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Illegal Corporate Behavior

Analyzing the Effectiveness of the 2002 Sarbanes-Oxley Act

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Abstract

This research examined the effects of organizational environmental factors on firms' illegal corporate behavior, and also the ability of the Sarbanes-Oxley Act of 2002 to moderate the relationship between prior violations committed and future illegal corporate behavior. Corporate Socially Responsible (CSR) behavior within business organizations was also examined to determine its relevance in predicting illegal corporate behavior. Moreover, this research provided an organizational level, five year pre and post, historical analysis of legal behavior across *Fortune 500* firms. Finally, this research aimed to determine if antecedents to illegal corporate behavior can be identified and if the Sarbanes-Oxley Act of 2002 can be an effective legislative tool impacting firm behaviors. The Sarbanes-Oxley Act itself was analyzed as an event. This research examined Baucus and Near's (1991) model of the illegal and corporate behavior process to test its ability to predict illegal behavior within historically corrupt industries. Moreover, CSR as an embedded theme within specific firms, and its implications toward both ethical and legal firm practices, was examined.

Key words: corporate social responsibility, internal controls, Sarbanes-Oxley Act, illegal corporate behavior, corporate corruption

Introduction

The lack of strong corporate ethics and fiscally responsible behaviors within corporations over the last decade created the need for the enactment of more external corporate controls, including enforcement of regulations to monitor and control private industry financial practices. This need for greater corporate accountability is being addressed by recent acts of U.S. corporate corruption. Additionally, this need is further evidenced by the fact that U.S. corporate corruption has become rampant and efforts to attain great wealth have led to unethical business practices. Furthermore, the focus on the attainment of wealth has led some firms to engage in both irresponsible and/or illegal firm behaviors to achieve their ultimate goals, thus, indicating a need for greater corporate accountability. Several studies have identified illegal corporate behavior as an important issue impacting corporate compliance (i.e., Baucus & Near, 1991; Alexander & Cohen, 1996; Eigen, 2002; Doh, Rodriguez, Uhlenbruck, Collins, & Eden, 2003; Kuncoro, 2006).

Recent Acts of U.S. Corruption and Corporate Crime

Several U.S. companies, including Adelphia, Healthsouth, McKeeson, Tyco, Refco, and Quest, were investigated for fraudulent activities" (Brickley, 2003). These investigations have led to criminal charges against over ninety corporate owners, executives and employees, and the investigations are still ongoing (Brickley, 2003, p. 358)". In addition to these examples, by August 2003, eighteen Enron executives had been indicted for acts of corporate fraud. It should be noted, however, that the pragmatic implications of the relationship between firm size and an organization's likeliness to engage in illegal corporate acts within respective industries have not been clearly identified. In response to unethical corporate practices of several American Chief Executive Officers (CEOs) and Chief Financial Officers (CFOs), the U.S. government developed legislation to strictly govern corporate fiscal behaviors. This action was a strategic governmental response based on the recognized need for a higher degree of compliance to both ethical and legal corporate standards. Moreover, this was a reaction based on the need to implement a strategic governmental initiative to address inadequate processes of measurement and control due to weaknesses in laws, regulations and pronouncements in external control measures (Heier, Dugan, & Sayers, 2005). Likewise, the need for further legislation is reflective of a lack of public trust in corporate executive officers to govern their corporations not only ethically, but also legally and responsibly. Likewise, it also indicates a lack of trust in corporate governance boards to appropriately oversee firm activities.

The Sarbanes-Oxley (SOX) Act may prove to be a significant piece of legislation moderating corporate ethics. However, little research has been conducted to determine the ability of SOX to moderate the ethical corporate behaviors of firm's within historically corrupt industries (Palazzo, 2007). Likewise, whether or not the SOX Act moderates socially responsible business practices and ethical and legal firm behaviors has yet to be determined. Additionally, the influence of SOX as an effective mechanism of internal control on firms within historically corrupt *Fortune 500* firms has yet to be examined.

The theoretical background for this research is derived from antecedent conditions to illegal behavior as described by Aldrich (1979) and Baucus and Near's (1991) model of predicting corporate illegal behaviors and the illegal corporate behavior process. Aldrich (1979) identified three key environmental dimensions representing firm characteristics independent of leader personality variables. These variables are described as scarcity, dynamism, and heterogeneity (Aldrich, 1979). Furthermore, Baucus and Near (1991) introduced situational variables that are directly related to instances of firm illegality.

Environmental Antecedents

Aldrich's (1979) formulation has shown to be important in understanding the role the environment plays on adaptive organizational behavior. Baucus and Near's (1991) research examined Aldrich's (1979) assertions by studying the illegal acts committed by all *Fortune 500* companies between the periods of 1974-1983. Baucus and Near (1991) compared this sample with 104 randomly selected non-convicted firms to compare firm similarities and differences by industry. This study revealed five key findings: 1) illegal activities occur under uncertain conditions, 2) large firms are more likely to commit illegal acts than small firms (although probability increases when resources become scarce), 3) illegal behavior is prevalent in fairly stable environments, but is more probable in dynamic environments, 4) membership in industries with a repeated history of wrongdoing is associated with illegal acts, and 5) the type of illegal activity may be dictated by the environmental and internal conditions under which the firm operates (Baucus & Near, 1991). Additionally, Baucus (1994) postulated that corporate corruption thrived in complex, uncertain, dynamic, and munificent environments. Baucus and Near (1991) concluded that environmental munificence, environmental dynamism, firm size, industry**,** three or more prior violations, and type of violations could be used to predict illegal corporate behavior. A significant relationship has been found between these organizational environmental factors and the performance, structure, and strategy of organizations (e.g., Keats & Hitt, 1988; Davis, n.d.). Two main environmental variables were examined within this research: munificence and dynamism. Control variables for this study included firm size, industry membership and prior violation committed.

Munificence

Castrogiovanni (1991) defined environmental munificence as the scarcity or abundance of resources available in an environment and demanded by one or more firms (Davis, n.d.).

