

Curbing Corporate Scandals for Global Business Success

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Abstract

This research looked at accounting standard and how it helped to address ethical issues within four selected Companies: WorldCom, Adelphia, Enron, and Tyco. Accounting Standard are rules and regulations that were set by accounting bodies to regulate financial transaction and accounting statement within an organizations. These standards helps the organization to operate with integrity, honesty, fairness, concise and ethically. Our findings showed that Enron, Tyco, Adelphia and WorldCom were caught going contrary to these accounting rules with understatement of company's expenses that leads to overstatement of company's net income to look good for investors and misappropriation of company's funds by CEO's and CFO's.

Key words: Ethics, scandals, performance, Reputation, Credibility

Introduction

In accounting, ethics are the important aspect in the profession. The organization, government and individual who used accountants to prepare their financial statement depend highly on them to make an effective decision on their financial statement. Therefore they expect these accountants to be highly competent, reliable, ethical and objective. Also the accountant should be qualified by possessing a high degree of professional integrity and have good reputation by indulging in a highly ethical standard in terms of decision making. This code of ethics helps to maintain a level of self-discipline that is very effective and regulation within the organization (Thomas, 2008).

There are several professional organizational standards accountants have to abide by, In America these include the code of professional conduct of American institute of CPAs (AICPA), The National Professional Association for CPA, has an ethical standard for its members, these standards or general guideline that professionals have to abide to perform their duties with professionalism. Especially in the field of medicine and accounting they have to be responsible for their clients and the public, therefore they have to accept and apply the code of ethical standard within their bodies so that there will be integrity and objectivity of what they do. Maintaining integrity and objectivity within an organization will avoid conflict of interest and create reputation which most organization needs from their professionals. In accounting profession, there are a lot of bodies who oversees that the accounting and ethics standard are undertaken by their professional to show competence, confidentiality, integrity and objectivity. In America, we have the CPAB, SEC, AICPA, IMA and others (McNamara, 2008).

Purpose of the research

This research investigated ethical issues within four selected companies and how these ethics affected the company's performance

Hypothesis statement

Alternative hypothesis

1. A company expenses will not affect the performance outlook

Research Question

- 1) How will one determine if ethical issues exist within a company?

Literature Review

A national system was developed during the Second World War about the regulation of the content of the company accounts. In most countries these regulations had been the responsibilities of the government, setting out specific legal rules and regulations to governing company accounts mostly under the company law. In France and some other part of Europe they have a codification plan; General Accounting Plan (GAP). While in other countries, professional Accounting bodies take upon themselves to create a good practice of accounting standards. In these countries companies looking for rights to trade on stock exchange, influence accounting norms and based their standard on the general accounting standard (Brooks Dunn, 2010).

Accounting standard had been founded in the United State where US Securities and Exchange Commission (SEC) had rules and regulations for over 12000 companies in the America capital market. SEC created delegates to take the task of setting accounting standard for companies in the United State and called it Financial Accounting Standard Board (FASB). FASB came out with 140 statement of financial accounting standard which are generally accepted in US Generally Accepted Accounting Principle (US GAAP). SEC wanted the European Committee to accept this principle in their accounting standard or to reconcile them. But when the need for international business came, international organization also created its own standards of commercial conduct (Brooks Dunn, 2010). In 1973, nine countries accounting bodies with 2000 members in more than 100 countries came with standards, International Accounting Standards Committee (IASC). The IASC came out with 40 International Accounting Standards (IAS) and some 20 standard interpretations to assist with compliance with IAS. IASC become very influential in consolidated financial accounts and the original standard on consolidate financial statement, and made contribution to the formulation of the European Union seventh Accounting Directive (Aldridge, 2005). In the global standard, there are also several and accounting ethics standard- actually there are not one acceptable accounting and ethics standard due to cultural relativism. The IASC was the first standard of accounting and ethic standard that was prepared to guide accounting practices in Europe and other countries. Since 2005 the IACS was one of the accounting standards prepare in accounting for the International Accounting Standard Board (IASB) and its international financing reporting standard had been used in over thousands of companies in the global level. The standard of the IASB are connected with the historical standards which were adopted by the historical standards, IASC, have standard that influence and enforce in financial reporting of today's business and accounting profession(Thomas,2008). The standard of IASC from 1973 to 2000, including its foundation was used to develop the standard and restructuring of the IASB in 2001. IASC standard have a very impact on national standard setting and accounting practice to develop the accounting standard of a particular, government, individual and the company. IASC standard also have influenced the policies of the United Nation (UN), the OECD and the US Securities and Exchange Commission (SEC), The International Organization of Securities Commission and the European Commission. The IASC standard for ethics and accounting had been a great concern to accountants in the global environment, which is used in academics, policy making and being professional (Thomas, 2008).

