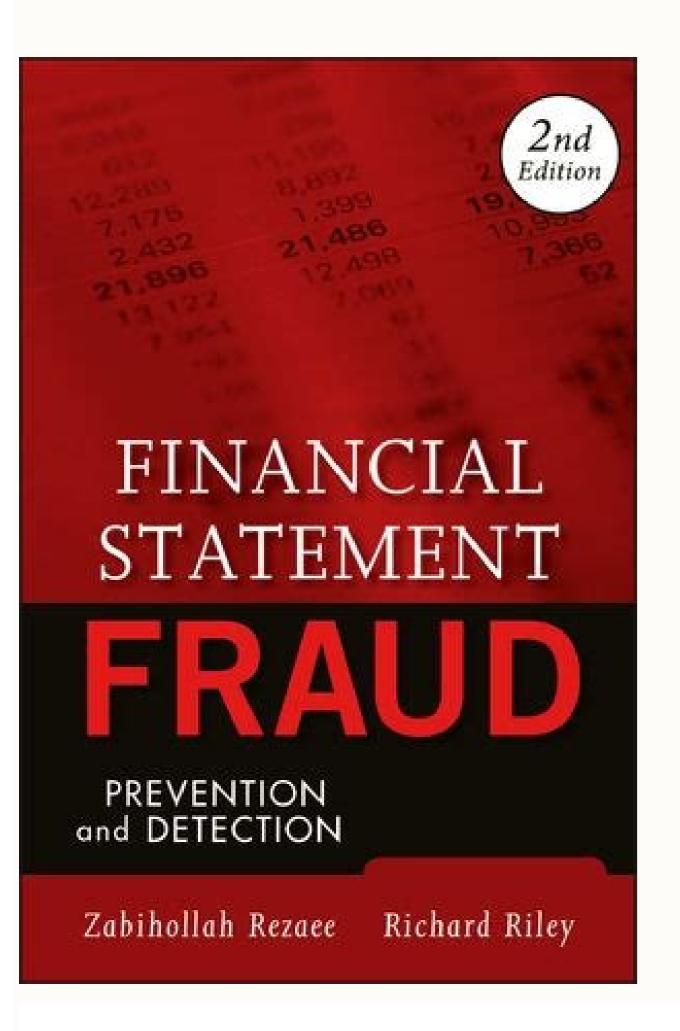
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BUSINESS ETHICS, FRAUD AND FRAUD DETECTION

CHAPTER 12

ETHICAL ISSUES IN BUSINESS

Ethical standards are derived from societal mores and deep-rooted personal beliefs about issues of right and wrong that are not universally agreed upon

CONTACT DETAILS

MS Word, Writing Skills, Organizational Skills, Problem Solving.

LANGUAGES English (Native) French (Professional) Spanish (Professional)

REFERENCES

Reference - 1 (Company Name) Reference - 2 (Company Name)

SKILLS



Robert Smith Fraud Detection Analyst

Seeking around Detection Analyst position with an outstanding career

opportunity that will offer a rewarding work environment along with a winning team that will fully utilize management skills. WORK EXPERIENCE

Fraud Detection Analyst ABC Corporation - October 2007 - January 2009

- Analyzed and identified daily fraud trends. Analyzed credit card transactions to uncover potential fraudulent use of credit cards.

 - Utilized system tools to improve the best judgmental decisions.
- INTERESTS · Evaluated risk to client relationships and work directly with the client to resolve problems. Communicated best-demonstrated practices to peers by preparing side Contributed ideas toward the monthly team contests to increase team
- Assisted with weekly team meetings, reviewing and informing important departmental updates with the team. Maintained a high level of ethical conduct handling customers personal

Fraud Detection Analyst Delta Corporation - 2010 - 2012 Made decisions based on good judgment, research, and problem solving

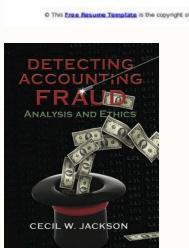
performance levels.

- · Coached and educated other associates on researching complex fraud
- . Handled inbound calls for the Customer Protection Team. · Conducted a thorough verification process through investigation and
- Ensured the orders that were received for new equipment were legitimate.

