been relatively heavier on smaller companies than larger ones.[19] A theoretical alternative would have been to provide some financial relief to companies in the form of tax credits or rebates (Baldwin and Cave, 1999). Therefore, the use of incentives-based regulation is considered to be minimal in the US and minimal-moderate in Canada.

It should be noted that no single strategy is clearly better than the others, and no optimum strategy exists. Each strategy possesses specific strengths and weaknesses, from the perspectives of different stakeholders, which must be carefully balanced by regulators. As a result, combination strategies may also be used. For example, self-regulation may be favoured, and, only if it fails, government regulation or oversight implemented. Baldwin and Cave (1999) referred to this strategy as enforced self-regulation. This explanation provides a reasonable rationale for the enactment of SOX in the face of large-scale corporate scandals, such as those involving Enron and WorldCom, and implies a loss of confidence in, if not a failure of, the self-regulating accounting profession (Davis, 2003-2004). Historically, the Securities Act (US

Congress, 1933) and the Securities Exchange Act (US Congress, 1934) were also enacted after the stock market crash during economic depression. The Canadian regulatory system may also be considered as enforced self-regulation, as extensive standard-setting authority remains in the hands of the accounting profession, but subject to oversight by the Canadian Public Accountability Board (CPAB), the Accounting Standards Oversight Council (AcSOC), and the Auditing and Assurance Standards Oversight Council (AASOC).

In summary, significant differences in accounting regulation strategies exist in Canada and the US. These findings may be surprising, considering that these two democratic neighbouring countries are fundamentally similar in terms of history, language, and culture. However, it has been argued that differences in capital markets and corporate governance structures in Canada warrant different strategies. These differences were described, for example, by Davis (2003-2004). A large number of Canadian corporations are smaller than typical US corporations and more closely held by single shareholders or small groups of shareholders, and many companies also hold shares of other companies. In addition, there can also be significant interrelationships among members of Boards of Directors, as the same individuals often serve on several boards. Consequently, the shareholders of Canadian companies may not be affected by information asymmetry arising from the separation of ownership and control to the same extent as shareholders of large widely-held US corporations.

Conclusion

This paper reviews major differences between the US and Canadian accounting regulatory systems, in particular requirements for internal control over financial reporting stipulated in the Sarbanes-Oxley Act (SOX) (US Congress, 2002) and Canadian requirements in a series of Multilateral Instruments (MI) (Canadian Securities Administrators (CSA), 2005a, 2005b, 2005c, 2005d, 2006), as well as implications for the major players. Although some significant similarities between the Canadian and US regulatory systems and strategies exist, marked differences are also evident. This finding may be surprising, given the physical proximity and similarities in history, language, and culture between the two countries.

In Canada, both legislation for and oversight of internal control over financial reporting are more diverse and decentralized than in the US. In the US, the key piece of legislation is the Sarbanes-Oxley Act (2002), whereas such legislation in Canada is under provincial jurisdiction. Nonetheless, the Canadian Securities Administrators (CSA) has been able to facilitate an agreement among all provinces, as stipulated in Multilateral Instrument (MI) 52-109 (CSA, 2007b), which has recently been ratified in all Canadian provinces. In the US, the main oversight body is the Public Company Accounting Oversight Board (PCAOB) created by SOX. In Canada, oversight functions are not centralized, but they are handled by several agencies, such as the Accounting Standards Oversight Council (AcSOC), Auditing and Assurance Standards Oversight Council (AASOC), and Canadian Public Accountability Board (CPAB). The diverse regulatory system and the more consultative processes in Canada have resulted in somewhat weaker regulation and slower implementation processes.

Both SOX and MI 52-109 regulate responsibilities of management, auditors, and Boards of Directors for internal control over financial reporting, but there are also significant differences.

They set out requirements relating to the audit committee's responsibilities, but SOX also specifically prohibits officers and directors from acting improperly in order to influence audits. Both the Canadian and US requirements call for management certification of internal control with a major difference being that, according to SOX, the external auditor must also audit and certify management's internal control assessments. Without the auditor attestation requirement in Canadian companies, there is an increased onus on management to detect and report on material control weaknesses. In addition, SOX requires public companies to include management's internal control assessment reports with their annual reports, whereas MI 52-109 allows reporting as part of management discussion analysis (MD&A) in financial statements. SOX stipulates many auditor independence and professional conduct requirements that are not set out in MI 52-109 in Canada, but that are governed by CICA in their professional conduct and auditing standards.

