Corporate Corruption: Building Public Confidence During Times Of Mistrust

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CORPORATE CORRUPTION:
Building Public Confidence During Times of Mistrust

by

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Chapter 1
Introduction and Overview

"Some investors believe that the worst is over, that no other scandals will erupt. But even so, the damage to investor confidence has been done." (The New York Times, Rebound From Ruin, If Not From Distrust, September 8, 2002) "It will take years for investors to trust again," said shareholder advocates. (Newsweek, "The CEO Party Is Over," December 30, 2002.)

This past year will go down in history as the "year of scandals in corporate America." A large number of recent corporate scandals, Enron, WorldCom, ImClone, and Tyco, involved Chief Executive Officers' with overflowing stock incentives that provoked greed, indulgence and fraud. These scandals unveiled a chain of companies with troubled finances, not necessarily as a result of scandalous behavior but because of overestimated profits after the 1990s Internet boom.

In the wake of scandals involving Enron Corp. and other companies in 2001, an October 2002 Harris Poll survey found that nearly 90 percent of Americans believe top executives had gotten rich at the expense of workers and shareholders.

Reportedly, the telecom and technology boom and bust over the past decade had skewed corporate expectations and financial judgments. Price-to-earnings ratios were multiplied by overly estimated future growth rates, putting new financial pressure on corporate leaders. In response, a select number of corporate leaders have lied and cheated to keep up with expectations when they should have just kept it simple and under-promised.

"I think it is fair to say that there was nobody in the business community who is not implicated in this in some way," said Jeffrey Garten, dean of Yale University's School of Management. (The Washington Post, In Blossoming Scandals, Culprits Are Countless, June 28, 2002) As long as the stock price rose, others who might have blown
the whistle--auditors, investment bankers, stock analysts, directors--also stood to profit greatly. With that said, bad habits were not rectified leading to long-term affects on share profits.

Several well-known stock analysts made large contributions to the fraudulent behavior. Henry Blodget, Merrill Lynch star Internet analyst, said one thing in internal emails and another in public reports, bringing down a $100 million fine on his firm. And Jack Grubman, Salomon Smith Barney's telecom analyst, has recently quit his $20 million-a-year job, but still faces lawsuits alleging, that he upgraded his rating on AT&T only so that his firm could get a lucrative underwriting deal from the telecom giant.

Analysts and accounting experts point out that many of the bookkeeping abuses of the 1990s, which led 330 companies to restate earnings last year and prompted the SEC to open 2,200 investigations of corporate finances, involved stretching or breaking rules and ethics guidelines that have been in place for decades. (The Washington Post, Culture Of Loopholes Bred Corporate Abuse, April 18, 2003.)

Experts said they believe the prevalence of big-bath charges grew during the 90s boom. Companies take “big baths” when they take charges for things such as restructuring costs, making their books look bad immediately but better in the future. “It became much more common and much more accepted to have a restructuring charge.” (The Washington Post, Culture of Loopholes Bred Corporate Abuse, April 18, 2003.)

When corporations prepare income statements, they are supposed to follow generally accepted accounting principles, which determine what can be counted as revenue and what must be counted as expenses. Some of the rules are very specific; others leave a fair amount open to interpretation. Revenue recognition -- booking revenue from the sale of products or services before they are delivered -- was the leading reason for financial restatements by public companies in 2002, according to Huron Consulting Group LLC, a forensic accounting firm. (The Washington Post, Culture Of Loopholes Bred Corporate Abuse, April 18, 2003.)
Politicians, auditors, analysts, lawyers, CEOs, are not the only experts involved in scandals on Wall Street. Some players in the media have given into the temptation. Seymour "Rudy" Ruderman, former broadcast editor of Business Week magazine, pleaded guilty to charges of trading on advance information gathered from stolen copies of the magazine's "Inside Wall Street" column the day before publication. He was released in November 1989 from a federal camp in Forth Worth, Texas, after serving six months. A former Wall Street Journal reporter, R. Foster Winans was convicted of secretly sharing the subject matter from his “Heard on the Street” column to a stockbroker in advance of publication. Winans served less than a year of an 18-month prison term.

The last year of scandals have been compared to the scandals of the 1930s. However, there reportedly has been a greater response by regulators and government to resolve misconduct in business. “This January the Securities and Exchange Commission issued more new rules than in any month since it was created in 1934 to clean up Wall Street, still devastated by the great crash of ’29.” (Newsweek, Living By Uncle Sam's Rules, February 17, 2003.)

Some industry experts are saying that reform is not the only movement toward preventing further outbursts of corporate scandals. Companies are beginning to concentrate internally, on its business integrity and reviewing business ethics. Big Four accounting firm Deloitte and Touch’s chief executive, James E. Copeland, said, “legislative and regulatory reforms aimed at restoring trust in financial reporting are no panacea.” (Atlanta Journal Constitution, Deloitte CEO Warns Of ‘Trap’ In Reforms, October 16, 2002.)

By the end of 2002, it was estimated that corporate scandals had cost the United States 200 billion dollars in investments, savings, jobs and pensions. This report was issued by the ‘No More Enrons’ coalition, partially funded by consumer groups and labor unions. “In Wall Street parlance, smart investors have ‘discounted’ for fraud, meaning
they now assume dishonesty in corporate auditing and have ‘priced it in’ when they calculate a stock’s value.” (The Washington Post, A Sorry Bunch, But Not Sorry Enough, July 7, 2002.)

Historic media reports show that the media has played a role in influencing the public’s perception of scandals. In 1934, U.S. political and economic commentator Matthew Josephson called the “economic princes” of his own day, “robber barons.” He wanted his audience to think back to European history, back to thugs with spears on horses who would bolster through town looting merchant caravans. He judged that their wealth was in no sense their own making but was like a tax levied upon the productive workers of the American economy. President Theodore Roosevelt spoke of “malefactors of great wealth” when he referred to economic capitalists, and built a political role for the government in antitrust: to curb and break-up private concentrations of economic power.

The media has been criticized throughout history for focusing on negative news and biased journalism. “The power of the media today constitutes the most significant exercise of ‘unaccountable power’ in our society,” (p.64, And that’s the way it isn’t). Today, news reporting is different then it was twenty even ten years ago. With 24-hour cable news stations, the media has too much time to offer opinion pieces leading to bias reports. News stations have covered CEOs in their final hour, escorted by the police out of their posh homes to face prison terms. The American public rarely had the opportunity through history to witness the humiliating arrest of corporate wrongdoers.

Today, in an effort to win back investor confidence, a series of corporate governance reforms have been mandated. President Bush appointed a Corporate Fraud Task Force to monitor his 10-point plan to restore faith and integrity in American business that included new laws and regulations. The most popular resolve amid a wave of business scandals that began with the collapse of Enron, was the Sarbanes-Oxley Act, which Congress passed in 2002. The premise of the act is to protect investors by requiring that financial reports of public companies be accurate and complete. The act requires that accountants answer to company audit committees, not management. It
prohibits accounting firms from providing most consulting services to audit clients. And it mandates disclosure of most "off-balance sheet" deals. While Sarbanes-Oxley applies only to publicly traded companies and the accounting firms they hire, local accountants say there's a possibility that the law, or portions of it, might one day also apply to private companies and their auditors. Also, in an effort to clean-up Wall Street investment firms, the Securities and Exchange Commission proposed new rules for analysts that call for increased oversight of research department activities by firms' compliance departments. This oversight would increase costs and reduce profits at brokerage firms. And, Chief Executive Officers have been asked to sign-off on year-end financial statements to ensure there accuracy.