Dynamism

The construct of dynamism is comprised of numerous variables including: 1) speed in which the environment is changing (stability-instability), 2) turnover rates, and 3) predictability and unpredictability contributing to uncertainty (Davis, n.d.). Organizations competing in environments characterized by high levels of dynamism must have greater flexibility to adapt to a changing environment (Mascarenhas, 1986). Organizations competing in environments characterized by high levels of dynamism may need to show more flexibility to adapt to the changing environment and to assist in ensuring the organization's survival (Mascarenhas, 1986). Moreover, Mascarenhas (1986) posits that dynamism is an important factor that assists in ensuring an organization's survival.

Study Purpose

The purpose of this study is two-fold, first, to explore the SOX act’s ability to function as an internal control mechanism to moderate the relationship between seriousness of violation committed and illegal corporate behavior. Its second intent is to examine whether illegal corporate acts (leading to corporate corruption) can be predicted. Historical data of illegal criminal corporate behavior will also be gathered to test the antecedents of Baucus and Near’s (1991) model of predicting corporate illegal behaviors. Moreover, this research will provide a historical analysis of firms criminally prosecuted five years prior to, and five years after SOX implementation. This historical analysis of SOX corporate activities will be employed to determine the overall influences of SOX and its ability to influence the relationship between corporate social responsibility and other behaviors specific to firms.

Research Objective

Through this study, this researcher will attempt to answer the following research question: How are antecedents to illegal firm activities, specifically, environmental munificence and environmental dynamism, impacted by corporate internal controls (i.e. SOX) and corporate socially responsible behavior?

Significance of Study

This study contributes to the advancement of the corporate reform literature by providing an analysis of the composition and characteristics of historically corrupt industries. Moreover, it examines the fundamental composition of U.S. firms to study antecedents of corporate corruption. Additionally, this study will serve as a five year pre and post event analysis of the effectiveness of the SOX Act to perform as an effective internal control mechanism.

This study is important because it may assist corporate boards and government legislators to understand factors influencing illegal corporate behavior. Additionally, this study intends to examine the impacts of corporate reform efforts on specific firm behaviors. Moreover, the SOX Act criminal punishment provisions will be examined to determine their impact on firm adherence to external and internal ethical and legal provisions. The impacts and consequences for failure to meet expected government standards of compliance under SOX will also be examined. This research contributes to the corporate illegal behavior literature stream by identifying antecedents to illegal corporate behavior.

Relevant Studies in Corporate Corruption

Kuncoro (2006) provides a quantitative analysis of corruption in the uncertain business environment of Indonesia. Kuncoro (2006) examined secondary data of two firm-level surveys provided by the Institute of Economic and Social Research, University of Indonesia (LPEM-FEUI) from 2001 and 2003 CODB (Cost of Doing Business) surveys. This research examined the decentralized effects of corruption and bribery on the economy of Indonesia (Kuncoro, 2006). The strategy utilized for collecting individual participant information on bribe payments was in-depth interviews of 1,333 respondents. Results indicated that a negative relationship exists between firm uncertainty and bribe activity (Kuncoro, 2006).

Eigen (2002) provides a quantitative secondary data analysis of 2002 surveys completed by business persons and analysts (N = 776) of one-hundred and two countries rating them from 10 (highly clean – few instances of corruption) to 0 (highly corrupt). He found that corruption thrives within an international economy based on misinformation and a climate of mistrust. Furthermore, results indicated that the countries of Bangladesh, Nigeria, Paraguay, Madagascar, and Angola were ranked as the top five countries with the most corrupt business practices (Eigen, 2002). Conversely, the countries of Finland, Denmark, New Zealand, Iceland, and Singapore, were recognized as the five least corrupt countries (Eigen, 2002).

A summary analysis of the above recent empirical studies regarding corruption among various countries reveals that international corruption involves political, social, economic and organizational environment considerations. Perhaps foremost, that corruption thrives within an environment of mistrust and misinformation within organizations (Eigen, 2002). Secondly, that strategies used to reduce corruption must involve both government intervention and the legislation of legal activities (Doh, Rodriguez, Uhlenbruck, Collins, & Eden, 2003). Therefore, understanding how business practices are impacted by multi-dimensional factors is an important consideration when determining appropriate strategies for legislating corporate behaviors. Although corporate corruption is largely considered to be an international business problem, very little research has been conducted to determine how oversight mechanisms of corporate internal controls and a firm's adherence to socially responsible behaviors directly impact firm CSR activities (Campbell, 2007). This research examines CSR activities of *Fortune 500* firms.

Baucus and Near's (1991) research examined antecedents of illegal firm behavior by studying types of criminal acts committed by 88 convicted *Fortune 500* firms from 1974 to 1983. Baucus and Near (1991) used a comparison group sample of 104 non-convicted *Fortune 500* companies. Alexander and Cohen (1996) expanded the literature on corporate illegal behavior through their examination of the criminal acts of 77 public manufacturing corporations between 1972 and 1994. They used a variety of archival data to provide an exhaustive review of the legal literature including the following sources: Wall Street Journal Index, Corporate Crime Reporter, keyword searches on Lexis-Nexus legal database, Anti-trust Trade and Regulation Reporter, and a periodical report by the U.S. Environmental Protection Agency. Alexander and Cohen's (1996) research suggests that larger corporations with larger sales transactions and higher numbers of employees typically have more opportunities to engage in criminal acts. Their research revealed a total of 120 convictions of 101 U.S. public corporations convicted during the time period 1975-1992, including 55 fraud conviction cases. They discovered two significant findings as follows: 1) larger firms are more likely to engage in crime than smaller firms, and 2) low rate of sales and employment (or employment growth) by a firm is a good predictor of environmental crime. Providing enhancements to Baucus and Near's (1991) model of the illegal corporate behavior process, this researcher explored additional antecedents to illegal corporate behavior specific to *Fortune 500* convicted and non-convicted firms.

Five research hypotheses of this research study are as follows:

H1: Firms having a high degree of environmental munificence (abundant resources) will have lower levels of illegal corporate behavior.