 Monitored customer credit and debit accounts for fraud activity Contacted cardholders to verify suspicious activity Analyzed fraud
- Education

High School Diploma

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. Los Angeles Times. As long as the publicly traded stock price of LDDS increased, there would be no end to the number of acquisitions it could make. In June 2013, a deal was made in which Skilling's sentence was reduced by ten years: "Under the deal, more than \$40 million of Skilling's fortune, which has been frozen since his conviction in 2006, will be distributed to victims of Enron's collapse" (Hays & Driver, 2013). Exhibit 7.2 provides a diagram of the LJM1 structure. Generally, equity investments in companies fall into one of three categories: 1. To bump up the numbers even further, apparently Adelphia also added cable subscribers from other Rigas Entities and even included long-

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distance telephone subscribers as basic cable subscribers. An editorial in Information Society Trends blamed the U.S. stock markets for "enabling a second-rank company such as WorldCom to become a global giant in a matter of a few years" (qtd. Foot, Phillipa, 52 Forbes, Walter, 126, 129 Foreign Corrupt Practices Act (FCPA), 300-302 Foreign Corrupt Practices and Information Society Trends blamed the U.S. stock markets for "enabling a second-rank company such as WorldCom to become a global giant in a matter of a few years" (qtd. Foot, Phillipa, 52 Forbes, Walter, 126, 129 Foreign Corrupt Practices Act (FCPA), 300-302 Foreign Corrupt Practices Act (FCPA), 300-3
payments, improper accounting of, 300-302 FR (final rule) Franchise acquisition rights, 304 Franchises, 304-305 Franklin, Benjamin, 52 Fraud, 26 See also Accounting fraud Freddie Mac (Federal Home Mortgage Corporation), 38, 327-328 Fuld, Richard, 334 Futures market, 232 An exchange where parties can trade futures contracts-financial
instruments in which parties agree to buy or sell quantities of a commodity at a specified price on a specified future date. In Lockheed's case, press articles pointing toward the losses of the TriStar program were abundant, and the capitalization of significant development costs for the program were clearly indicated on the balance sheet and in notes
to the financial statements. With Franks's recommendation, LDDS had 200 customers soon after opening. online.wsj.com Smith, Rebecca, and John R. John Kenneth Galbraith's description of the Great Crash of 1929 is equally true of what happened on Wall Street in 2008. 17, 18). Unfortunately, Enron's accounting fraud was just one more case in an
all-too- frequent litary of falsified financial reports that had grown in incidence over the 1990s and into the people at Pearson for their various and invaluable contributions to this project: to Sari Orlansky for initiating the venture; to Stephanie Wall
for bringing me on board; to Donna Battista for her guidance; to Lacey Vitetta, Nicole Sam, Liz Napolitano, and Christine Donovan, thank you for successfully and expertly steering the project through the complex publication process. During the year ended December 31, 2007, the Company recorded $653 of system sales revenue and $287 of gross
margin on this transaction under the percentage-of-completion method of revenue recognition. The unrelenting pace of these acquisitions caused the company to constantly redefine itself and its focus" (First Interim Report, 2002, p. Without sufficient consideration for the relevant accounting rules, Stanaway and McIntosh typically then directed R&Q
to add certain "below-the-line" items to the warranty reserve calculation process because they thought these items would reflect potential reductions that the Company hoped to achieve in future warranty costs. Regrettably, the oversight division lacked the weapons to protect its domain. 10. Large amounts allocated to goodwill on the acquisition of
other companies, accompanied by the creation of large reserves on acquisition. Dr. Jackson developed Leventhal's highly regarded course on "Detecting Fraudulent Financial Reporting (2006) received favorable reviews from publications such as
Barrons, The CPA Journal, Investor's Business Daily, the Motley Fool, and The Accounting Review. What about children's rights to be supported by their parents? AHERF should have increased that reserve by $40 million and recognized the expense of $40 million in the income statement. Securities and Exchange Commission Accounting and Auditing
Enforcement Release, April 19, 2005. di Florio Director, Office of Compliance Inspections and Examinations* National Society of Compliance Professionals October 22, 2012 Effective Practices for Managing Conflicts of Interest**. Furthermore, as scrutiny of the Enron failure showed, independent auditors would frequently leave the auditing