Additional reforms created to prevent corporate fraud and document shredding passed in 2002 are the House Corporate Fraud bill which includes prison terms of up to 25 years for securities fraud; the House Accounting bill which creates a five member oversight board with disciplinary powers; and the Senate bill which includes 10 year prison terms for securities fraud and doubles sentences for mail and wire fraud and bans personal loans from company's to top officials (Enron CEO, Kenneth Lay's defense.) Other reforms have been passed concerning mutual and hedge funds.

There has been debate over the need for new regulations or strengthening the compliance of existing regulations such as greater punishments if policies are not abided. "A simple application of the law is not going to produce what people will perceive to be justice, because many of the things that have been happening are not necessarily illegal, even if the public considered them immoral," said Tom R. Tyler, a professor of psychology at New York University who specializes in the study of popular conceptions justice. (The New York Times, Even if Heads Roll, Mistrust Will Still Live On, October 6, 2002)

Where do we go from here? Through research, this paper will offer recommendations on how corporations could win back the public’s confidence during this time of mistrust as a result of corruption.
Research Question

What dimensions are necessary for building positive public perception of corporate entities during times of mistrust and misperception?

Subsidiary Questions

In an effort to comprehend the public’s reactions to the current corporate environment, this paper will concentrate on the following topics:

1. The history of corporate corruption.
2. Examining media perception during times of corporate corruption.

Definition Of Terms

#1- Accountants and Auditors: This position ensures that the Nation's firms are run more efficiently, its public records kept more accurately, and its taxes paid properly and on time. They perform these vital functions by offering an increasingly wide array of business and accounting services to their clients.

#2- Black Friday: Sept. 24, 1869, in U.S. history, day of financial panic. In 1869 a small group of American financial speculators, including Jay Gould and James Fisk, sought the support of federal officials of the Grant administration in a drive to corner the gold market. The attempt failed when government gold was released for sale. The drive culminated on a Friday, when thousands were ruined—the day is popularly called Black Friday. There was great indignation against the perpetrators. Several other days of financial panic have also been occasionally referred to as Black Friday.

#3- Carbine- A light, short barreled rifle.
#5- Dutch Tulip Mania of the 17th century - Great market for Tulips around 1630s. Market exploded but dropped suddenly causing the Amsterdam Stock Market crash.

#6- Enron- Investigation revealed that the energy company used off-the-book partnerships to conceal debt on balance sheets and inflate profits. Chairman Kenneth Lay took hundreds of millions of dollars in stocks and other benefits out of the company before it imploded. He invoked his 5th amendment rights against self-incrimination before Congress.

#7- 'Golden Parachutes'- Wall Street slang for the generous but controversial multimillion dollar severance benefits vanquished management can receive after a takeover.

#8-Great Depression- Worldwide economic collapse following the stock market crash in 1929, in which unemployment remained high for an extended period and many businesses failed.

#9- ImClone- The biotech company’s Chief Executive Officer Sam Waksal was indicted in 2002 on insider trading, bank fraud and obstruction charges. He allegedly warned friend Martha Stewart to sell her shares before stock went down and forged the company’s top lawyer’s signature on bank loans. Stewart’s Merrill Lynch broker and his assistant were fired after the assistant pleaded guilty to withholding information from federal investigators looking into the trading investigation.

#10- National Whistleblower Center in Washington- This national organization is dedicated solely to supporting individual whistleblowers. Since 1988, it has played a role in obtaining legal protections for those persons courageous enough to “blow the whistle” on corporate fraud, environmental violations and government misconduct.

#11- “Perp-walk”- One who perpetrates; esp., one who commits an offense or crime is being escorted by legal representatives [police] shamefully in front of a crowd of people.
#12- Railroad Robber Baron: A term coined in the 1900s, at the peak of track development, referencing businessmen engaging in fraudulent railroad business. These rings bribed state legislators and other officials and took the sale of bonds.

#13- Tyco International- Chief Executive Officer Dennis Kozlowski was indicted on charges he evaded more than $1 million in sales taxes; he is also charged with looting the company of $170 million and acquiring $430 million by covertly selling company stock.

#14-WorldCom- Chief Executive Officer Bernard Ebbers faced Congressional Committee and SEC investigation for company’s accounting fraud. The company improperly accounted for $9 billion.

Limitations

The survey was designed to interpret the public’s perception of the current corruptive environment in business over the past year. The limitations in this survey are quite extensive due to the fact that allegedly there were several links (trades) in the current chain of corruption.

With that said, this survey excluded industries involved in the past year of scandals including stock analysts, accountants, lawyers and Chief Executive Officers.

Summary and Transition Paragraph

The purpose of this paper is to acknowledge corporate scandals in America throughout history and review the effects such scandals had on investor confidence. Reviewing the events of the past year, it is obvious that corporate America has not learned from past scandals and the infamous “boom years,” in retrospect, invited more scandalous acts because every party involved wanted to keep the profit going, which was at an unusually high level.
The author picked the most significant scandals throughout history that had greatly affected the public, rules and regulations and the corporate system in general. The survey concludes and represents the public’s reaction to such corruption. Finally, the author recommends resolve to win back investor trust and confidence.
Chapter 2
A History Of Corporate Corruption

Great financial scandals...stock manipulation, insider trading, and bribing state or local government officials, have plagued world business for centuries. According to the author's research, many business historians are not surprised by the 2002 wave of corporate corruption. The fact is there has been a long history of abuses by capitalists who would not/could not place the public interest over their own greed. "The 'robber barons' might have been among the first, but their legacy lives on today," said Paul Tiffany, adjunct professor of management at both The Wharton School of the University of Pennsylvania and The Haas School of Business at the University of California.

Historians say a distinct pattern has evolved since the 1930s: scandal, usually a result of a bull market, followed by an impulsive crackdown, followed by a return to business as usual under the eyes of lenient regulators. "What you have here [in 2002] is an institutionalized structure feeding on itself -- slippage between the rules as written and the rules in practice," says Dale A. Oesterle, a University of Colorado law professor and critic of Wall Street's regulatory structure. (Business Week, A Sorry Legacy the Street Can't Shake, May 13, 2002.)

Historic events prove that the American way of business has always given corporate leaders a large playing field when it comes to pursuing and managing their activities in a self-regulated manner. Many experts in corporate corruption today are not shocked that individuals in large business once again took advantage of the autonomy of regulation. "It should be obvious that America has done the least to constrain its businesspeople relative to other advanced nations," Tiffany said.

America's legal concept of the corporation is rooted in its 17th-18th century origins, in England; the U.S. adopted these same concepts in our American legal system in the 18th and 19th Centuries, and still uses them today. When corporations were
“invented” they were essentially small. The corporation itself has a tremendous benefit for society: limited liability. As such, this legal form of business structure should and will remain in place. But when these corporations were small, the legal owners—shareholders—were also the people who worked in them. As the corporation grew in size at the end of the 19th century, they needed more capital than the in-house managers could accommodate so outsiders began to buy into shareholding.

In a famous 1932 study, it was found that over 90 percent of large firms in America were not controlled by the legal owners—shareholders—but rather were controlled by the managers who effectively had small stakes in ownership. The “legal owners”—the shareholders—had bought in only in the hope of the share price rising, not to exercise ownership responsibilities. This split between ownership and control is still a problem that haunts corporations in America today.

For most of the 19th and early 20th century some people “could cause the price of a stock to rise or fall by as much as 50 percent in a session,” wrote Robert Sobel, a historian and author of *Inside Wall Street: Continuity And Change In The Financial District*. (Beard Group, 2000) Some [people] he said could create millions of dollars in cash and then “push a favorite stock up or down getting out when the goal was accomplished.”