The relationship between munificence and corporate illegal activity has been identified throughout the illegal corporate behavior literature. Staw and Swarjkowski (1975) examined the relationship between scarcity-munificence within organizational environments and the occurrence of illegal corporate acts. They found support for the proposition that environmental scarcity leads to trade violations including: price fixing, reciprocity, mergers, and acquisitions (Staw & Swarjkowski, 1975). Moreover, Staw and Swarjkowski (1975) found that firms in hostile or non-munificent environments were more likely to commit illegal corporate acts. They concluded that in non-munificent environments, scarcity of resources causes firms to focus on the conservation of resources. Conversely, Simpson's (1986) study of antitrust crime reveals further insights into the relationship between environmental munificence and corporate crime. She found that, although there is a negative correlation between criminality and profitability, serious antitrust violations appear more likely in situations when industry profitability is declining. Additionally, Baucus and Near (1991) examined antecedents to corporate illegal behavior (including munificence) and found that firm illegal activity was more likely when resources were scarce.

Koberg (1987) argues that the greater the environmental scarcity, the more likely changes in administrative, personnel, and strategic changes will occur, thereby, requiring organizational structural changes. Therefore, firm's with an abundance of resources may prove to be less involved in illegal corporate behavior.

H2: Firms having high levels of environmental dynamism will have a high degree of illegal corporate behavior.

The conceptual link between corporate illegal behavior and dynamism has been established through corporate behavior literature streams. Baucus and Near's (1991) research examined dynamism in relation to illegal corporate behavior. They denoted a curvilinear relationship between environmental dynamism and organizational criminality. They found that illegal acts were present in situations where resources were both scarce and also overly abundant. Moreover, Goll and Rasheed's (1990) study examined the moderating role of environmental munificence within 64 manufacturing firms. They concluded that both environmental munificence moderated the relationship between firm rationality and performance. Firm rationality for decision making and overall performance outcomes obtained from decision making may prove important factors in understanding how dynamism impacts the organizational environment. Firm's exhibiting high levels of dynamism may also prove to be more prone to commit illegal corporate acts.

Anand and Ward (2004) posit that today's competitive and rapidly changing business environment requires firms' to become flexible to ensure their success. These ever-changing environmental conditions may create volatile and unpredictable environments requiring firm strategies that promote both environmental fit and overall flexibility (Anand & Ward, 2004). Anand and Ward (2004) conducted an empirical analysis of 101 manufacturing firms to explore organizational impacts of environmental dynamism. This research argued that environmental fit is an important variable explaining business benefits achieved from any approach to flexibility.

H3: There will be a negative association between seriousness of violation committed and illegal corporate behavior.

The relationship between the seriousness of prior violation committed and subsequent criminal acts has been examined throughout the literature (Baucus & Baucus, 1990; Baucus, 1994; Baucus & Near, 1991; Finney & Lesieur, 1982). Finney and Lesieur (1982) propose through their contingency theory of organizational crime, that events leading to the criminal offense and the enactment of consequences for crimes committed are important considerations in determining a firm's decision to commit criminal acts. Additionally, Baucus (1994) purports that firms that show sufficient gains in performance after unethical activities may also be more prone to re-engage in criminal activities. Baucus (1994) also posits that firms experiencing few negative consequences for unethical actions, coupled with increased financial performance, may also be encouraged to commit subsequent criminal acts. Baucus and Baucus's (1990) study examined the financial consequences of convicted firms. They examined whether criminal consequences significantly impacted long-term firm performance. Baucus and Baucus (1990) studied the number of additional convictions firms received within one to five years after their initial conviction. The data set consisted of 47 firms with one conviction, 19 firms with one two convictions, and 2 firms with three or more convictions. Baucus and Baucus (1990) concluded that there was a negative relationship between firms with multiple convictions (within a five year period) and overall firm performance. The functionality of crime as a means of achieving organizational success may prove a highly significant concept in understanding why some firms commit subsequent criminal acts. Vaughan (1985) posits that "successful achievement of organizational goals through unlawful conduct tends to reinforce the occurrence of this behavior" (p. 61). Additionally, Baysinger (1991) postulates that "when rational individuals compare the cost of government imposed economic-sanctions for failing to meet performance objectives, they may conclude that violation of the law is the more desirable alternative" (p. 355).

H4: There will be a negative correlation between a strong emphasis on corporate socially responsible activities and illegal corporate behavior.

Firm obligations go far beyond legal requirements and corporate duties to shareholders. Moreover, "fulfillment of corporate obligations requires firms to strive to both minimize harm and maximize the long-run beneficial impacts of the firm on society" (Bloom & Gundlach, 2001, p. 142). Additionally, firms are directly responsible to a wide variety of community stakeholders including: people, groups, organizations, institutions and societies, and even the environment (Wood, 1991). Therefore, a firm's commitment to morally legitimate behavior may involve a wide variety of considerations including social and normative judgments and values, promulgated by institutional sources and their industries (Scott, 1995).

An empirical survey of Carroll's (1991) CSR Pyramid utilizing a sample of 503 large African American businesses in the U.S found that within the businesses surveyed, the economic considerations ranked as most important, ethical responsibilities were prioritized above legal responsibilities, and there was differential between philanthropic and legal responsibilities (although this finding was relatively small) (Edmondson & Carroll, 1999). Ibrahim, Howard and Angelidis (2003) found that 307 board members (198 outside and 109 inside directors) indicated that outside directors exhibit greater concern about the discretionary component of corporate responsibility and a weaker orientation toward economic performance. Similarly, Aupperle, Hatfield & Carroll (1985) surveyed 241 *Forbes 500* listed CEOs utilizing 171 statements pertaining to CSR. Their statistical analysis supported their model: 1) by confirming that there are four empirically interrelated, but conceptually independent components of CSR; and 2) by giving tentative support to the relative weightings assigned to each of the four components.

H5: The Sarbanes-Oxley Act will positively moderate the relationship between seriousness of violation committed and illegal corporate behavior.

Deterrence theory provides the framework to describe why some individuals are deterred from the commission of criminal acts. One basic tenant of deterrence is that individuals that receive swift, severe and certain punishments will likely be deterred from committing future criminal activity. Moreover, deterrence theorists posit that general deterrence of crime can only occur when punishments are not overly harsh, but that the 'punishment fits the crime'. This research attempts to examine whether the 2002 SOX act deters firm illegal corporate behavior.