profession and join the staff of a company that they had audited. Respondent shall cooperate fully with the Commission in any and all investigations, litigations or other proceedings relating to or arising from the matters described in this Order. He may have overdone the gentility, however, for Sunbeam at this stage had many strong personalities
pulling in opposite directions. WorldCom already controlled half of all the domestic Internet traffic through UUNet and commanded a stunning investment in bandwidth through the IDB, WilTel, and MFS acquisitions. (ATC). He is now reportedly a "document review clerk" at the Houston law firm that worked his civil cases (Partington, 2012). The
duties of the external auditors regarding the system of internal control were not well specified. After McGowan's gradual retreat from the company lost some of its focus and discipline. Therefore, the conspirators discussed a scheme to hide WorldCom's increasing
expenses by causing substantial portions of WorldCom's line costs to be transferred from current expense accounts into capital expenditure accounts into capital expenditure accounts. In 1965, he was transferred to Kimberly-Clark's plant in Wisconsin. (a) Accounts receivable increases as a percentage of sales. Inside Job. For a some quarters during the time of Sunbeam's bill and
hold sales and heavily discounted sales, it reported positive operating income but negative CFFO. Based upon the terms of the written agreements, the outside auditor agreed that the transactions qualified for sale-leaseback accounting. Sometimes companies abuse this procedure, and the SOX Report (SEC Report Pursuant to the Sarbanes-Oxley Act
2002) described the abuse or improper use as follows: Reserves may be improperly used to manage earnings. Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet service provider and Enron had purchased 5.4 million shares of Rhythms was an Internet se
should have done. His main mistake, he said, was ignoring the principles behind the rules he creatively circumvented. 059402 01 ch7 p226-291.indd 245 7/7/14 9:08 AM 246 Chapter 7 • Enron and the Tale of the Golden Goose However, this Commission was largely ineffective; it lacked subpoen power, and its weak efforts did not uncover the
scams. (b) Decreasing the prepaid asset amount on the balance sheet. Kind of difficult, I'll tell you that." Eventually, Noonan told the government what he knew. Edison was listed on NASDAQ in November 1999. • September 26, 1997. Greasy Patties Corporation, a hamburger chain, has 100 stores. Also as a result of the conduct described above,
 Beazer violated Section 13(a) of the Exchange Act and Rules 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security registered pursuant to Section 12 of the Exchange Act, which require that every issuer of a security register of the Exchange Act, which require that every issuer of the Exchange Act and th
and mandate that periodic reports contain further material information as may be necessary to make the required statements not misleading. Explain how Enron used the "Prepay Transactions" to overstate CFFO. Improper Valuation of Assets WORLDCOM (continued) * Table 1.1 was updated in 2013. 23. An Andersen spokesperson said that Stupka's
division did not need the reserve of $400 million. Specifically, Beazer falsely stated its net income in certain periods in various Commission filings and other investor disclosures. Sunbeam captured extra revenue by extending its quarter-end date by two days. Basin Water Inc. (b) Decreased total liabilities and reserves. This might explain why Adelphia
did not restrict itself to misleading financial information, but misrepresented its performance in non-GAAP financial measures as well. 104) 3. (Quotes from AAER 1393, 2001). In his analysis of Ebbers's relationship with SSB, the Bankruptcy Examiner stated: The Examiner believes that Mr. Ebbers breached his fiduciary duties of loyalty and good faith
by putting his personal interest ahead of those of the Company. Case No. CV11-05316 R(AGRX). Third and Final Report of Dick Thornburgh, Bankruptcy Court Examiner. "A Brief History of Fannie Mae and Freddie Mac," Time. Scheme #3: Slow Shipping Requests Another tactic Sensormatic allegedly used to accelerate its revenue recognition was
what is called "slow shipping," or requesting the shipping company to delay the shipping company
when I went to them," he mused. However, by May 7, 2004, the stock price had dropped to $22.51 per share and kept sliding. 101 b. Signal #3: Decrease in a Company's Asset-Turnover Ratio When a company's asset-turnover ratio declines, either for a category of assets or for total assets, it is an indication that the assets may be impaired. No