In the 19th century, railroad robber barons obtained a monopoly control of all railroads by peddling politicians and gaining millions of dollars from taxpayer subsidies. Jay Gould, a legendary railroad robber baron, earned most of his business through stock manipulation and paying off politicians. Aided by James Fisk and Daniel Drew, he defeated Cornelius Vanderbilt for control of the Erie Railroad and manipulated its stocks in his own interest and that of his group. Gould partnered with Fisk in a scheme to corner gold in 1869 that caused the Black Friday panic. Public protest forced the Gould group out of the Erie, ending with Gould’s expulsion in 1872. The Erie’s stock price plummeted, as investors concluded that Gould was paying the railroad’s money into shell construction companies that Gould owned and were not even up and running.
Richard Norton Smith, director of the Dole Institute at the University of Kansas said, “In some ways you could almost say that modern government arose around the beginning of the 20th century in response to the growth of a modern industrial economy and the abuse is represented by so called robber barons like John D. Rockefeller and J.P. Morgan.” (PBS NewsHour, Interview with Jim Lehrer, February 26, 2002)

John D. Rockefeller was best known for his “secret” business engagements. He would secretly purchase or create new oil-related companies such as engineering and pipeline firms, and disguise them as independent operators. Rockefeller would secretly control the firms and give his main oil company Standard Oil, hidden rebates, such as railroad rebates to transport his oil. He was pumping oil from his company at such low prices (which led to customer increase) because he was transporting the oil over the railroads at a low fee. J. P. Morgan was a very wealthy businessman who controlled the government with his money during a time when there was little regulations. He had sold 5000 defective carbines to Gen. Fremont, reportedly practiced “pillage, fraud, distortion.” Morgan gained control of great properties particularly railroads by what was later referred to as “Morganization” through the instrument of the voting trust, meaning shareholders voted to give their rights to Morgan’s board nominees, which resulted in added costs to operations and reduced value of original bondholders. His response to these results was, "I owe the public nothing."

It was almost 100 years ago in his first message to Congress that Theodore Roosevelt (served as president from 1901-1909) said that a modern industrial democracy government had a right acting as a steward on behalf of all the people to have access to all corporate information to investigate corporate functions, something we're talking about 100 years later. J.P Morgan and President Roosevelt had conflicting views about the state of American business during this time in history.

In 1913, a reform-minded accountant named Arthur Andersen started his firm on the promise of offering investors an alternative to the lax accounting standards that had
existed and were then prevailing. 89 years later, Andersen imploded after being charged for obstruction of justice after auditors destroyed important Enron documents. Enron is the energy company under investigation for its off-balance sheet partnerships, hiding debt and inflating earnings, it filed for bankruptcy in December 2001.

Business historians have said that the circumstances and events that led to the 1920s market-boom were similar to those of the 1990s market boom. At both times, new technologies and the power of industry promised great wealth to companies and the public. In the 1920s, it was the automobile, radio and the regional electric utility. In the 1990s, it was the Internet.

Devastating financial racketeering scandals crushed investor confidence and led to the stock market crash of 1929 and the Great Depression. President Herbert Hoover had to act promptly to deter a panic of poverty among Americans. He promised a reduction in taxes. Hoover called a series of conferences of business leaders who expressed public disapproval of the idea of lowering wages. He recommended the building of public works to take up the impending slack in employment. And he and his associates set themselves to build up the shaken morale of business by proclaiming that everything was all right and presently would be still better; that “conditions” were “fundamentally sound.” President Hoover said, “I am convinced that through these measures we will have reestablished confidence.”

Public anger over the scandals helped defeat President Hoover in the 1932 election. The shift to a new congress and a new president, Franklin Roosevelt brought hope to the American public crushed by crooked business. Roosevelt spoke of “the ruthless manipulation of professional gamblers and the corporate system.” (Counterpunch, Ferdinand Pecora: An American Hero, January 11, 2003) He lashed out at the “economic nobles,” that had allowed “a few powerful interest to make industrial cannon fodder of the lives of half the population.”
In an effort to restore public confidence and clean-up big business, Roosevelt ordered for Wall Street banks to be prosecuted. Ferdinand Pecora was counsel in the National City Bank (NCB, known today as Citicorp) hearings. Among the conspirators was “Sunshine Charley” Mitchell, president and chairman of the board of the NCB. He had a reputation of selling bonds based on tips from the inside. Just like some of today’s headlines, “Mitchell himself constantly traded on inside information whether it was the knowledge that a company which NCB had just brought public wasn’t nearly as profitable as promoted, or the fact that foreign governments were about to default their obligations.” (StocksandNews.com, by Brian Trumbore, 2002.) It was a case similar to the current scandals surrounding Wall Street banks. Congressional investigators uncovered evidence that the NCB had pushed its brokers to sell Peruvian bonds to clients while knowing full well that the Peruvian government was on the verge of default. Although Mitchell did not do anything criminal, he had misguided his own stockholders and the investing public for his own benefit. Charles Mitchell was forced to resign as president of NCB and was tried for income tax evasion in 1934, yet acquitted.

This scandal led to legislation that created the Securities and Exchange Commission (SEC) and separated the banking industry from Wall Street investment houses. That separation was effectively cancelled during the 1990s. Again, today New York Attorney General Eliot Spitzer is motioning to strengthen separation after Wall Street banks recently were involved in insider trading.

The SEC was formed to protect the investor and maintain the integrity of the securities industry. The institution requires public companies to disclose meaningful financial and other information to the public, so individuals or large companies can make sound investment decisions. The SEC also oversees other key participants in the securities world, including stock exchanges, broker-dealers, investment advisors, mutual funds, and public utility holding companies.

Business scandal in the 1970s involved [overseas] bribery scandals, deceitful mergers and acquisitions, and illegal political-contributions scandals. The Gulf Oil
Corporation was charged with paying out $5 million to government officials in South Korea and Bolivia. During this time, there was nothing in American law that prohibited bribery, although under the SEC, it is a criminal offense for a company to disguise such payments from shareholder accounts, which Gulf Oil did unsuccessfully. In January 1975, U.S. companies publicly admitted to making more than $300 million in questionable or illegal political payoffs. As a result of the Gulf Oil scandal, the Federal Election Commission instituted a political action committee that would solicit contributions for candidates of a company's choosing.

Another example of overseas bribery and corruption in the mid-70s involved United Brands Company. "Had not Mr. Eli Black, chairman of the United Brands Company, jumped from the 44th floor of the Pan Am building in Manhattan, the $2 million that the company handed out in bribes to government officials in Honduras and Italy might never have been discovered." (The Economist, Business Corruption: Banana bribes, April 19, 1975.) Again payment of bribes to government officials was not against the law at the time, however again the SEC was able to bring suit against the company since, shareholders were not notified of the bribes.

A well-respected management guru, Peter Drucker compared the merger and acquisition boom of the 1970s to "a pattern of fraud, deception and manipulation comparable to the stock market swindles of 1929." (The Washington Post, Business Guru Drucker Sees Insider Case Reminiscent of '29 Swindles," February 16, 1987.) He believed that managements of some takeover targets might have conspired with their acquirers. "'Golden Parachutes'-- may have perverted management's ability to act beyond its self-interest."

In the late 1970s, the SEC unraveled a scandal that was 20 years in the making involving General Services Administration (GSA). Members of the organization colluded in illegal and improper federal agency contract awards. Indications of fraud were uncovered in some contracting for building repairs, alterations, and services in the Washington area. Also, in the 70s, the Equity Funding Corporation of America created
fake insurance policies, fake documents, and inflated profit reports in the hopes that it could one day buy a legitimate insurance company. The widespread fraud was known by as many as 1,000 people, but it took a whistle-blowing ex-employee tipping off a Wall Street analyst to bring the scandal out in the open. As a result, insurance and auditing regulations were tightened.