The linkage between criminal behavior and crime has been clearly established, however, few studies have examined this linkage in respect to deterrence of firm criminality (Simpson, 1986). The concept of deterrence is theoretically rooted in the premise that all individuals know the difference between 'right and wrong' and are aware *o*f the consequences of their actions (Schallmeger, 2002). This concept is fundamentally important in our understanding of why some individuals/firms are deterred by the consequences of crime, while offers remain non-deterred. Conversely, firms that are not punished harshly enough for their crimes may choose to engage in future criminal acts.

Enhancements are proposed to Baucus and Near's (1991) model of Illegal Corporate Behavior as indicated in Figure 1.

Figure 1: Factors Leading to Illegal Corporate Behavior: Proposed Enhancements to Baucus and Near's (1991) Model

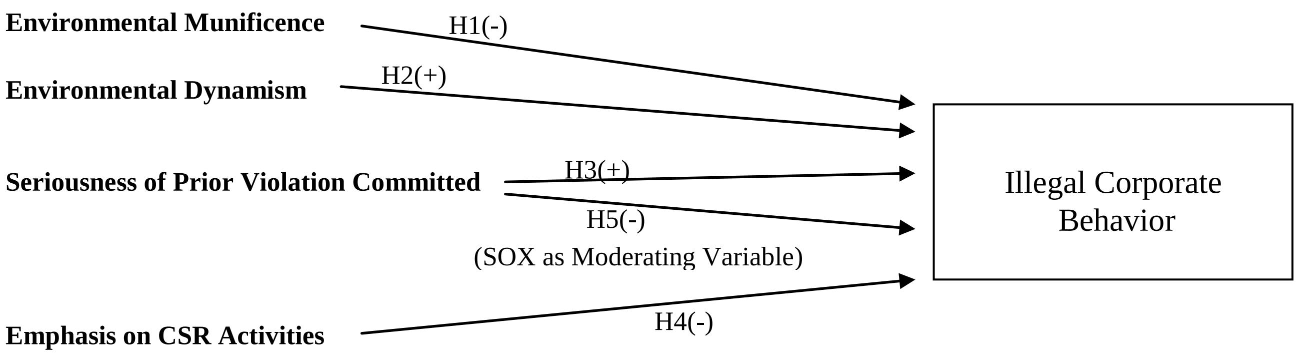

Table 1: Key Study variables - Operational Definitions

Study Variables	Operationalized as:
Environmental Munificence	The scarcity or abundance of resources available in an environment and demanded by one or more firms.
Environmental Dynamism	Speed in which the organizational environment is changing from stability-instability and the predictability and unpredictability of this change contributing to uncertainty
Prior Violation	The level of offense classification of firm violation resulting in criminal prosecution and conviction.
Emphasis on CSR Activities	A firm's commitment to embrace behaviors that promote corporate social responsibility.
Illegal Corporate Behavior	Corporate behaviors resulting in illegal acts committed by firms leading to criminal conviction for violations of legal compliance standards.
Sarbanes-Oxley Act of 2002	Federal legislation developed as a mechanism for corporate governance regulation/standards compliance.

Control variables = firm size; industry membership; prior violations

Table 1 and Figure 1 outline this study's independent variables, dependent variable, and the direction of the proposed relationships.

Sample Selection

A search of prosecution and conviction data of *Fortune 500* firms convicted of 'white collar' crimes for the years spanning 1990-2007 resulted in the identification of 50 convicted firms and a total of 126 convictions.. Each instance of corporate corruption was treated as a separate observation. Moreover, multiple data sources were utilized to triangulate data source findings and identify all incidences of firm convictions. Additionally, a list of comparable non-convicted *Fortune 500* firms (matched based on industry type and firm size) was generated to create a matched pair dataset of both convicted and non-convicted firms. The sample of 50 non-convicted *Fortune 500* firms was randomly selected (based on firm size and respective industry type) for the time period 1990-2007. This time period provided a total of 1,800 firm years' worth of financial data. The four-digit SIC industry code was used to indicate the number of both convicted and non-convicted firms identified by major industry type. The industry code was selected to describe the industry sectors within which individual firms operate.

Matched pair design was utilized within this study to create pairs of firms that are similar in both industry type and sales (firm size). Matched firm pairs were constructed by pairing each of the identified convicted firms (n=50) with a comparable non-convicted firm match (n=50), (total sample size - N=100) based on the following characteristics: firm size (dummy code: 1 = small, 2 = medium, 3 = large), industry type (designated by use of the four digit SIC code), and firm sales (per million). Additionally, firm matches were created at the same point in time. For example, a firm with a conviction in the year 1990 was matched with a non-convicted firm at the same point in time based on the above aforementioned characteristics. Each of the qualifying non-convicted firms eligible for consideration was assigned an identifying number. A random number generating calculator was then used to select each individual non-convicted firm to create matched firm pairs.

Data Collection and Procedures

In summation, data collection for this research included the collection of archival/historical conviction data from relevant reputable sources documenting corporate criminal acts. These secondary data sources include: 1) Lexis-Nexus, 2) 2002 Corporate Fraud Task Force, and 3) Corporate Crime Reporter. Corporate financial reports were acquired from Standard and Poor's COMPUSTAT and the U.S. Statistical Abstract. Additionally, data collected to examine the independent variable, industry reputation for CSR behavior, was derived from content analysis of corporate website reports of CSR related activities.