For ethical standard, ISAC standard review that any accounting bodies who want to use the US, GAAP and their standards should have a permit and the standard should use the

international accounting standard (IAS). Cash flow; accept IAS22, business combination which narrate the accounting for the business and also the use of the IAS21 the effects of changes in foreign exchange rate to check the hyperinflationary economy. The ISAC, establish a higher or lower disclosure standards for foreign companies then for domestic companies when reconcile with the US GAAP. Since accounting standards in the global environment is convergence and financial reporting in the convergence standard are very difficult. IASC have standards that are very transparent, since their reporting are more for the worldwide. Using IASC standard for your financial statement with reconciliation with US GAAP is like not following the accounting standard. To provide a comprehensive body of accounting principle, IASC had to prepare a plan to identify the issues address by IOSCO about their core standard work program. The IOSCO endorse the ISAC standard, because large, multinational companies used their code of standard (Katz, 2000).

In the IASC standards there major issues in which a criteria have to setup to check if these standards: is generally accepted as basis of accounting; are of high quality; and can be ruinously interpreted and applied. IASC standard being copyrighted by IASC and having copy in the public reference room and placing it on website seem to be unethical to the publishers. The IASC standards have to be determine either it has high quality accounting standard checking if the standard relevant, reliable information that are very useful to the stakeholders, investors, lenders, creditors and the others who make decision (Katz, 2000). For the standard of IASC be standard it should result in consistency, it must provide transparency, provide a full disclosure, information including all the basic of the financial statement to understanding the accounting practices applied, then IASC standard should be consistent underlying accounting conceptual framework; result a comparable accounting by showing similar transaction and avoiding or minimizing alternative accounting treatments, require consistent accounting policies from one period to the next and finally be clear and unambiguous (Katz, 2000). IASC standard develop strategies to address issue that were determined by the preparers, auditors and the users of the financial statement and then benefited from the standard and the improvement over the US Accounting practices.

The issue of the IASC standard will produce the same level of transparency and comparability that provide by the US investor under the standard of US GAAP. For political, cultural, financial and economic reasons over the years most foreign companies have to make a decision either to use the US securities or use the IASC which most of the regulatory requirements. But sometimes, most of the foreign companies feel reluctance to adopt US accounting, since they think they have forgone standard that they didn't contribute to the formation. They rather have to adopt IACS accounting without requiring the reconcile to US GAAP. And also litigation exposure and certain public disclosure deter the foreign companies in the US market for them to use their standard (Katz, 2000).

Assessment of the IASC standard, after studying the issues of the IASC from IOSCO identified the necessary components of the core standards. IASC was advice to prepare core standard work program, IOSCO, have to adopt this core standards of the IASC for IOSCO'S technical committee have to recommend the endorsement of the IASC standards. For the assessment they requested that the IASC standard; constitute a comprehensive, generally basis of accounting, are of high quality and finally it can be rigorously interpreted and applied to accounting standards (Katz, 2000). IOSCO, identified the work of the IASC, addressing the core standard and pointing the issues of IASC in their standard about industry specific accounting principles and the difference between the ISAC standard and USGAAP are very significant, the only challenge

between this two standard, the financial position and operating result are difficult to compare the result of the US GAAP and the IASC. Another issues that we have to think about is that if the IASC standard are highly quality financial reporting standard. Since accounting standard have to satisfy its objective, the prepares have to recognize the responsibility and they requirements of the standard, the standard have to be very intent and ethical for the auditors and regulators around the world would be able to read , interpret ate and apply the standard. From, this point it is very difficult to access and evaluate the effectiveness of the IASC standard (Katz, 2000).

Since there are little direct use of the ISAC standard and it is use directly in the required market. IASC standard in the financial statement do not reflect the improvement by the IASC in the core standard project. For the IASC standard to be rigorously interpreted it needs a sufficient level of implementation guidance. The IASC standard is always lacking a vigorous implementation comparing to the US GAAP. IASC formulate its standard using bold (black) lettering to emphasize basic standards while placing explanatory text in normal (gray lettering but their requirement are not limited to black lettered. The black and grey chosen of color in IASC standard are very significant and should be regarded as very necessary. Comparing the IASC to the US GAAP, The IASC published only two of its standard promote consist tent understanding of the GAAP standard (Katz, 2000).