question about it," he admitted. He persuaded Lay and Skilling to convince the board of directors to appoint him as general partner of LJM1. What is Saturn's cash flow from operations (CFFO) for the year? Signals of Insignia's Fictitious Reporting Scheme of Failing to Value Revenue Properly Since overstatement of revenue via failing to provide
 adequate allowances for returns leads to accounts receivable that do not get realized in the form of cash, the first two signals that follow are the same as the major signals for the overstatements of revenue 9 Insignia consented to the order without admitting or denying the findings. McLean, Bethany, and Joe Nocera. (Note: KPMG strongly defended
its audit work at Xerox.) Scheme #3: Improper Disclosure of Sales of Leases Xerox also sold approximately $400 million of its existing leases. On December 31, 2012, Bronto paid SPOCK1 the $1,000 for the put option. Quality and track record of company leaders should be combined with an analysis of whether the business plan outlined by
management is likely to produce the reported results in the published. For this reason, many cases of accounting fraud are tried in civil court or result in civil actions such as SEC enforcement actions.
Also, the inventory of a bill and hold sale must build up somewhere—either at the seller's or the buyer's warehouses. www.justice.gov. March 24, 2005. The start-up costs could be appropriately deferred only if the Company had received from the Automaker a written guarantee of specific reimbursement. 059402_01_ch3_p069-116.indd 101 7/7/14
9:01 AM 102 Chapter 3 • The Sizzling Saga of Sunbeam Accounting and Auditing Enforcement Release (AAER 2884) for Beazer Homes 7 UNITED STATES OF AMERICA Before the SECURITIES EXCHANGE ACT OF 1934 Release No. 8960 / September 24, 2008 SECURITIES EXCHANGE ACT OF 1934 Release No.
58633 / September 24, 2008 ACCOUNTING AND AUDITING ENFORCEMENT Release No. 2884 / September 24, 2008 ADMINISTRATIVE PROCEEDING File No. 3-13234 In the Matter of BEAZER HOMES USA, INC., Respondent. During this period, Navistar booked 35 rebates and related receivables from its suppliers. Similarly, although the audit
committee of the board of directors was ineffective and the Examiner referred to "the mistaken deference" that this committee showed to senior financial management, Thornburgh did not recommend claims against the audit committee. † After 2005, only loans delinquent for 90 days or more were reported. If a company capitalizes costs that other
companies in the industry do not, it could be an alert that the company may be aggressive in capitalizing expenses. Additionally, Beazer violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, which prohibit fraudulent conduct in connection with the purchase or sale of securities. Thus, it is also useful to test each of the following
ratios, looking for the same trend of a decline in sales as a percentage of these particular assets • Ratio of sales to total assets • Ratio of sales to total assets Signal #3: Decrease in Revenue While Fixed-Cost Expense Remains Constant as Percentage of Sales Revenue When an
expense that has a fixed-cost component remains a constant percentage of sales revenue as revenue a
parties deserve equal information in order to make a rational decision. www.sec.gov 059402_01_ch9 p325-360.indd 355 7/7/14 9:11 AM 356 Chapter 9 • Mortgage Mayhem quarter thereafter. Jore, Dharmendra. December 27, 2007. We did not have a reserve for unfunded loan commitments at December 31, 2006. As in the implosion of Lehman
 Brothers, the fall of Bernard Madoff and other cases in recent years, many asked: Where were the accountants?" While there are those who say that the SOX reforms have not done enough to transform the financial-reporting environment, others believe that SOX "has strengthened auditing, made the accounting industry a better steward of financial
standards, and fended off Enron-sized book-cooking disasters" (Drawbaugh & Aubin, 2012). This, in a nutshell, is the story of an ego gone wild, of an insane spending spree, and of a compensation committee that acquiesced to the CEO's wishes. As part of the defendant's forfeiture, the government has entered into a settlement with Madoff's family
that requires the forfeiture of all of his wife Marion's and daughter Shana's assets and assets belonging to other family members. These "below-the-line" items included anticipated vendor reimbursements and engineering fixes* that lacked historical trend or other data evidencing their likely effectiveness. After Lily-Tulip, Dunlap went on to work in
Britain and then in Australia for Kerry Packer's Consolidated Press Holdings. Kazarian performed a true turnaround of the company, producing genuine profits and taking the company public very successfully. • We conclude dramatic failures of corporate governance and risk management at many systemically important financial institutions were a