A search of *Fortune 500* firms convicted by the courts during of the period 1990-2007 was conducted to determine the quantity and type of criminal violations committed by corporate firms. The four-digit SIC code representing each industry was utilized to indicate the illegal acts committed by each firm within its respective industry. The SIC code was also utilized to categorize each industry and delineate each firm's membership within its respective industry. The 10 major categories of industrial classification are as follows:

Division A—*Agriculture, Forestry, and Fishing* (SIC 0109)
Division B—*Mining* (SIC 1014)
Division C—*Construction* (SIC 1517)
Division D—*Manufacturing* (SIC 2039)
Division E—*Transportation, Communications, and Public Utilities* (SIC 4049)
Division F—*Wholesale Trade* (SIC 5051)
Division G—*Retail Trade* (SIC 5259)
Division H—*Finance, Insurance, and Real Estate* (SIC 6067)
Division I—*Services* (SIC 7089)
Division J—*Public Administration* (SIC 9197)

*Source: U.S. Census Bureau, 2008, http://www.census.gov/epcd/www/sic.html

The SIC code was utilized throughout this research to delineate the assigned membership of corporate firms as well as to analyze patterns and emerging trends within industries. The sample of convicted firms was matched with comparable firms within their respective industries. Divisions A-J (as indicated above) were recorded as 1-10, respectively, to serve as a control for industry type during the matching process. Specifically, SIC code divisions were recoded as follows: 1 = 0109, 2 = 1014, 3 = 1517, 4 = 2039, 5 = 4049, 6 = 5051, 7 = 5259, 8 = 6067, 9 = 7089, and 10 = 9197.

A convenience sample of available conviction data of 50 convicted *Fortune 500* firms was selected and compared with 50 non-convicted *Fortune 500* firms (N=100). Logistical (logit) regression analysis techniques were utilized to determine the maximum likelihood of predicting illegal corporate behavior utilizing two main explanatory variables – environmental munificence and environmental dynamism. Moreover, Ordinary Least Squares (OLS) regression was also utilized to model the data through two separate time periods to determine the impact of the SOX Act of 2002 on illegal corporate behavior.

Data Analysis

Data analysis was performed using a variety of techniques including logistical regression, Chi-square, OLS regressions, and t-tests. The formula employed to investigate the proposed empirical relationships within this research is represented in the following expression:

$\Pr(\text{convicted}_{it} = 0;1) = \exp(x_{it})/(1 + \exp(x_{it}))$

where

convicted_{it} = *i* indicates criminal conduct in the year *t*; 0 = no firm conviction; 1 = firm conviction; and

$x_{it} = \beta_0 + \beta_1 J_{1it} + \beta_2 J_{2it} + \epsilon_{it} \ldots (t_1, t_2)$

whereby, *i* and *t* denote firm and year, and J denotes control variables: J_1 (firm size), J_2 (industry type), and ϵ_{it} estimates chance of error.

The results of both convicted and non-convicted firms within the pre- and post- SOX eras are presented in Tables 2-4. Table 2 below shows the overall logistical regression results of all firms during the pre- and post SOX eras.

Hypotheses 1 and 2 were tested utilizing logistical regression analysis. Model 1 above shows that environmental munificence (-0.645), firm size (-0.442), and SOX (-0.271) are negatively and significantly related to illegal corporate behavior. This suggests that there is an association between a high level of abundant firm resources (munificent environment), and a low likelihood that the firm will engage in illegal corporate behavior. Similarly, if the firm is large in size, it is less likely to engage in illegal corporate behavior in the post-SOX era. It is expected that SOX will mitigate illegal corporate behavior even in an abundant resource environment. This is confirmed by the higher odds ratio result for SOX (0.763). The results support the argument that SOX will moderate illegal corporate behavior.

Model 2 presents the results for environmental dynamism. Though environmental dynamism does not show a significant relationship with the independent variables, firm size (-0.445) and SOX (-0.260) have a negative and significant relationship with illegal corporate behavior. The results lend support to the argument that SOX influences actions of firms convicted of illegal corporate behavior in both munificent and dynamic environments. However, the impact is more profound in environmental munificence. This is evidenced in model 3 within Table 2. The results of the interaction term – environmental munificence and SOX indicate a relationship between environmental munificence and SOX with illegal corporate behavior. The negative relationship suggests that in the post-SOX era, environmental munificent firms suffer more in cases of illegal corporate behavior.

Table 2: Logistic Regression Results of Sample Firms during Pre- and Post- SOX Era

	***ILLCORP* as Dependent Variable**				
MODEL #:	**(1)**	**(2)**	**(3)**	**(4)**	**(5)**
ENVIRMU	-0.645				-0.666
	(2.9102)				(3.0461)
ENVIRDYN		0.105			0.174
		(0.0767)			(0.2100)
FRMSZ	-0.442	-0.445	-0.412	-0.424	
	(5.1956)	(5.2474)	(4.5014)	(4.7684)	
SICOD	0.072	0.070	0.061	0.061	0.074
	(3.7450)	(3.5792)	(2.7540)	(2.7165)	(3.9127)
SOX	-0.271	-0.260			
	(5.0871)	(4.7099)			
ENVIRMU*SOX			-0.4657		
			(3.3042)		
ENVIRDYN*SOX				0.064	
				(0.0695)	
FRMSZ*SOX					-0.103
					(6.8387)
Constant	1.380	1.324	0.950	0.9319	0.122
	(5.0492)	(4.6524)	(2.6159)	(2.5253)	(0.3456)
Odds Ratio for *ENVIRMU*	0.522				0.514
Odds Ratio for *ENVIRDYN*		1.111			1.190
Odds Ratio for *FRMSZ*	0.643	0.641	0.662	0.655	
Odds Ratio for *SICOD*	1.075	1.073	1.063	1.062	1.076
Odds Ratio for *SOX*	0.763	0.771			
Log Likelihood Ratio	15.402	12.552	11.044	7.775	12.540
Number of Observations	1193	1193	1193	1193	1193

N = 1193
Wald statistics are given in parentheses
0 = No Illegal Corporate Behavior (Non-Convicted Firm)
1 = Illegal Corporate Behavior (Convicted Firm)

Models 4 and 5 indicate that environmental munificence and firm size have a negative impact on illegal corporate behavior. The interaction term for environmental dynamism with SOX does not show a significant relationship with illegal corporate behavior, but for firm size, it is negatively significant.

Table 3 below presents the chi-square results utilizing a binary logistic model analysis of both pre-SOX and post-SOX firms testing model goodness-of-fit:

Table 3 presents the results of an analysis of convicted and non-convicted firms using a Chi-square test. This analysis revealed the statistical findings within both pre-SOX and post-SOX eras. Chi-square test results suggest that the logistic model works better in the pre-SOX era than in the post-SOX era. However, the logistic model works well with the entire sample data as reported in Table 3.