Although Canadian requirements have been modelled after US law, and the core requirements for internal control over financial reporting are very similar, several major differences exist as to regulatory authority and strategies. The Canadian regulatory system relies heavily on both professional and legislative approaches and is generally based on broad principles, whereas the US system is more centralized and rules-based with key powers concentrated in the hands of SEC and PCAOB. CICA and its boards play key roles in both the standard-setting and oversight functions in Canada. Even on the legislative front, a great deal of voluntary provincial collaboration and consensus is necessary among the provinces in order to enact uniform provincial law. As compared with the US approach, the Canadian approach results in greater influence by the accounting profession in standard setting and greater responsibility of management for ensuring the effectiveness of internal control. However, the standards and processes are still evolving and subject to ongoing refinement, and possibly increased requirements, as more experience is acquired. As concluded by Kuras (2003-2004, p. 476), Canada has a unique challenge "to create securities regulation reform that reflects Canadian values and principles, yet which facilitates access to the capital markets of the United States in the post Sarbanes-Oxley era". These findings cast some doubt on the validity of the assumptions inherent in the Anglo-American and continental models of accounting regulation, and even in a uniform North American model. It appears that accounting regulation and strategies are influenced by the existing political and institutional structures of each country, and that, even if modelled after another country's practices, they must be adapted to fit the specific context of the adopting country.

This paper contributes to the accounting literature and practice by highlighting that different approaches have been used, and are useful, in setting accounting regulation and standards in jurisdictions with different political, legal, and social environments. These experiences can help other jurisdictions in implementing and improving their regulations, systems, and processes, as well as aid academics in refining theory in this relatively new and under-researched area. Further theoretical and empirical studies are needed to investigate the characteristics, context, and effects of accounting regulation in different jurisdictions.

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Table 1. Major Accounting Regulators in Canada and US

Characteristic	*Canada*	*US*
Accounting Standard-Setting Agencies	• Accounting Standards Board (AcSB), CICA: sets **accounting and reporting standards** for profit-oriented and non-profit organizations • Auditing and Assurance Standards Board (AASB), CICA: sets **auditing and assurance standards** for all sectors • Public Sector Accounting Standards Board (PSAB), CICA: sets accounting and reporting standards for **federal, provincial, territorial, and local governments and boards**	• Financial Accounting Standards Board (FASB): establishes and improves **financial accounting and reporting standards** • Governmental Accounting Standards Board (GASB): establishes and improves financial accounting and reporting **standards for state and local governments** • Financial Accounting Standards Advisory Council (FASAC): **advises FASB** on technical issues, project priorities, task forces, and other matters • Financial Accounting Foundation (FAF): **oversees and funds activities of FASB and GASB**, selects members of both Boards and their advisory councils
Legislative and Oversight Agencies	• Accounting Standards Oversight Council (AcSOC): **oversees activities of AcSB and PSAB** • Auditing and Assurance Standards Oversight Council (AASOC): **oversees activities of AASB** • Canadian Securities Administrators (CSA): national body of provincial securities regulators **promoting harmonized provincial securities regulations** • Provincial Securities Commissions: administer and enforce **securities legislation in their respective provinces** • Canadian Public Accountability Board (CPAB): oversees **auditing firms** engaged in public company audits (e.g., inspects firms and imposes auditor independence and quality control rules) • Public Accountants Council (PAC): **sets standards for public accounting in Ontario** and certifies that the three professional accounting bodies meet these standards	• Securities and Exchange Commission (SEC): **regulates and oversees securities markets** in US, and enforces securities legislation, notably Sarbanes-Oxley Act (SOX) (US Congress, 2002) (agreed to coordinate enforcement of Sec. 404 with PCAOB (SEC, 2007)) • Public Company Accounting Oversight Board (PCAOB), created under SOX: **inspects and registers public accounting firms**; establishes, adopts, or modifies **auditing, quality control, ethics, independence, and other standards**; enforces compliance with the Act, professional standards, and securities laws; investigates potential violations; imposes sanctions