key cause of this crisis. Fastow ordered Enron to buy a put option from LJM1 in May 1999, which would give Enron the right to sell its Rhythms stock to LJM1 in June 2004 at $56 per share. Each guarter she submitted the guarterly consolidated report to her supervisors. Problems at WorldCom After the MCI merger (in which WorldCom acquired all
of MCI's stock), things started to spin out of control. High debt means high interest expenses, which eat into profits. (a) The board of directors. Furthermore, the income from operations reported on Enron's income statement would be way above the CFFO reported in its statement of cash flows unless something drastic was done to manipulate the
CFFO. Now let us consider the stakeholders who potentially could suffer negative utility or hardship if the auditor could be fired and lose compensation and status; he or she may suffer workplace hostility from colleagues who wanted the auditor to "be more of a team player" and go along with
the client and the rest of the team; or the auditor may keep his or her job but lose the client and the fees and possibly lose status or promotion in the firm. July 5, 2006. Salomon is engaged by WorldCom on the MCI transaction, receiving fees of more than $48 million, including fees from a related investment-grade debt offering. Madoff was integrally
involved with both the SEC registration process and in the creation of the forms, known as "Forms ADV," which were materially false and misleading. 7 Obtained from U.S. Securities and Exchange Commission. • Such officers are responsible for internal controls designed to ensure that they receive material information regarding the issuer and
consolidated subsidiaries. It then would take on an obligation to buy the commodity required for delivery and to pay for it in installments. Some skeptics kept a careful watch for signs of overstated sales and earnings. In its Financial Crisis Inquiry Report of 2011, the Commission on the Causes of the Financial and Economic Crisis explained why the
housing bubble was particularly toxic: Unlike so many other bubbles—tulip bulbs in Holland in the 1600s, South Sea stocks in the late 1990s—this one involved not just another commodity but a building block of community and social life and a cornerstone of the economy: the family home. Explain why the overstatement
of a reserve for accumulated depreciation of an acquired company at the time of acquisition would cause an overstatement of goodwill. It has been well over a decade since the implementation of SOX. Consider whistleblowing in the context of virtue ethics. There are a number of criteria that must be met before bill and hold sales are allowed to be
recorded in a current period's sales and earnings: a. • Potential employees may accept jobs at firms that they may not have joined had they been in possession of correct financial statements. March 15, 2005. A couple of weeks later, on April 18, Ebbers pledged his other personal and business interests as security. 197). "Insignia Solutions Keeps
Nasdaq Listing," San Francisco Business Times. Beazer's Earnings Management 3. There were also vague references, in notes to the financial statements, to investments in partnerships and trusts and the financial News. The utilitarian or consequentialist
 focuses on the consequences of the action to establish the morality of the action, whereas the deontologist insists that morality is determined by doing one's duty at all times. "Walter Forbes Connecticut Mansion Sells for $7 Million." New York Times. Skrypek is 33 years old and a resident of Rosemount, Minnesota. The company stressed the short-
term result rather than the long-term. The speaker continued: "We feel strongly that we have vetted the scenarios, and the risk is offset by the opportunity for market share and revenue gain ..." (p. On December 1, 2012, Saurus Company went public, and by December 31, 2012, its shares were trading at $5 per share. www.cfo.com. • Michael Rigas
son of John Rigas, entered a guilty plea in November 2005 to "a charge of making a false entry in a financial record" ("Status of High-Profile ...," 2005). (a) As accounts payable. This dramatic lagging of CFFO behind net income should have been a major red flag, signaling that something was seriously amiss regarding Xerox's
reported 5 Recall that "cookie-jar" reserves refer to reserves created by overstating a future period. • List the methods that Sunbeam used to recognize future periods' sales in current periods. Glater, Jonathan D. Howe
would you characterize Beazer Homes' method of overstating its revenue? Hard Times As the mortgages, credit-default swaps grew as a tool intended to insure investors against loans that went into default. (Fixed cost refers to a category of a