In the 1980s, there was a rapid succession of insider-trading scandals. Insider trading refers to the trading of securities on the basis of important information, such as a pending takeover offer or stock buyback plan, that has not been announced to the general public. Federal law prohibits individuals with access to inside corporate information from using that material to reap profits in the stock market.

"The Dennis Levine case started an almost domino effect into the investigation of insider trading." (The Associated Press. Former Investment Banker Dennis Levine Sentenced to Prison Levine, February 20, 1987.) Levine, a former managing director at Drexel Burnham Lambert Inc., led the Securities and Exchange Commission to Wall Street speculator Ivan Boesky, who was accused of making $50 million in illegal profits from trading on inside information supplied by Levine. Levine publicly admitted one illegal transaction: a 1984 purchase of Jewel Companies stock which he knew would soon be the subject of a takeover bid. When the bid from American Stores Inc. was made public, the value of Jewel stock soared and Levine sold the stock at a $1.2 million profit.

The SEC charged Ivan Boesky, speculator in takeover stocks at Drexel Burnham Lambert Inc., with illegally trading on information not available to the public and conspiracy to make false statements to the SEC. He paid $50 million in fines and $50 million in disgorged profits and also pleaded guilty to one count of lying to federal regulators to settle his case in 1986. Boesky testified against some old Wall Street friends, information that was used in cases against high-profile financiers ranging from Victor Posner to Michael Milken. Boesky served two years of a prison term. Former U.S. attorney Rudolph Giuliani prosecuted Boesky and other Wall Street criminals during this era of corruption. Boesky's attorney was former chairman of the Securities and Exchange
Commission, Harvey Pitt. He resigned from this position during the wave of corporate corruption in 2002.

Giuliani led the indictment against Richard Wigton, former vice president of Kidder, Peabody and Co.; Timothy Tabor, a former vice president at Kidder and Merrill Lynch & Co.; and Robert Freeman, a former partner at Goldman Sachs. All three were charged with violating securities laws by making illegal securities trades using non-public information, otherwise called insider trading. Television networks taped the men handcuffed and arrested at their office and homes, similar to today’s “perp-walk.” In May 1987, the prosecutors voluntarily dropped the charges after a judge refused the government more pretrial preparation time. Giuliani later admitted that his team arrested the men too early in the investigation. In 1989, the U.S. attorney's office ended its probe of Wigton and Kidder co-worker Timothy Tabor. However, former Goldman Sachs & Co. arbitrager Robert Freeman agreed to plead guilty to one felony.

“The grasp-and-greed era of the 1980s tempted many go-getters, even respected professionals, to cut corners on ethics and lunge for the quick money.” (Cleveland Plain-Dealer, An S&L Humbling For Jones, Day, 1990, Op-Ed.) Another example of the decade’s corporate irresponsibility was the savings-and-loan scandal and the man behind the nation’s largest thrift failure, was Charles H. Keating Jr., the Cincinnati swindler who was convicted of looting his Lincoln Savings & Loan (owned by his American Continental Corp.) and costing taxpayers about $2.5 billion. He was accused in federal court of fraud and conspiracy. The “Keating controversy” involved five U.S. senators accused of helping Charles Keating’s Lincoln Savings & Loan avoid fraudulent charges, in return for large campaign contributions. Big Four accounting firm Ernst & Young had reached a $400 million out-of-court settlement with federal regulators over its “botched” audits. Among the clean-up tactics, the Senate had approved a broad crime bill that stiffened prison terms for federal crimes. The scandal also inspired a number of campaign finance reforms. Bush did approve a stiffened campaign reform bill in 1991. “There is just no question that the reason these contributions were made was to buy favorable support, favorable laws,” said Sen. William Proxmire, D-Wisconsin, former Banking

The Lincoln Savings & Loan scandal produced prosecutions and regulatory overhaul, but accountants were not prosecuted and it was as much of an accounting debacle as Enron. However the accounting industry was also to blame for the fraudulent behavior. The accountants allowed thrifts to keep junk bonds on the books at cost, rather than marking them to market when they lost value. “The Savings & Loan scandal did not result in any reforms – it resulted in just the opposite, a so-called reform act that made accountability less important,” noted Melvyn I. Weiss, a prominent securities lawyer representing plaintiffs.

A 1986 Business Week magazine poll, suggested that most Americans believe “insider” trading of securities was common on Wall Street and that most of them also would buy stock based on an inside tip. At one point the definition of insider trading was so vague it sounded almost legal. Regulators moved to revise its definition in an attempt to get justified convictions.

The Penn Square Bank scandal involved misconduct and fraud that temporarily shook up the banking system. Federal regulators cited fraudulent energy loans when they closed Penn Square Bank in July 1982. The scandal left financial institutions nationwide with billions of dollars of bad loans. Coopers & Lybrand, the accounting firm (Coopers & Lybrand merged with Pricewaterhouse in 1998 to form PricewaterhouseCoopers) allegedly conspired with Penn Square Bank to fraudulently promote Swan's Longhorn drilling ventures.

As a result of the market crash of 1987, several Federal agencies had joined a broad investigation of stock manipulation, using evidence that came to light F.B.I. agents were being trained by the SEC to recognize market manipulation. Then-U.S attorney Rudolph Giuliani described these forces as “a task force without a name.” (The New
History is filled with scandals that have not been rectified through improving regulations. Consider the collapse of Long-Term Capital Management (LTCM) in 1998. Attention focused on LTCM's leverage and use of derivatives and on the secret world of hedge funds. Study commissions were appointed and legislation was proposed to resolve the corruption but nothing resulted. Likewise, the penny-stock scams of the 1980s resulted in regulations, known as the sales-practice rules governing shares trading at less than $5, but these were reportedly ignored during the 1990s by a new generation of stock scammers.

Events of corruption throughout history show that Wall Street has a way of avoiding the best regulations. For example, there was the controversy with price-fixing on the Nasdaq Stock Market in the 1990s. After years of complaints that market analysts colluded to fix-prices, the Justice Department brought suit. The result was a set of new order-handling rules designed to get customers fairer prices. But then-chairman Arthur Levitt was alarmed and disappointed with the failure to comply by those rules and an SEC study in 2000 showed and confirmed a great failure among financial institutions to comply.

"The late 1990s environment of 'greed without fear' is what caused the current rash of scandals," said Peter Knutson, emeritus accounting professor at the University of Pennsylvania's Wharton School. (The Philadelphia Inquirer, Scandals Hit, Tarnish Many; Balance-Sheet Cheats Are Rare, Experts Say, July 20, 2002.) In recent years, some companies, such as Enron Corp., WorldCom Inc. and Xerox Corp., have generated fake numbers by counting revenue too soon, by exchanging similar goods with a rival and both booking the transaction as revenue, by shifting current expenses to later periods, or by hiding debts.
Enron has adopted the reputation of being the “largest bankruptcy in American history.” The company’s own filings showed that the top executives made out like bandits, cashing in $614 million in Enron shares in two years while encouraging employees to buy even more stock, meanwhile actively chiseling away at employees pension plans. WorldCom is referred to as one of the largest accounting fraud in history. In 2002, an internal audit discovered executives had pumped up profits over the last 15 months. Andersen was its auditor since 1989. Xerox inflated revenue by $1.9 billion over the past five years by misreporting sales of equipment and service contracts. The copier company posted too much revenue from equipment contracts upfront instead of over the life of the leases for servicing and financing equipment. That had the effect of pumping up a given year’s revenue figure.