Table 3: Analysis of Chi-Square Testing Pre-SOX and Post-SOX Firms

Variables	**Binary Response Variable: Non-convicted and Convicted Firms**	
	Pre-SOX	**Post-SOX**
ENVIRMU	-0.811 (2.6453)	-0.633 (1.0500)
ENVIRDYN	0.285 (0.2921)	0.048 (0.0074)
FRMSZ	-0.769 (5.9206)	-0.216 (0.7314)
SICOD	0.091 (3.0885)	0.0533 (0.9673)
Constant	2.022 (4.4944)	0.250 (0.1082)
Likelihood Ratio	11.2617	3.1923
Number of Observations	708	485

N = 1193
Wald Chi-Square given in parentheses.
The firms are assigned a value of 0 (no conviction) and 1 (conviction).

Hypotheses 3 and 5 were tested utilizing a seriousness of crime index to determine the seriousness of corporate crime(s). Both quantitative and qualitative results of expert panel member findings indicated that seriousness of crime, defined here as the harm done to society, was lower in the pre-SOX period than in the post-SOX period. Thus, indicating that corporations and their officers face more serious consequences for their actions in the post-SOX era. Table 4 below shows the regression results of the seriousness of crime committed during both pre- and post-SOX periods.

Table 4: Regression Results for seriousness of crime committed and illegal corporate behavior during pre and post-SOX periods

Variables	***Seriousness Index* as Dependent Variable**	
	Pre-SOX Period	**Post-SOX Period**
ENVIRMU	-3.847 (-2.80)	10.987 (-1.64)
ENVIRDYN	-0.706 (-0.31)	-1.054 (-0.77)
CRIME INDEX	0.001 (0.01)	-0.006 (-0.01)
FRMSZ	-1.652 (-2.07)	-0.166 (-0.22)
SICOD	0.011 (0.12)	0.328 (1.49)
Constant	6.707 (2.89)	1.064 (0.33)
Adjusted R-Square	0.12	0.13
Number of Observations	80	28

N=108 T-value given in parentheses p<5%

Pre-SOX period results indicate that the conviction of a firm has a negative association with environmental munificence (-3.847). Thus, indicating that firm conviction results in a reduction in firm resources. Further, results show that the larger the firm the more negative the impact. The coefficient for environmental dynamism (-0.706) is negative, though insignificant.

When the regression results are analyzed during the post-SOX period, it indicates that, although environmental munificence and dynamism both have a negative coefficient, they are not statistically significant. Further, the coefficient of firm size is negative, even though it is not statistically significant. This result suggests that the SOX Act provides a moderating effect on illegal corporate behavior. This may in turn be a result of increased punishments and harsher penalties under the SOX act. Thus, the above findings support hypothesis 5 regarding the SOX Act having a moderating effect on illegal corporate behavior.

Table 5 below provides an analysis of the means of CSR related terms frequently used within firms that espouse a strong commitment to corporate socially responsible behavior.

Hypothesis 4 was examined utilizing t-tests. The data compiled in Table 5 were used for this analysis. T-test results indicated that the mean of CSR indicators differ in four industry segments. Statistically significant differences were found in the following segments: 2800-2865 (p=0.01), 2911 (p=0.02), 3318-3534 (p=< .0001), and 4813-4953 (p=0.02).

CSR was found to be negatively correlated with seriousness of crime and SOX, at a low correlation level (-0.19 and -0.28). However, CSR is highly and positively correlated with environmental munificence (0.54). This suggests that in an abundant resources environment, firms act more socially responsible. As expected, CSR is not significantly related to other predictor variables.

Table 5: Descriptive Statistics of CSR Variables

Variables	**N**	**Mean**	**Med**	**St.Dev**	**Min**	**Max**
	Panel A: Non-convicted Firms					
Corporate Social Responsibility	50	1.22	0	2.59	0	12.00
CSR	50	1.80	0	4.50	0	24.00
Social Responsibility	50	2.58	0	5.72	0	34.00
Socially Responsible	50	0.18	0	0.60	0	3.00
Corporate Sustainability	50	0.40	0	1.59	0	10.00
Corporate Citizenship	50	3.16	0	8.84	0	60.00
	Panel B: Convicted Firms					
Corporate Social Responsibility	50	1.26	0	3.77	0	22.00
CSR	50	0.70	0	2.87	0	18.00
Social Responsibility	50	1.20	0	2.07	0	9.00
Socially Responsible	50	0.34	0	2.00	0	14.00
Corporate Sustainability	50	0.20	0	0.81	0	4.00
Corporate Citizenship	50	2.32	0	5.83	0	29.00

N=100; Med=Median; St.Dev=Standard Deviation; Min=Minimum; Max=maximum

Conclusion

In conclusion, the lack of strong corporate ethics and fiscally responsible behaviors within corporations over the last decade has created the need for more external corporate controls, to include enforcement of regulations to monitor and control private industry financial practices.

In this research, environmental munificence (-0.645), firm size (-0.442), and SOX (-0.271) were negatively and significantly related to illegal corporate behavior. However, results differed in both the pre- and post-SOX eras. Larger firms in the pre-SOX era were found to be more likely to engage in illegal corporate behavior. However, in the post-SOX era, the results indicate no statistically significant relationship with firm size and environmental munificence. Thus, no support was found for hypothesis 1. It should be noted that smaller munificent firms were found to be more likely to be convicted of illegal corporate behavior more frequently than larger munificent firms. One possible explanation for this occurrence is the fact that larger firms have more resources, and thus, have the ability to avoid detection of illegal acts more readily than smaller, more transparent firms.

In testing hypothesis 2, it was found that during the pre-SOX era, larger firms are more likely to engage in illegal corporate behavior. This is implied by the firm size coefficient (-0.730) which is statistically significant. The insignificant coefficient for environmental dynamism for both convicted and non-convicted firms during pre and post-SOX eras, however, suggests that environmental dynamism does not appear to be a significant factor in predicting illegal corporate behavior.

