

# Did Conservatism in Financial Reporting Increase after the Sarbanes-Oxley Act? Initial Evidence

Gerald J. Lobo, Professor; Jian Zhou, Assistant Professor

[+ Author & Article Information](#)

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In this paper, we investigate the change in managerial discretion over financial reporting following the Sarbanes-Oxley Act (hereafter SOX). We document an increase in conservatism in financial reporting following SOX and the resulting requirement by the SEC that financial statements be certified by firms' CEOs and CFOs. First, we find that firms report lower discretionary accruals after SOX than in the period preceding SOX. Second, based on the Basu (1997) measure of conservatism, we find that firms incorporate losses more quickly than gains when they report income in the post-SOX period. These results are obtained with alternative estimation and measurement approaches and after controlling for potentially confounding variables. This empirical evidence suggests that SOX and the resultant SEC certification requirement may have altered management's discretionary reporting behavior to make it more conservative.

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