Presently, even companies that are remotely connected to scandal-ridden companies have fallen under the “guilt by association” factor by the public. For example, Mirant, an Atlanta-based energy company, has been involved in many of Enron’s businesses and just this year ranked No. 52 on the Fortune 500 list, but as of September 6, 2002, in the height of scandalous reports, Mirant’s stock fell from $47 a share in May to $13.64. According to Marc Fuller, CEO of Mirant and ranked by Fortune as the fifth most powerful businesswoman in the U.S., “We’ve led the way to be very open in our disclosures and had no characteristics of Enron, but investors are more skeptical these days.” (USA Today, Scandals, Setbacks Topple CEOs Formerly Golden Image, April 8, 2002.)

Once again, corporate scandals have affected political views, for instance some people question the 2002 campaign funds. ImClone’s indicted chief, Sam Waksal had donated $25,000 to Hillary Rodham Clinton during her run for governor. In an attempt to avoid public scrutiny, Senator Clinton gave the contribution to charity. Karen Dunn, a spokeswoman for Mrs. Clinton said that Mrs. Clinton had decided to give up the donation because “it is the right thing to do and it is important to take action that will restore faith in both our markets and our political system.”
The greatest challenge today for Chief Executive Officer’s and Congress is to rebuild the reputation of America’s big business. Corporate scandals stemming mostly from accounting irregularities, has created a shaky economy; an increase in unemployment; and lost shareholder and retirement savings. According to economic historians, the kind of corporate chicanery that occurred in 2002 occurred after every financial bubble since the Dutch Tulip Mania of the 17th century. And, experts say, it could be months or even years before the full extent of the damage is revealed and the final bills come to light.

The extended excitement of the [1990s] Internet boom years led to a slow, steady deterioration in professional and ethical standards. Some experts argue that many companies were engaged in the kind of fudging, gamesmanship and ethical misbehavior that, while legal, is unacceptable in today's post-boom environment. Paul Tiffany points out that “business training over the past twenty or so years has shifted far more to bottom-line orientation rather than some other equally worthy topics.” A message was taught in the classroom during the 1970s and 1980s that rather than profit being the reward for producing and distributing quality products/services that were competitively priced, “we put the cart before the horse: get the profit by any means,” Tiffany said.
Chapter 3
Research Perspectives And Perceptions

Investor confidence is crucial to the success of our economic system. Over the past two years, this confidence has been threatened by the historic pressure on Chief Executive Officer’s to deliver high shareholder value; lax regulations; and the dramatic decline in accounting standards.

By the end of 2002, publicly traded companies were worth 7 trillion – 43 percent—less than they were at the market’s peak in early 2000. Also, nearly $20 billion has left stock mutual funds. With the post-90s Internet bubble burst (or explosive stream of profit) and the threat of war, the market was bound to suffer over the past year and a half, but would it be better if corporate scandals did not occur? David Dreman, the Jersey City (N.J.)-based guru of contrarian investing (a contrarian investor generally focuses on turnaround situations and stocks currently out of favor) ventured a guess to this observation and said that leading market indexes might be 5 to 10 percent higher now if it were not for the scandals. “We have not had a breakdown like this in corporate governance and ethics since 1929,” he said. (Philadelphia Inquirer, Imagine Stock Market Without 2002 Scandals, December 29, 2002)

It is getting increasingly harder for the public to find out what a company actually earns and what its stock is actually worth. In 2002, an astonishing 723 companies had been forced to restate and lower their earnings since 1997. The Securities and Exchange Commission enforced this action in an effort to increase investor confidence. The Sarbanes-Oxley bill by Congress, proposed in response to the scandals, has been accepted with mixed reviews. Some critics say the bill was created to quick, too rash and too impulsive.

In 2002, Xerox, Vivendi, Global Crossing, Gazprom, and other accounting-related scandals came down hard and fast. Experts say that a myriad of business parties, in addition to the accounting industry, contributed to the influx of scandals. Economic
critics also say that greed, share price, and power are significant reasons for chief executives to alter financial statements such was the case with Enron and WorldCom.

For investors blaming the scandals solely on Chief Executive Officers’ or Chief Financial Officers’ its important to point out that, in addition to both these parties and other leadership respectively, accountants, auditors, lawyers, and analysts play a role in business practices that affect the company and shareholders. Muriel Siebert, the first women of Wall Street and business author said, “It was not just the company and its executives. It was not just the accountants. They had to get legal opinions from a law firm. They had to get the derivatives from banks and Wall Street firms. One group alone could not have done it.” (The New York Times, Siebert interview, November 24, 2002)

A New York Securities lawyer said that Congress should share the blame for Enron when it passed the Private Securities Litigation Reform Act of 1995. “The government removed the ‘ aider and abettor’ rules, so accountants, lawyers and consultants could give advice without any liability.” Another factor that could have led to scandals, most notably the savings-and-loan scandals, was the era of deregulation under President Reagan (served as president from 1980-1988.) Taking away regulations that were set in place for decades earlier, sparked competition and a ‘no holds bar’ effort to increase profit and lead an industry, whether it was the energy industry or aviation.

We can also examine the other side of the coin when it comes to regulations. In examining the history of reforms, each new reform creates a new link (or headache) in the economic chain of circumstance. For instance, previous reforms aimed at providing investors more timely information about the profitability and financial condition of public companies. Thus began the focus on quarterly earnings. Other reforms tied executive compensation to performances as indicated by the company’s stock price. Thus began the use of stock options for executive compensation. Followed by the great pressure brought to company leadership to keep stocks high and corporate boards satisfied.
The concept of stock options sounds good in theory, but instead of treating the stock like a successful company earning, Chief Executive Officers began boosting their own net worth as well as the boards, often crippling the system along with the company’s long-term prospects. During the downsizing of the early and mid-90s, reports show that Chief Executive Officers have been criticized for favoring shareholders rather than other groups, most notably employees and communities. Now even shareholders feel betrayed as a result of the corruptive actions by select Chief Executive Officers.

In 2002, a dozen of Wall Street investment firms have been under investigation. New York Attorney General Eliot Spitzer charged the industry’s largest companies for a range of crimes, most of which revolved around allegations that they routinely lied to investors to generate additional business for themselves. “If I’m an investor...I watch the scandals and say, ‘Not only did Wall Street punish me by having me hold onto losing stocks for the past three years, but now I find that some of the books were cooked as well,’” said Ned Riley, chief investment strategist at State Street Global Advisors. Wall Street brokerages paid more than $1 billion in fines to settle charges that they misled investors.

According to a survey by Cavendish Asset Management in September 2002, almost half of the respondents said they had no faith in advisers, analysts or stockbrokers following the downfall of the US corporate gains. When asked to respond to “the Enron/Worldcom scandals show you cannot trust even professional people such as investment advisers, analysts or stockbrokers with investment advice,” 47 percent said they agreed with the statement. Younger investors were most concerned with 59 percent now refusing to trust advisers.

The era of the celebrity Chief Executive Officer had its beginnings in September 1979 with the arrival of Lee Iacocca to Chrysler Corp. He rescued the company at a time when America’s economic self-esteem was withered and captivated the public’s attention like no other Chief Executive Officer since the robber barons. Never mind that Chrysler’s
turnaround required a huge government bailout or that its stocks lagged behind the market during the second half of his tenure, he had a presence like no other Chief Executive Officer of that time. He appeared in more than 80 of his own commercials. The public related to him. The media coverage helped foster helped foster the impression of a great leader, whether he was or not.

We haven't heard much this year from working Chief Executive Officers themselves. But there are exceptions in the Chief Executive Officer arena, for instance Henry Paulson Jr. of Goldman Sachs and Dick Grasso of the New York Stock Exchange. Paulson was especially outspoken, “American business has never been under such scrutiny. To be blunt, much of it is deserved,” he said at the National Press Club in Washington recently. “These guys deserve big credit for guts, because they're risking the wrath of their peers, alienating customers and inviting scrutiny,” he added.