Financial reporting should be very effective, since it provide a comprehensive body of accounting principles. Therefore it needs a rigorous and consistent accounting standards, auditors and regulators. Since there is a concern that the IASC standard are not very vigorous and auditors failed to identify properly, lack of compliance IASC requirement in reports on an issuer's financial statement. In this circumstance the SEC required adjustment to the financial statement in order to use IASC standard. In 1997 IASC formed standing interpretation committee (SIC) to provide a resolution interpretive issue arising in the application of the IASC standard that received divergent or unacceptable treatment in the absence of authoritative guidance of the IASC (Katz2000). The IASC, to be used effectively as an accounting standard, the board have to restructure the IASC standard and having an effective high quality the IASC, standard have to characterized by an independent decision making body, an active advisory function, a sound process, an effective interpretive function, independent oversight representing the public interest and finally have adequate funding and staffing to implement the standard very effectively. The role of the auditors and the regulators are very important in the organization, in which the accounting and ethical standard have to be very effective, therefore the IASC standards have to be accepted and apply to company accounting standards. The board has to identify a way to stop the diverging interpretation of IASC standard (Katz, 2000).

For reorganization of the IASC standard, the standard will depend on the current assessment work and it was on two aspects considering the quality of each of the IASC standard individually and evaluating whether the body of the standard operates effectively as a whole. Since the goal of the IASC with the core standard was to develop high quality set of generally accepted international accounting standard that will eliminate reconciliation to national standard for commission action to take any form by maintaining current reconciliation requirements, removing reconciliation standard in IASC standard and adding IASC standard as warranted based future review standard, relying on the IASC standard for recognition and measurement principles and finally accepting financial statement prepared and interpreted with the accordance with the IASC standard without requirement to reconcile with the US GAAP(Katz,2000).

In conclusion, the business and accounting profession had been changed through this modern age. With the series of the fraud in the accounting profession through Enron, WorldCom

and others and the fiasco of the subprime mortgage system, there have been a reform accountability and governance on our cooperate and professional accounting. This reform by the government, introducing the Sarbanes-Oxley Act 2002 to governance the fraud situation and also making sure that the professional ethics are influenced to bring challenges and opportunities for directors, professional accountants and executives. These reforms also had brought the standard in accounting and its ethics. It has Make Corporation and professional accountants more accountable of their ethical behavior to their stakeholders; investors, shareholders, employees and the community as a whole. (Brooks& Dunn, 2010)

Methodology

Data collection and analysis

This research used secondary data especially the income statement, and decision made by management to analyze ethical issues that affected multimillion companies within the United State such as WorldCom, Tyco, Adelphia, and Enron.

With the case of WorldCom, 1999 to 2002 financial statement data were collected from the 10k annual financial statement. For Enron, data collections were from 1996 to 2000 10k annual financial statement. Under WorldCom, the Company was involved in a “3.8billion dollar underestimating of their expenses and against their revenue, as a result, this goes to give the company a high overstated profit that looks good in the face of their investors. However, this practice does not follow the standard of accounting procedure which stated that expenses should be subtracted from revenue. Though WorldCom accountants should have identified the problem, they were the same people looking into the accounting issues with Adelphia, Tyco and Enron which fall under the same ethical issues and were therefore being accused of withholding information (SEC, 2002).With the case of Tyco and Enron it was not different of understatement of expenses and overstatement of net income.

Table 1 Source: Tyco International Inc.