Table 2. Major Differences in Canadian and US Accounting Regulations

Characteristic	*Canada*	*US*
Legislation and Regulations	• MI 52-109—**Certification of Disclosure in Issuer's Annual and Interim Filings** (CSA, 2004a, 2005d, 2006, 2007a) • MI 52-110—**Audit Committees** (CSA, 2004b, 2005a) • NP 58-201—**Corporate Governance Guidelines** (CSA, 2005b)	• **Sarbanes-Oxley Act** (SOX) (US Congress, 2002) • **Auditing Standard No. 2** (PCAOB, 2004) • **Auditing Standard No. 5** (PCAOB, 2007)
Applicability	All **publicly listed** Canadian companies, except investment funds and companies that comply with similar SOX regulations (Sec. 302)	All **US public companies**, their foreign subsidiaries, and **foreign companies** listed on US stock exchanges
Effective Dates[1]	• **Control "design"** certification by management applies for fiscal years ending after June 29, 2006 • **Control "effectiveness"** certification by management postponed, with proposed applicability for fiscal years ending after June 29, 2008 (CSA, 2007a)	• **Large US companies** (accelerated): management and auditor certification requirements for fiscal years ending after November 14, 2004 (SEC, 2006) • **Large foreign companies** (accelerated): fiscal years ending after July 14, 2006 for management certification, and July 14, 2006 or July 14, 2007 for auditor certification (SEC, 2006) • **All small companies** (non-accelerated): fiscal years ending after December 14, 2007 for management certification and December 14, 2008 for auditor certification (SEC, 2006)
Reporting on Internal Control	Reporting can be done as part of **management discussion and analysis** (MD&A) in financial statements	**Periodic reports** must contain management's internal control reports (SOX, Sec. 302; Sec. 404)

Note: [1]For SOX, two main categories of filers exist: accelerated and non-accelerated. Accelerated filers have market value of common equity of at least $75 million, and non-accelerated filers less than this amount. For some purposes, for example, for foreign companies, large accelerated filers with market value of at least $700 million are distinguished from other accelerated filers, with the latter allowed an extra year to comply with the auditor certification requirements (SEC, 2006).

Table 3. Major Differences in Responsibilities of Boards of Directors, Management, and Auditors

Party	*Canada*	*US*
Board and Audit Committee	**Audit committee's** responsibilities (MI 52-110): • Recommending **external auditor** to Board and overseeing external auditor • Reviewing **financial statements**, MD&A, and annual and interim earnings press releases before their publication • Establishing procedures for handling anonymous **complaints** on accounting, internal control, and auditing matters • Approving **hiring policies** regarding current and former partners and employees of current and former auditors **Board's** responsibilities (NP 58-201): • Ensuring **integrity** of chief officers and culture of integrity throughout company • Identifying **principal risks** and ensuring appropriate systems to manage them	**Audit committee's** responsibilities: • Selecting, compensating, retaining, and overseeing independent **audit firm** • Establishing procedures for handling confidential and anonymous **complaints** regarding accounting, internal control, and auditing matters by employees and others (Sec. 301) • Pre-approving all audit and **non-audit services** provided to company by auditor, and disclosing any pre-approval policies and audit services and fees (Sec. 202)
Management	**CEO and CFO** must certify that (MI 52-109): • **Financial statements** and reports do not contain material misstatements and omissions, and that they fairly present company's financial condition • They are responsible for designing, establishing, and maintaining **disclosure control** and **internal control** over **financial reporting** (DC and ICFR) • They have **designed** DC and ICFR • They have **evaluated effectiveness** of DC and ICFR and **reported conclusions** of their assessments as part of MD&A • They have reported any **changes** in DC and ICFR that have materially affected, or are reasonably likely to materially affect, DC and ICFR	**CEO and CFO** must certify that (SOX, Sec. 302, Sec. 404): • Periodic **reports filed** do not contain material misstatements or omissions, so as to be misleading • They are responsible for establishing and maintaining **disclosure control and procedures** and **internal control over financial reporting** (DC and ICFR) • They have designed and **evaluated effectiveness** of DC and ICFR • They have **reported conclusions** on effectiveness of DC and ICFR • They have disclosed to external auditor and audit committee **significant deficiencies** in design and operation of DC and ICFR and **any fraud** by management or employees • They have reported any **significant changes** in DC and ICFR or other factors that could subsequently significantly affect DC and ICFR
Auditor	• Certification of management's internal control assessments by external auditor **not required** (CSA, 2005c, 2006) • *Assurance Handbook* (Sec. 5751) provides standards for **auditor communication** with oversight bodies • *Assurance Handbook* (Sec. 9110), effective May 1, 2007, addresses auditor's responsibilities in conducting **reviews on internal control** over financial reporting and form and content of such reports	• External auditor **must attest** to, and report on, internal control assessment made by management (SOX, Sec. 404) • Before issuing audit report, external auditor must **communicate to audit committee** critical accounting policies, alternative accounting treatments and their impact discussed with management, and treatment preferred by auditor (SOX, Sec. 204)