Aside from losing respect from peers, experts say there will be more Chief Executive Officer firings this time around as previously passive corporate boards get tough with the boss, there will most likely be 10 percent less in their pay package and the Chief Executive Officers that did the “perp-walk” will most likely be trading in their pinstripes for prison stripes in 2003.

What bothers many investors, particularly the old-school investors that have watched their earnings flourish in the 90s tech-boom and disintegrate, due to the scandal-infected economy, is that many of the executives accused of wrongful gains still have not faced charges. Former Enron chairman Kenneth Lay remains under indictment and so does Martha Stewart, who has dodged insider-trading charges and just refuses to answer any questions regarding the investigation.

“When it comes to arrogance, power and lack of accountability, journalists are probably the only people on the planet who make lawyers look good.” – Steven Brill.
There are more than fewer media elites that have expressed a liberal bias when reporting the news. Former CBS news reporter Bernard Goldberg felt it in the reporting of fellow news anchors like Dan Rather. He brought his story to the Op-Ed section of the Wall Street Journal to share with the world the bias that showed up too often on the evening news. His example of a story reported with bias was a report by Eric Engberg (CBS) that ridiculed Steve Forbes, (former presidential candidate for the 1996 election and founder and Chief Executive Officer of Forbes, Inc.) views of the flat tax. Anyone who opposes the flat tax is most likely from the “Left.” Liberals have an uneasy feeling about tax cuts in general, and are hostile toward tax cuts that benefit the wealthy in particular, even if they help out the rest of Americans. After the Wall Street Journal article was published the executive producer of the CBS evening news, Andrew Hayward said what Goldberg did was, “an act of disloyalty” and a “betrayal of trust.”

Goldberg claims that reporters tend to call on experts that best fit the slant of their story. “Well news fans, here’s one of the dirty little secrets newscasters are never supposed to reveal to the regular audience: a reporter can find an expert to say anything the reporter wants!” (Bias: A CBS Insider Exposes How The Media Distort The News, 2002)

David Aubrey, one of the editorial columnists of the Wichita Eagle, in Kansas, referred to journalists as “having little understanding of the working class middle-American family.” (p. 25)

The 80s were known as the “Reagan Years.” Through the media, Reagan was created as Norman Rockwell world of family values. He told the American people what they wanted to hear with news reports saying Russia was a terrible empire and Americans pay too much in taxes. (p. 54)

There are recorded incidents that major news anchors have chosen to be loyal to the major conglomerates that sign their paychecks rather than report the news to the public. On January 2, 2001, The Wall Street Journal ran a lead story on page one
reporting that federal safety officials were looking into problems with a certain General Electric (GE) airplane engine. After the story broke GE confirmed that the Wall Street Journal got the story substantially correct and came out publicly with an explanation. GE stock went down because of the news. All the news stations covered it, but Tom Brokaw did not cover it on Nightly News because he decided not to “attack” GE, his own organization.

Twenty years ago you would not have seen on television Chief Executive Officers getting arrested or hear the disclosure of Chief Executive Officers compensation and incentives through their divorce proceedings on the radio. Today’s media follows the juicier stories but that’s what the public demands. It appears through research that more people are interested in listening to corporate scandal trials then resolutions or issues of corporate regulation. Debates about corporate behavior that have been percolating for years have become mainstream once again.
Chapter 4

Research Results: Outcomes And Opinions

Description of the Survey

The survey (see Appendix A) included ten statements that were measured on the basis of the Likert scale: a survey system utilizing a five-point scale. The rating scale ranged from five to one: five meaning that the individual strongly agrees with the statement, four implies the individual agrees with the statement, three states that the individual takes a neutral stand on the statement, two signifies that the individual disagrees with the statement and one indicates that the individual profoundly disagrees with the statements. In reviewing the ten statements that were designed for this survey, each had a general stance on the effects of present corporate scandals. The author’s incentive was to understand the public perception of big business as a result of the past year’s unraveling of corporate scandals.

Sample

The goal was to survey 35 individuals (33 were included) in order to receive a quantitative response that would be relevant to this study. The participants are U.S. citizens, over the age of 25 and employed.

Purpose of the Survey

The intent of developing this survey was to assess the public’s perception of the past year of corporate scandals. Specifically, the author wanted to get an idea of the public’s reaction to the past year of corporate scandals.
Quantitative Results

Statement 1: In reading the papers and watching the news, it appears that a large number of Chief Executive Officers unethical and corrupt.

For this statement, four respondents (12 percent) strongly agreed that, “In reading the papers and watching the news, a large number of Chief Executive Officers are unethical and corrupt.” 15 respondents (45 percent) agreed with statement one. Seven respondents (21 percent) took a neutral position. There were 5 respondents (15 percent) who disagreed with this statement and there were two respondents (6 percent) who strongly disagreed.

Since the majority of respondents (45 percent) agreed, the author concludes that there is a belief among the public that, “a large number of Chief Executive Officers are unethical and corrupt.” This number could be a product of biased media reporting. It is the author’s belief that the media spent more time reporting on Chief Executive Officer scandal-ridden companies, when in fact there was really only a handful of company’s with faulty Chief Executive Officers.

Statement 2: It is quite apparent now that Enron was not an isolated incident of major corporate scandal.

In evaluating this statement, 11 respondents (33 percent) strongly agreed “it is quite apparent now that Enron was not an isolated incident of major corporate scandal.” 16 respondents (48 percent) agreed with statement two. Six respondents (18 percent) took a neutral position. Zero respondents disagreed and zero respondents strongly disagreed.

By the majority of respondents (81 percent) it is evident that a substantial number agree with this statement. Based on this statistic, the author’s confirmed her belief that a majority of the public feels that Enron was not an isolated incident but in fact, just the
first scandal to be disclosed. It tipped off further investigations into disclosure, corruption, and reform.

Statement 3: In general, most corporate Chief Executive Officers seem to have too much power and too much ability to profit illegally and/or unethically from their businesses.

The breakdown of respondents for this statement went as follows: seven respondents (21 percent) strongly agreed that “in general, most corporate Chief Executive Officers seem to have too much power and too much ability to profit illegally and/or unethically from their businesses.” 18 respondents (54 percent) agreed with statement three. Five respondents (15 percent) took a neutral position. Three respondents (9 percent) disagreed. Zero respondents strongly disagreed.

The majority of respondents (75 percent) either profoundly agreed or agreed with this statement. This confirms the author’s belief that a majority of the public feels that Chief Executive Officers have too much power and the author suggest that a company’s board of directors must play a larger role in the decision-making as well as manage the lines of leadership.

Statement 4: It is unfair that an entire company should suffer due to the actions of a few corrupt leaders.

In assessing statement four, 19 respondents (57 percent) strongly agreed with the statement, “it is unfair that an entire company should suffer due to the actions of a few corrupt leaders.” Eleven respondents (33 percent) agree with statement four. Zero respondents had a neutral reaction. Three respondents (9 percent) disagree. Zero respondents strongly disagreed.

Overall, according to the majority of respondents (90 percent) strongly agree or agree, proving a majority believes that an entire company should not suffer due to the actions of a few corrupt leaders. The author chose this statement to exemplify the
public’s reaction to the sudden implosion of Andersen. More than 28,000 U.S. employees lost their jobs. Andersen, a Chicago business institution for 89 years, disintegrated after it was indicted and convicted by the U.S. Justice Department for destroying documents proving the financial deception of Enron Corp. Allegedly, Enron kept debt off the books through complex partnerships.

Statement 5: For the most part, the government has done all it can to alleviate investor mistrust.