| Income statement in (millions) | Year 2002 | Year 2001 | Year 2000 | Common size percentage | | |
|--------------------------------|-------------|-----------|------------|------------------------|-------|-------|
| | | | | 2002 | 2001 | 2000 |
| Total Revenue | \$35,589.80 | 34,002.10 | 28,927.50 | 100 | 100 | 100 |
| Cost of Revenue | 23,065.30 | 20,935.60 | 17,954.50 | 64.81 | 61.57 | 62.07 |
| Gross profit | 12,524.50 | 13,066.50 | 10,973.00 | 35.19 | 38.43 | 37.93 |
| Selling & administrative | 8,181.60 | 6,745.30 | 5,500.70 | 23.00 | 19.84 | 19.02 |
| Depreciation & Amortization | - | - | - | - | - | - |
| R&D | - | - | - | - | - | - |
| Restructuring | 5,795.30 | 704.80 | 274.30 | 1.63 | 2.07 | 0.95 |
| Other expenses/income | - | - | - | - | - | - |
| Special items | - | - | - | - | - | - |
| Operating income/loss | (1,452.40) | 5,616.40 | 5,198.00 | -4.08 | 16.52 | 17.97 |
| Interest expense | 1,077.00 | 904.80 | 844.80 | 3.03 | 2.66 | 2.92 |
| Interest income | 117.30 | 128.30 | 75.20 | 0.33 | 0.38 | 0.26 |
| Net interest exp/income | 959.70 | 776.50 | 769.60 | 2.70 | 2.28 | 2.66 |
| Loss/gain on | - | - | - | -- | - | - |
| Financing activities | - | (24.50) | (1,760.00) | - | -0.07 | -6.08 |
| Other loss/income | 216.00 | (250.30) | 0.30 | 0.61 | -0.74 | 0.001 |
| Total cost/expense | (2,628.10) | 5,114.70 | 6,188.10 | 107.40 | 84.96 | 78.61 |
| Income/Loss BIT | (2,628.10) | 5,114.70 | 6,188.10 | -7.38 | 15.04 | 21.39 |
| Income tax exp/benefit | (208.10) | 1,172.30 | 1,850.90 | -0.58 | 3.45 | 6.40 |
| Income tax after income taxes | (2,836.80) | 3,942.40 | 4,337.20 | -7.97 | 11.59 | 14.99 |
| Income/loss from operation | (283.20) | 3,894.90 | 4,318.50 | 0.80 | 11.45 | 14.93 |
| Net income/loss | (9,179.50) | 3,464.00 | 4,318.5 | -25.80 | 10.19 | 14.93 |

Table 2: Enron Financial Statement

| Enron Financial Report (in millions) | 2000 | 1999 | 1998 | 1997 | 1996 |
|--|-----------|----------|----------|----------|----------|
| Revenues | \$100,789 | \$40,112 | \$31,260 | \$20,273 | \$13,289 |
| Net income | | | | | |
| Operating Results | 1,266 | 957 | 698 | 515 | 493 |
| Item impacting comparability | (287) | (64) | 5 | (410) | 91 |
| Total | 979 | 893 | 703 | 105 | 584 |
| Dividends paid per common share | 0.50 | 0.50 | 0.48 | 0.46 | 0.43 |
| Total Assets | 65,503 | 33,381 | 29,350 | 22,552 | 16,137 |
| Cash from operating activities excluding working capital | 3,010 | 2,228 | 1,873 | 276 | 742 |
| Capital expenditure & Equity investment | 3,314 | 3,085 | 3,564 | 2,092 | 1,483 |

Source: Enron Annual Report

Table 3: WorldCom Financial Statement

| WorldCom Financial Statement (in millions) | 1999 | 2000 | 2001 | 2002 | Total |
|--|-------|-------|-------|------|-------|
| Revenue | \$205 | \$328 | \$358 | \$67 | \$958 |
| Line Cost | 598 | 2,870 | 3,063 | 798 | 7,329 |
| SG&A Expenses | 46 | 283 | 181 | 25 | 535 |
| Other | 89 | 393 | (4) | (50) | 428 |
| Total | 938 | 3,874 | 3,598 | 840 | 9,250 |

Source: SEC.Gov

Hypothesis analysis

From the findings above, it was clear that expenses has an effect on a company's performance; a high expenses may lead to a low net income and vice visa, for the case of Tyco International in table 1, the Company had a 3.24% more in expenses in 2002 than in 2001 and 2.74% in 2002 than in 2000, as a result, there was a huge loss in net income in 2002.

Recommendations:

- 1) For effective and less scandal business environment, CEO's, CFO's and other leaders need to be reminded all the time of their responsibilities not left their fate of holding a certificate
- 2) Routine checks on performance should be conducted and not only at the time of suspicious activities

Conclusion

From all the four companies, our findings showed that WorldCom financial personnel had wrongly transferred \$3.852billion from line cost expenses to asset account in 2001 and the first quarter of 2002. It was also found that from 1999 to 2002, WorldCom improperly reduced its line cost by \$7billion. WorldCom company performance was on the decline however, management insisted it was doing great; this was due to the fact that the company had also used general accrual account to accumulate excess accruals that could later be used to offset expenses for the benefit of the company. For the case of Tyco, certain actions by the CEO and CFO were contrary to accounting standard, these included but not

limited to relocating employees to certain places without board approval, and using the relocation to receive non-qualifying loans and unauthorized benefits. We conclude that unethical methods and behavior may have benefits for the short term, but the long term has a consequential effect on the company and management of those companies including job losses, companies filing for bankruptcy and fines.

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