Table 4. Major Differences in Use of Accounting Regulation Strategies in Canada and the US

Regulatory Strategy[1]	*Canada*		*US*	
	Extent of Use	*Examples*	*Extent of Use*	*Examples*
Command-and-Control	MODERATE	• CSA national facilitator of securities market regulation • Provincial securities legislation and enforcement • Offences and penalties set out in provincial legislation and enforced by provincial securities commissions • Audit committee oversees external auditor	EXTENSIVE	• Sweeping centralized powers of SEC and PCAOB to regulate securities markets, auditing standards, and accounting profession • Severe penalties and personal liability by executives for non-compliance and fraud • Audit committee oversees external auditor
Self-Regulation	EXTENSIVE	• Auditing standards primarily principles-based • CICA primarily responsible for auditing and professional conduct standards • Accountants heavily represented on standards oversight councils and CPAB	MODERATE	• Auditing standards primarily rules-based • Accounting firms must register with PCAOB
Disclosure Regulation	MODERATE	• Corporate governance practices • Qualifications and independence of audit committee members • Management's internal control assessments	MODERATE-EXTENSIVE	• Code of ethics • Financial expertise of audit committee members • Non-audit services • Management's internal control assessments • Auditor certification of management's internal control assessments
Incentives-Based Regulation	MINIMAL-MODERATE	• CICA guidance documents on internal control certification • Relief from Canadian regulations for companies complying with SOX • Some penalties as negative incentives	MINIMAL	• Severe penalties as negative incentives

Note: [1]The strategies are adapted from R. Baldwin and M. Cave (1999). *Understanding Regulation: Theory, Strategy, and Practice* (Oxford: Oxford University Press), pp. 58 – 62.

Endnotes

[1] However, a contested point for the last half-century has been whether the Federal Government would also have the power to set up a national securities regulator under the Constitution Act. The prevailing view is that the Federal Government would have power to do so. For example, in 2003 the so-called Wise Persons' Committee, which recommended the enactment of a new Canada Securities Act and the establishment of a single Canadian Securities Commission (Cox, 2004).

[2] Puxty, Willmott, Cooper, and Lowe (1987) referred to them as market, state, and community.

[3] Baldwin and Cave (1999) labelled economic-based theories as private interest theories and included public choice and capture theories in this group. Public choice theories "stress the extent to which governmental behaviour can be understood by viewing all actors as rational individual maximizers of their own welfare" (Baldwin and Cave, 1999, p. 22). Capture theories recognize the possibility of "the pursuit of the regulated enterprises' interests [by the regulator] rather than those of the public at large" (Baldwin and Cave, 1999, p. 36).

[4] "A public good is a good such that consumption by one person does not destroy it for use by another" (Scott, 2006, p. 143).

[5] Capture theorists warn of the danger that regulators may over time become more protective of the interests of those being regulated than public interests. Therefore, regulatory agencies themselves should be required to demonstrate accountability to some higher-level oversight agency or legislator to maintain their objectivity (Baldwin and Cave, 1999).

[6] The term 'true and fair' refers to the need for judgment in making financial statements useful for investment decisions, as opposed to ensuring that they comply with legislation (Wolk et al., 2001).

[7] Puxty et al. (1987) provided an alternative model of accounting regulation and classified predominant regulation styles as being driven by market, state, or community (profession). They characterized accounting regulation in the UK as being primarily community-driven, in Germany state-driven, and in the US as a mixture of the three styles. However, they noted a convergence towards state (central government) control in both the UK and the US.