The results for statement five were as follows. Zero respondents strongly agreed with the statement “for the most part, the government has done all it can to alleviate investor mistrust.” Three respondents (9 percent) agree with statement five. Four respondents (12 percent) remain neutral. 19 respondents (57 percent) disagreed. Seven respondents (21 percent) strongly disagreed.

Overall the majority of the respondents (78 percent) profoundly disagree with this statement. The opinions and beliefs of these respondents suggest that in order for the government to win back the public’s trust it must be proactive and strengthen existing reforms to avoid future corporate misdeeds even if the economy recovers.

Statement 6: The media has great influence in my investment decisions.

Upon examining statement six, the results were as follows. Three respondents (9 percent) strongly agreed “the media has great influence in my investment decisions.” Ten respondents (30 percent) agreed with statement six. Six respondents (18 percent) remain neutral. Ten respondents (30 percent) disagreed. Four respondents (12 percent) strongly disagreed.

Overall, this is a split decision (60 percent) with (30 percent) of the respondents agreeing that the media has had influence over their investment decisions and (30
percent) disagree with the statement. The author assumed that the media’s reporting throughout the scandals of 2002 confused the public and displayed too much bias.

Statement 7: The corrupt accounting practices of firms like Andersen have contributed substantially to the downturn in the economy.

In reviewing the results for statement seven, two respondents (6 percent) strongly agreed “the corrupt accounting practices of firms like Andersen have contributed substantially to the downturn in the economy.” 14 of the respondents (42 percent) agreed with statement seven. Eight of the respondents (24 percent) remained neutral and an additional eight respondents (24 percent) disagreed. One respondent (3 percent) strongly disagreed with the statement and added, “it is not the accounting practices but the greed of the individuals involved in the corruptive practices that contributed substantially to the downturn of the economy.”

Overall, the majority of the respondents (42 percent) agreed with the statement indicating to the author that the public does not feel that strong that accounting firms like Andersen are to blame for the troubled economy. The author agrees that accounting firms are not the only institutions to blame for this economic debacle. The low number is surprising being that there was a media frenzy against the accounting firms involves in the scandal of big corporations as well as the high media exposure of Andersen throughout its implosion.

Statement 8: Big corporations need stringent government regulations to remain honest.

Responses for statement eight were as follows: Five of the respondents (15 percent) strongly agree, “big corporations need stringent government regulations to remain honest.” 13 of the respondents (39 percent) agree with statement eight. Five of
the respondents (15 percent) remain neutral. Eight of the respondents (24 percent) disagree. Two of the respondents (6 percent) strongly disagree.

Overall, a majority of the respondents (54 percent) profoundly agreed or agreed which suggests that there is a belief that new regulations are integral to keeping companies honest. Which mirrors the author’s belief that there needs to be a push for corporate governance countrywide.

Statement 9: At this point in time, my trust in stock analysts and investment firms is waning.

For this statement, eight respondents (24 percent) strongly agree with "at this point in time, my trust in stock analysts and investment firms is waning." 11 of the respondents (33 percent) agree with statement nine. Seven of the respondents (21 percent) remain neutral. Seven (21 percent) disagree with this statement and zero strongly disagreed.

Overall, a majority of the respondents (67 percent) profoundly agree showing the author that investment firms like Merrill Lynch have displayed signs of greed and need to adhere to strict regulations that watch out for the best interest of the investor.

Statement 10: We have probably not seen the end of significant corporate corruption.

15 of the respondents (45 percent) strongly agreed with "we have not seen the end of corruption." 17 of the respondents (51 percent) agreed with statement ten. There were zero respondents that remained neutral. One of the respondents (3 percent) disagreed. And, zero respondents strongly disagreed.

Overall, a majority of the respondents (96 percent) profoundly agreed, confirming the author’s belief that the public expects scandals to be a part of capitalism, it’s an essential component of large corporations and the economic system. Standards should be
strengthened because the extent of this past year of corporate greed can be contained in the future. A greater stand should be taken internally on developing ethical business practices and relationships. A cynical response from one of the participants on fostering an honest corporate environment is as follows, “Values are time sensitive—what we value today may change in a week. Teaching ethics to corporate executives does not bring lasting change. Changing the culture takes 3-7 years minimum.”

Conclusion

The survey participants were glad to participate and interested in learning of the results. The topic universally affects all employed Americans but to what degree varies. A large number of the results validated the author’s points. Although, there was two revelations within these findings. First, the result to question six, “the media has great influence in my investment decisions” was split with 30 percent agreeing and 30 percent in disagreement. Considering the heavy media attention and significant drop in the stock market at the time of expert interviews, national surveys and “perp-walk’s,” the author expected that a larger number of the participants would have agreed that the media had a great influence on their activity in the market during this time of mistrust.

Second, the result for question seven was surprising, “the corrupt accounting practices of firms like Andersen have contributed substantially to the downturn in the economy,” in that less than half of the participants agreed with the statement hence, the public does not feel that accounting firms like Andersen are to blame for the troubled economy. Another significant response to this question was 24 percent of the respondents in fact disagree, while another 24 percent are neutral. These numbers are surprising considering the past year of negative media reports on the role of the accounting firms in corporate scandals and the alleged mastering of “cooked books.”
Chapter 5
Conclusion & Summary

The purpose of this paper is to express the author's recommendations on how to restore investor confidence in big business during times of mistrust and misperception. This paper examined infamous scandals throughout history; public reactions; existing and new regulations, and expert opinions on scandals throughout history. According to the author's survey, big corporations have a long way to go in order to win back investor confidence. In the meantime, the author suggests steps that could help in the recovery process.

The author of this paper has found through her research that the solution to avoiding corruption is not only in additional regulations, but to have a greater respect and order for the existing rules. Experts say that the complexity of the existing regulations made it easy to play financial games in the first place. Additionally, recent fraud has violated laws that were already in place. Perhaps the corporate system needs greater "watchdogs" and independent advisory boards to watch over the company assuring investors that there is a movement to uphold and maintain ethical standards. Currently the Financial Accounting Standards Board has addressed the issue of how to treat off-the-book partnerships made infamous by Enron Corp. and is now tackling the question of whether companies should count stock options as expenses.

A major overhaul of corporate governance is in order. Companies should separate the roles of chairman of the board and chief executive, and give the chairman post to an independent director. This move would promote a major shift in the balance of power, which is a strong move toward shaking up the system. An independent director has nothing to lose and nothing to gain from decisions and practices. The person in this position will most likely have the best interest of the investor in mind. Also a company's corporate governance should not have interlocking relationships. For example, the Chief Executive Officer of company A should not sit on company B's board and vice versa. Such roles might cause conflicts of interest.
Corporate leaders and boards should go public acknowledging the inappropriate actions of numerous corporations and indicate that this is not normal. CEOs like former CEO of Chrysler during the 1980s, Lee Iacocca, who will assure the public that not all company’s and Chief Executive Officers are greedy and this is an unfortunate time that the corporate system will overcome successfully. Leaders should rally for a reasonable set of reforms that will help prevent such abuses in the future. Investors need to know that beating corruption is on the top of the company’s agenda.

Research shows that good companies are run with leadership principles and good governance. The best interest of the investor should be first and foremost. Company boards should publish its principles of corporate governance for all its shareholders and employees, perhaps in the annual report. The board should make an annual report to shareholders about how it adhered to and strengthened these principles. Shareholders should also be given the opportunity to suggest changes to the company’s governance system. The compensation packages of top management should also be included and explained in the annual report.

Chief Executive Officers must share more information with the corporate boards before meetings so they have time to fully understand and digest the issues of discussion. Chief Executive Officers should encourage directors to take on-site visits. Attendance should be mandatory at year-end meetings.

