Chapter XII
Sarbanes–Oxley Compliance, Internal Control, and ERP Systems: The Case of mySAP ERP

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ABSTRACT

The effort to comply with the Sarbanes-Oxley Act (SOX) has focused management attention in companies all over the world on the importance of assessing, developing, and maintaining an effective and efficient internal control system. Enterprise resource planning (ERP) systems are a crucial factor in developing such a system. Despite the attention this has attracted in practice, little academic research has focused on this area. This chapter addresses the question: How are ERP systems implicated in Sarbanes-Oxley compliance? It aims to show how SOX requirements regarding assessment and improvement of internal controls are related to the functionalities of an ERP system both in local and global implementations. It examines a solution (mySAP ERP) offered by one specific vendor (SAP) and what functionalities are relevant to global SOX compliance. Based on this, the chapter discusses likely developments regarding compliance functionalities in future releases of ERP systems.
INTRODUCTION

Corporate governance can be defined as the framework of rules, relationships, systems, and processes within and by which authority is exercised and controlled in corporations (Owen Report 2003 as cited in du Plessis, McConvill, & Bagaric, 2005, p. 2). Thus the concept embraces not only the models or systems themselves, but also the practices by which this exercise and control of authority are in fact effected. It should be clear that corporate governance is a complex concept encompassing values and ethics, systems and organizations, behavior and activities, and results and performance.

One aspect of corporate governance is complying with the rules and regulations of society. The term compliance has emerged as something of a buzzword in the past five years. Looking through various journals, it seems that compliance is yet another term that has different implications for different areas. In accounting and auditing, compliance has become almost synonymous with Sarbanes-Oxley and strengthening of internal controls and the quality of financial reporting. In production management, compliance can mean conformance with product specifications and quality standards as well as respecting environmental regulations. In human resource management, compliance means adhering to regulations and requirements related to employees including information privacy, health regulations, and codes of safety. Compliance seems to be a generic concept as well as focused on specific functions and processes.

The catalyst for the current focus on compliance in accounting and control is a series of high-profile financial frauds and bankruptcies including companies such as ENRON, WorldCom, Tyco, Parmalat, and Hollinger International Inc. These sent shock waves through the business world. How could well-renowned companies with assets worth billions of dollars disappear from the face of the earth in a matter of weeks, leaving thousands of employees without jobs and whole communities reeling from the aftermath? The answer was deemed to be lack of internal controls, management fraud, and fraudulent financial reporting.

The institutional reaction has been threefold (Baker, Bealing, Nelson, & Blair Staley, 2006). First, there was a government reaction where laws were enacted to strengthen internal control frameworks and increase the accountability of external auditors. This reaction mainly focused on reestablishing investor trust in financial reporting. Second, the monitoring of corporate accountability was strengthened with the emergence of new organizations such as the Public Company Accounting Oversight Board (PCAOB) in the United States. This reaction focused on strengthening the government control regime and possibilities of stepping in should the need arise. Third, there was a professional reaction in accounting and auditing institutions focusing on changing accounting and auditing practices and taking measures to ensure the independence of accounting firms. This reaction focused on reestablishing public trust in the accounting and auditing profession.

The legal reaction was spearheaded by the Public Company Accounting Reform and Investor Protection Act of 2002, more popularly known as the Sarbanes-Oxley Act (SOX) after its main architects, Senator Paul Sarbanes and Representative Michael Oxley. The Sarbanes-Oxley Act has brought about an extensive reform of the U.S. financial markets, with ripple effects spreading around the globe (PricewaterhouseCoopers, 2003) and into other areas of compliance (Atkinson & Leandri, 2005). As such it has changed the landscape for internal controls, auditing, and management accountability in thousands of companies all over the world—changes which will be visible for years to come.

One of the issues often mentioned regarding SOX compliance is the importance of information technology in the compliance effort (MacNally & Wagaman, 2005; Byington & Christensen, 2005; ACL, 2005; Cannon & Growe, 2004). This