[8] However, harmonization of accounting regulation and standards is a complex issue beyond the scope of this paper. For example, in North America, a multi-jurisdictional disclosure system (MJDS) adopted in Canada and the US in 1991 allows the SEC to accept some Canadian disclosure documents filed by eligible Canadian companies and vice versa (Kuras, 2003-2004), and the new Canadian securities regulations have been modelled after the US regulations. In Europe, the European Union (EU) is also in the process of implementing similar securities regulations. At the international level, the International Organization of Securities Commissions (IOSCO) promotes harmonization of securities regulations among its members. As to accounting standards, the EU and many countries, including Canada, have voluntarily adopted or made commitments to adopt international accounting standards developed by the International Accounting Standards Board (IASB). Given diverse institutions, systems, and political environments in different countries, complete harmonization is not possible, and it has been described as a process rather than an outcome or state (Uddin, 2005; Tay and Parker, 1990), and as means to achieving some social goals instead of being an end in itself (Leebron, 1996). Furthermore, Leebron (1996) identified four possible levels of harmonization: specific rules, policy objectives, principles, and institutional structures and procedures.

[9] In addition, the states have their own securities laws, called "blue sky" laws, which can vary somewhat from state to state, and which historically have had significant duplication with federal laws. The National Securities Markets Improvement Act (US Congress, 1996) removed some state duplication of registration requirements for many securities and gave additional powers to SEC, but state regulation remains pertinent in many areas, particularly, investment advisors and fraud litigation.

[10] For example, the Ontario Securities Act (Ontario, Legislative Assembly, 1990) governs registration for and trading in securities, continuous disclosure, insider trading, enforcement, and civil liability.

[11] Provincial securities commissions administer and enforce securities legislation in their respective provinces. In addition, some authority over securities regulation has been delegated to self-regulatory organizations such as stock exchanges and the Investment Dealers Association (IDA) (Cox, 2004). For example, stock exchanges can establish trading rules and penalties, including delisting of companies; and IDA monitors its investment dealer members for both their capital adequacy and conduct of business.

[12] Companies subject to SOX must file certificates signed by the CEO and CFO through the System for Electronic Document Analysis and Retrieval (SEDAR), which is the official filing system for reports required by the Canadian Securities Administrators (CSA), as soon as reasonably practicable after they have been filed with SEC (CSA, 2006).

[13] It is also noteworthy that a constitutional challenge had been launched in the US. In March 2007, a US federal judge dismissed a lawsuit filed by a small audit firm challenging the constitutionality of the Public Company Accounting Oversight Board (PCAOB) and SOX (WebCPA, 2007).

[14] The *Assurance Handbook*, Section 9110, paragraph .02 (CICA, 2007) states: "The purpose of such an engagement is solely to assist those charged with governance, those having oversight responsibility for the financial reporting process, or management in assessing the design, implementation or operating effectiveness of the entity's internal control over financial reporting. The public accountant reports the results of the agreed-upon procedures without providing assurance or an opinion on the design, implementation or operating effectiveness of the entity's internal control over financial reporting".

[15] Disclosure control and internal control over financial reporting are defined in MI 52-109 (CSA, 2004a) and Sections 302 and 404 of SOX. Disclosure control comprises controls and other procedures intended to provide reasonable assurance that information required to be disclosed by securities law is accumulated and communicated to company's CEO and CFO to allow them to make timely decisions regarding appropriate disclosures. Internal control over financial reporting comprises processes and procedures designed and implemented by management, staff, and Board of Directors intended to provide reasonable assurance regarding reliability of financial statements and reports and their compliance with Generally Accepted Accounting Principles (GAAP). They include procedures for maintenance of accurate, detailed, and timely records; proper authorization of receipts and expenditures by management and directors; and prevention or timely detection of unauthorized material transactions.

[16] Although audit committees have been established and regulated as major corporate governance mechanisms in many countries, Turley and Zaman (2004) concluded that there currently is no clear evidence on how they influence organizational behaviours and achieve particular governance objectives.

[17] For example, the Ontario Securities Act (Ontario Legislative Assembly, 1990) has continuous disclosure requirements for annual and interim financial information, and penalties applicable to directors and officers who have made, authorized, or permitted materially misleading statements and documents.

[18] For example, Section 127(1)(2) of the Ontario Securities Act authorizes the Ontario Securities Commission (OSC) to impose administrative sanctions, such as cease trade orders.

[19] A survey by CRA International (2006) revealed that larger companies spent an average total of US $13,280,000 (0.08 percent of revenues) and smaller companies US $2,101,000 (0.3 percent of revenues) over the first two years of SOX Section 404 implementation. It noted, however, that the annual costs for the second year declined significantly due to learning, efficiencies, and reduced use of consultants.