Chief Executive Officers and Chief Financial Officers should sign a document committing themselves to transparency and integrity. This tactic would be an extension of “Oath Day”, the August 14, 2002 deadline after which chief executives and chief financial officers of the largest U.S. companies had to swear to the truth of their quarterly accounts. Compensation packages have been a big part of the scandal. The author suggests that the Chief Executive Officer is no longer an active part (along with the board) in setting compensation for the company’s top management. Such involvement invites pressure to over-perform.
At the core of the scandals, lies the abuse of stock options. Senior executives should not be given a large portfolio of stock options because it brings extreme pressure making them feel they need to over-perform to keep shareholders happy and even keep their jobs. The author agrees with the proposal that stock options should be treated as an expense. The fact that options value is not subtracted from profits has led corporations to give loads of options to reward Chief Executive Officers who make huge profits when the stock rises but lose nothing when it falls.

Companies need to concentrate more on building leaders from entry level to top management. The author recommends that companies invest more time and money in training existing employees instead of hiring outside the company. To rebuild investor trust it is imperative that boards move away from offering excessive perks to prospective executives. It does not make sense to go above and beyond to recruit a stranger of the company and assume that he/she would have the best interest of the company at heart, never mind the best interest of its investors.

Companies need to re-examine their policies and enforce self-regulation. Some corporate makeovers may require hiring a team of experts to restructure the company. For example, WorldCom hired a former attorney general to restore the company’s credibility and consult on finances after declaring bankruptcy protection. Some manager’s need coaches to reform leadership. Management coaching is a new niche across industry since the influx of scandals.

Technology should promote information sharing on a global level. Such as the new proposal by financier George Soros called “Publish What You Pay,” which urges natural resource companies to make public what they pay to governments through technologic resources. This would make it harder for politicians and government officials to divert resources from government treasuries helping foster trust in companies that participate.
Whistleblowers should be awarded not condemned. Companies should encourage honesty and integrity in the organizations and perhaps less unethical behavior will occur. The letter of Enron whistleblower Sherron Watkins to chairman Kenneth Lay in August 2002 warned of accounting scandals but Ms. Watkins was asked to leave the company a few months later. Employees willing to take a risk and confront upper management on wrongdoings should be encouraged and protected by the company. However, according to a survey by the nonprofit National Whistleblower Center in Washington, “most employees who expose workplace wrongdoing face some form of retaliation, and many still lack the legal right to protect themselves.”

Off-balance sheet financial engineering became the key to boosting stock pricing and earnings. Imaginative “pro forma” numbers tailored to companies needs rather than based on objective numbers are still around. The only movement by accounting firms that resembles reform is the unloading of their consulting business. If the Big Four accounting firms ease up on lobbying against strengthening regulations maybe the public will forget about the tax shelters fiasco and they’re promoting of moving headquarters to places like Bermuda to avoid U.S. taxes on U.S. income. The author suggests that the Big Four (PricewaterhouseCoopers, KPMG, Ernst & Young and Deloitte & Touche) use their power to speak out on their support of strengthening existing reforms. Also, the author recommends the rotation of auditors. There was a proposal to rotate auditors off accounts every 5-7 years and the big four are very much against this idea. The author believes that changing the auditors will alleviate the pressure for auditors to feel a certain loyalty to a sign-off on the books of a long-time client.

In February 2003, Deloitte & Touche announced that the accounting firm would not separate from its consulting services, citing a tight credit market and an uncertain economic climate. Pressure to divide consulting operations from auditing functions became intense in the wake of the Enron scandal, as critics focused on the way Arthur Andersen provided both types of services to the disgraced energy trader. The consulting division of the now-defunct Andersen became Accenture; KPMG's consulting unit became BearingPoint in 2002; Ernst & Young's consulting arm was sold to Cap Gemini;
and PricewaterhouseCoopers sold its consulting wing to IBM. Several of Deloitte’s top-tier clients have dropped some of the firm’s services in an effort to abide by the Sarbanes-Oxley Act. The measure, passed overwhelmingly by Congress last year, bars auditors from providing nine different consulting services, including bookkeeping, information systems and internal auditing, to their clients.

In a post-Enron environment, there is no excuse for companies to allow unethical behavior to go unchecked. Companies should hold mandatory corporate ethics and integrity training programs or seminars. Such programs can take as long as 15 minutes and delivered firmwide through email. As long as preventative steps are taken internally to keep employees honest the company can’t be held as accountable if there is misdeed for it made attempts to take preventative steps against unethical behavior.

In house general counsel must play a more active role in preventing unethical behavior. It is a violation of a lawyer’s ethical responsibilities and duties to ignore corporate misconduct. With that said, as of January 2003, after Congress required the SEC to reform corporate lawyers, lawyers are now required to report material evidence of securities fraud to the chief executive or chief legal officer.

The company’s general counsel needs to accept more responsibility in educating the board as to whom they should turn to if a crisis hits. It’s technically their job to hand-deliver these experts to the board. The general counsel needs to be upfront and honest with the company’s leaders. Nancy Temple, in-house Arthur Andersen lawyer, who advised David Duncan, the auditor on the Enron account, to destroy all Enron-related documents is not a role model for corporate legal advisors.

Crisis communication teams should have a response plan in place in the event of a crisis. A company’s ultimate goal in a crisis situation should be to protect the brand. Companies should not delay and cover-up negative situations. The response is all about sustaining the company’s long-term image rather than winning short-term legal or financial victories.
There are many people to blame for recent corporate scandals- auditors, Chief Executive Officers, the SEC, lawyers. However, the author believes that the media has reported on scandals in a bias fashion. All media outlets: print, television, and virtual, can play a part in helping big business win back investor confidence. The media can concentrate on the corporate leaders and boards making changes and commitments. More time should be spent reporting on the strengthening of regulations assuring investors that the country is moving toward resolve. Too much time has been spent reporting the misconduct and greed of a handful of executives and not reporting the fact that while the worst abuses were limited to a few companies there were widespread examples of companies exaggerating their numbers and explain why and what is going to be done about it.

In July 2002, President Bush recommended a 10-point plan to restore faith in the integrity of American business that included new laws, enhanced regulations and several suggestions that I feel should be incorporated into the procedures of public companies. He suggested a maximum prison sentence for mail and wire fraud that is often used to prosecute financial fraud, be doubled to ten years. Corporate executives should get larger prison sentences after being charged with fraud. He also encouraged greater security and prevention by the Justice Department. The author agrees that examples need to be made of the corruptors today in an effort to avoid similar scandals in the future.

One year after Bush's investor confidence restoration plan the former chief executive of Enron and WorldCom, who have been the symbols of corporate corruption have yet to be prosecuted. However, the new emphasis by the Justice Department to play a larger role in fraud cases has encouraged the investigation of other big cases, currently undisclosed as of April 2003. With the new advisory board and Sarbanes/Oxley, cases are investigated quicker. “The SEC -- which in the 1990's had a difficult time persuading prosecutors outside Manhattan, Brooklyn and San Francisco to follow up on its referrals of potential fraud cases -- is now working with prosecutors in offices across the country.” (The New York Times, A
U.S. Push on Accounting Fraud, April 9, 2003) When there are accusations of serious fraud at companies based in states where prosecutors lack experience in accounting investigations, the Justice Department is sending specialists from Washington to help them.

It is apparent that there is a greater movement today toward preventing corporate corruption than there was in the 90s. Perhaps because there were so many scandals this year; or there is more news outlets to report on the scandals; or layoffs and employee losses were so great. Whatever the reason, in time, these actions should bring results and reincarnates a trustworthy corporate America.
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