Hypothesis 3 was tested utilizing a seriousness of crime index to determine the seriousness of corporate crime(s). Both quantitative and qualitative results of expert panel member findings indicated that seriousness of crime was lower in the pre-SOX period than in the post-SOX period, thus indicating that corporations and their officers face more serious consequences for their actions in the post-SOX era. Seriousness of crime was found to be associated with the munificence of a firm’s environment and punishment was found to vary by firm size. Thus, a negative relationship was found to exist between seriousness of violation committed and illegal corporate behavior.

Hypothesis 4 was successful in providing support for the premise that CSR is an important variable impacting corporate illegal behavior. Through means analysis of CSR related terms and their frequency of occurrence within both convicted and non-convicted firms, it was determined that non-convicted firms were less likely to be convicted of illegal corporate behavior than non-convicted firms. Thus, this finding supports the appropriateness of CSRs use in an enhanced model of illegal corporate behavior. Future research should specifically focus on CSR’s predictive ability in identifying firms that may have a propensity to engage in illegal corporate behavior.

In hypothesis 5, regression analysis results indicated that firm convictions have a negative association with environmental munificence (-3.847) in the pre-SOX era. However, no such effect was found in the post-SOX era. Thus, the negative coefficient of both environmental munificence and dynamism lends support to the moderating impact of SOX.

The overall results of this research suggest that the SOX Act provides a moderating effect on prior violation committed and illegal corporate behavior. This may in turn be a result of increased punishments and harsher penalties under the SOX act. Therefore, more research is needed to examine the impact of SOX, as well other legislative efforts, to determine their overall effectiveness in deterring illegal corporate behavior.

Implications for International Business

The Sarbanes-Oxley Act is touted as a significant piece of legislation aimed to rid American of corporate corruption by providing an enhanced mechanism of internal control. It has been a decade since the enactment of this act. However, the overall impact of SOX as an effective internal control mechanism is still evolving. Despite legislative efforts to manage corporate behavior, corporate corruption continues. Further empirical research is needed to examine antecedents to illegal corporate behavior and their implications for predicting and detecting future corporate illegal activity and corporate socially responsible behaviors utilizing a cross-cultural/international perspective. Directions for future research should be internationally focused on cultural norms and institutionalized regulatory practices. Moreover, more industry level studies are needed to determine the impacts of CSR on curbing illegal corporate behavior among firms within and among various nations.

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English Abstract

Illegal Corporate Behavior

Analyzing the Effectiveness of the 2002 Sarbanes-Oxley Act

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Abstarct

This research examined the effects of organizational environmental factors on firms' illegal corporate behavior, and also the ability of the Sarbanes-Oxley Act of 2002 to moderate the relationship between prior violations committed and future illegal corporate behavior. Corporate Socially Responsible (CSR) behavior within business organizations was also examined to determine its relevance in predicting illegal corporate behavior. Moreover, this research provided an organizational level, five year pre and post, historical analysis of legal behavior across *Fortune 500* firms. Finally, this research aimed to determine if antecedents to illegal corporate behavior can be identified and if the Sarbanes-Oxley Act of 2002 can be an effective legislative tool impacting firm behaviors. The Sarbanes-Oxley Act itself was analyzed as an event. This research examined Baucus and Near's (1991) model of the illegal and corporate behavior process to test its ability to predict illegal behavior within historically corrupt industries. Moreover, CSR as an embedded theme within specific firms, and its implications toward both ethical and legal firm practices, was examined.

Kewords: Corporate social responsibility, internal controls, Sarbanes-Oxley Act, illegal corporate behavior, corporate corruption

French Abstract*

Illegal Corporate Behavior

Analyzing the Effectiveness of the 2002 Sarbanes-Oxley Act

Comportement illégal des entreprises

Analyse de l'efficacité de la loi Sarbanes-Oxley de 2002

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Résumé

Cette recherche examine les effets des facteurs environnementaux sur le comportement organisationnel illégal des entreprises ainsi que la capacité de la loi Sarbanes-Oxley de 2002 à modérer la relation entre des violations antérieures commises et un comportement illégal futur de l'entreprise. Les entreprises affichant un comportement socialement responsable (RSE) sont également examinées afin de déterminer la pertinence de concept RSE pour prédire un comportement illégal des entreprises. De plus, cette recherche fournit un niveau organisationnel et une analyse historique, cinq ans avant et après, des comportements juridiques dans l'ensemble des entreprises du Fortune 500. Enfin, cette recherche vise à déterminer si des antécédents d'un comportement illégal des entreprises peuvent être identifiés et si la loi Sarbanes-Oxley de 2002 peut être un outil législatif efficace pour influer sur les comportements des entreprises. La loi Sarbanes-Oxley elle-même a été analysée comme un événement. Cette recherche examine modèle de Baucus et Proche (1991), sur les processus de comportement illégal des entreprises, afin de tester sa capacité à prédire des comportements illégaux au sein d'industries historiquement corrompues. En outre, la RSE comme un thème intégré au sein des entreprises spécifiques ainsi que ses implications pratiques, éthiques et juridiques sont examinées.

Mots-clés : Responsabilité sociale des entreprises, contrôle interne, la loi Sarbanes-Oxley, comportement illégal des entreprises, corruption des entreprises]

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German Abstract*

Illegal Corporate Behavior

Analyzing the Effectiveness of the 2002 Sarbanes-Oxley Act

Illegales Verhalten im Unternehmen

Eine Analyse der Effektivität des Sarbanes-Oxley-Acts aus dem Jahr 2002

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Abstract

Diese Untersuchung betrachtet die Effekte der organisationalen Umwelt auf illegales Verhalten im Unternehmen und zudem die Fähigkeit des Sarbanes-Oxley-Act (SOX) aus dem Jahr 2002 die Ergebnisse früheren und zukünftigen illegalen Verhaltens zu beeinflussen. Corporate Social Responsibility (CSR) konformes Verhalten innerhalb der Unternehmen wurde zudem analysiert, um die Relevanz zur Vermeidung von illegalem Verhalten zu belegen. Vielmehr bietet die Untersuchung eine Betrachtung von legalen und illegalen Aktivitäten fünf Jahre vor und fünf Jahre nach dem Sarbanes-Oxley-Act für die Fortune 500-Firmen. Abschließend zielt die Untersuchung darauf ab, Einflussfaktoren auf illegales Verhalten abzubilden und die Wirksamkeit des SOX zu überprüfen. Der SOX selber wird hierzu als Event gesehen. Die Untersuchung nutzt Baucus und Near's (1991) Ansatz, um illegalen Verhaltens in Unternehmen vorherzusagen. Zudem wurde die CSR-Komponente für entsprechende Unternehmen eingebunden und die Auswirkungen auf ethische und gesetzliche Unternehmenspraktiken untersucht.

Keywords: Corporate Social Responsibility, Internes Kontrollsystem, Sarbanes-Oxley-Act, illegals Verhalten, Korruption]

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Spanish Abstract*

Illegal Corporate Behavior

Analyzing the Effectiveness of the 2002 Sarbanes-Oxley Act

Acciones Ilegales en las Empresas

Análisis de la Eficacia de la Ley Sarbanes-Oxley (2002)

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Abstract

Esta investigación examinó los efectos de los factores organizacionales ambientales en la conducta corporativa ilegal de las empresas, y también la capacidad de la Ley Sarbanes-Oxley de 2002 para moderar la relación entre las violaciones de la ley cometidas previamente y la futura conducta corporativa ilegal. También se examinó el comportamiento respecto a la Responsabilidad Social Corporativa (RSC) dentro de las organizaciones empresariales de cara a determinar su relevancia en la predicción del comportamiento de las empresas ilegales. Por otra parte, esta investigación proporciona un nivel de organización de análisis histórico (cinco años antes y después) del comportamiento legal a través de la lista de empresas *Fortune 500*. Por último, esta investigación tuvo como objetivo identificar antecedentes en el comportamiento corporativo ilegal y si la Ley Sarbanes-Oxley de 2002 puede ser un instrumento legislativo eficaz que impacte en el comportamiento de las empresas. Se analizó el hecho de la puesta en marcha de La Ley Sarbanes-Oxley en sí misma. Esta investigación examinó el modelo Baucus y Near (1991) sobre el proceso de la conducta corporativa ilegal para poner a prueba su capacidad de predicción sobre el comportamiento ilegal dentro de las industrias históricamente corruptas. Por otra parte, se examinó la RSC como un tema integrado en empresas concretas, y sus implicaciones, tanto éticas como legales, hacia las prácticas de las empresas.

Keywords: responsabilidad social de las empresas, controles internos, ley Sarbanes-Oxley Act, comportamiento empresarial ilegal, corrupción empresarial.

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Arabic Abstract*

Illegal Corporate Behavior

Analyzing the Effectiveness of the 2002 Sarbanes-Oxley Act

السلوك غير القانوني للشركات

تحليل فعالية قانون ساربينز أوكسلي 2002

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ملخص

درس هذا البحث آثار العوامل البيئية التنظيمية على السلوك الغير قانوني للشركات، وأيضا قدرة قانون ساربينز أوكسلي لعام 2002 على تعديل العلاقة بين انتهاكات ارتكبت في السابق و سلوك الشركات غير القانوني في المستقبل. وقد قامت الدراسة بالتطرق إلى موضوع المسؤولية الاجتماعية للشركات (CSR) لتحديد أهميتها في توقع سلوك الشركات غير القانوني. وعلاوة على ذلك، قدم هذا البحث تحليلاً تاريخياً و على المستوى التنظيمي، لمدة خمس سنوات قبل وبعد، لسلوك الشركات عبر القانوني في لائحة فورتشن 500. وأخيرا، هدف هذا البحث إلى تحديد ما إذا كان يمكن تحديد السوابق لسلوك الشركات غير القانوني وإذا كان قانون ساربينز أوكسلي لعام 2002 يمكن أن يكون أداة فعالة تشريعية تؤثر في سلوكيات الشركة. و تم تحليل قانون ساربينز أوكسلي نفسه كحدث.وتم فحص نموذج (Baucus and Near's, 1991) لدراسة السلوك والممارسات الغير قانونية للشركات لاختبار قدرته على التنبؤ بالسلوك غير القانوني داخل الصناعات الفاسدة تاريخيا. وعلاوة على ذلك، تم فحص CSR باعتباره جزءا لا يتجزأ من من العديد من الشركات الخاصة، والآثار المترتبة عليه تجاه الممارسات شركة الأخلاقية والقانونية على حد سواء.

الكلمات الدالة: المسؤولية الاجتماعية للشركات، الرقابة الداخلية، قانون ساربينز أوكسلي، السلوك الغير قانوني للشركات، فساد الشركات

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Italian Abstract*
Comportamento Aziendale Illegale
Analisi dell'efficacia della legge Sarbanes-Oxley del 2002

Comportamento Aziendale Illegale
Analisi dell'efficacia della legge Sarbanes-Oxley del 2002

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Abstract

Questa ricerca ha esaminato gli effetti sui fattori organizzativi di aziende protagoniste di comportamenti illegali, e anche l'efficacia della legge Sarbanez-Oxley del 2002 di moderare la relazione fra comportamenti illegali già compiute e comportamenti illegali futuri. Il comportamento aziendale rispettoso della società (CSR) è stato anche esaminato per determinare la sua efficacia nel predirre comportamenti aziendali illegali. Inoltre questa ricerca ha fornito, 5 anni prima dell'evento e 5 anni dopo l'evento, un'analisi storica di comportamenti legali di aziende che fanno parte del gruppo Fortune 500. Infine questa ricerca ha mirato a discernere se aneddoti riguardanti comportamenti illegali aziendali possano essere identificati e se la Sarbanes-Oxley del 2002 può essere uno strumento legislativo efficace. La Sarbas-Oxley stessa era analizzata nei suoi sviluppi. Questa ricerca ha esaminato il modello Bocus Near (1991) riguardante i processi di corportamenti illegali aziendali per mettere alla prova l'abilità di predirre comporamento illegale fra aziende il cui comportamento è stato storicamente illegale. Inoltre sono state analizzate le implicazioni della CSR, come tema integrante di aziende specifiche, e le sue implicazioni riguardo a pratiche sia etiche che illegali.

Keywords: responsabilità sociale aziendale, controlli interni, legge Sarbanes-Oxley, comportamento aziendale illegale, corruzione aziendale

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