business entity's expenses that one would expect to remain constant for a range of volume of units produced or services rendered.) Also, without a technical expert to optimize the configuration of the circuits, its line costs were very high. An opinion piece in The Economist celebrated the repeal of Glass-Steagall: It is always good to be rid of bad
legislation—and Glass-Steagall was a lousy law from day one. Income Statement Sales Operating Income Balance Sheet Accounts receivable year 1 $ 1,200 Year 2 $ 1,800 Year 3 $ 2,400 135 You also read in the financial press that Blake Co. sold $2,000 of its accounts receivable in
year 3. 059402 01 ch3 p069-116.indd 112 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 113 Beazer Homes USA, Inc. 732-734. Enron began to use mark-to-market accounting wherever it could. Everyone assumed that Borget would be fired, and everyone was surprised when Lay overlooked the fraud and kept Borget on. Complaint. If
he was wrong, Shore's reputation would be in shreds. The book also presents a detailed examination of the main Signals indicating possible fictitious reporting in financial statements. August 27, 2013. The fifth factor is to take reasonable steps to ensure that the compliance and ethics program is followed, including monitoring and auditing, as well as
periodic testing of the effectiveness of the program, and to have and publicize a system by which employees and agents of the organization can report or seek guidance regarding potential criminal conduct without fear of retaliation. Accumulated deficit Unearned portion of deferred compensation. Tkaczyk, Christopher. In determining to accept the
Offer, the Commission considered remedial acts promptly undertaken by Respondent and cooperation afforded the Commission staff. and demonstrated once again the genesis of his nickname: 'Chain-Saw Al.'" Dunlap's plan estimated with plant
closings." Furthermore, the reduction of 6,000 people "appears to represent one of the single biggest percentage cutbacks ever announced by a major US corporation." The downsizing expert and author, Alan Downs, commented, "You don't cut that dramatically without creating chaos inside the company." (Qtd. "An Appeals Court Is Urged to Upholcome, the reduction of 6,000 people "appears to represent one of the single biggest percentage cutbacks ever announced by a major US corporation."
Ebbers Conviction." November 12, 2005. 059402 01 ch9 p325-360.indd 339 7/7/14 9:11 AM 340 Chapter 9 • Mortgage Mayhem Signal #1: Allowance for Loan Losses not increase in proportion to the increase in the riskier portion of the
company's loans, it is a sign that the allowance for loan losses may be understated. In addition to significant financial losses to investors, corporate fraud has the potential to cause immeasurable damage to the U.S. economy and investors, corporate fraud has the potential to cause immeasurable damage to the U.S. economy and investors, corporate fraud has the potential to cause immeasurable damage to the U.S. economy and investors, corporate fraud has the potential to cause immeasurable damage to the U.S. economy and investors, corporate fraud has the potential to cause immeasurable damage to the U.S. economy and investors, corporate fraud has the potential to cause immeasurable damage to the U.S. economy and investors, corporate fraud has the potential to cause immeasurable damage to the U.S. economy and investors are considered in the potential to cause immeasurable damage to the U.S. economy and investors are considered in the potential to cause immeasurable damage to the U.S. economy and investors are considered in the potential to cause immeasurable damage to the U.S. economy and investors are considered in the potential to cause immeasurable damage to the U.S. economy and investors are considered in the potential to cause immeasurable damage to the U.S. economy are considered in the potential to cause immeasurable damage to the U.S. economy are considered in the potential to cause immeasurable damage to the U.S. economy are considered in the potential to cause immeasurable damage to the U.S. economy are considered in the U.
one of its customers. Scheme #1: Improper Timing of Revenue Recognition via Bill and Hold Sales, Consignment Sales under intense pressure to make the sales and profit targets, Sunbeam recorded future periods. An example of such a right to liberty. However, consequentialists are
vulnerable to the argument that one cannot predict all the consequences that will follow in perpetuity from one's actions. "SEC Files Amended Complaint Charging Five Enron Executives with Fraud and Insider Trading Relating to Enron's Broadband Subsidiary," U.S. Securities and Exchange Commission, 2003-58, May 1, 2003. It is therefore
important to search the notes to the financial statements for "gains" or profits earned outside of regular operations, especially where such gains appear to have been made in connection with unconsolidated affiliates of the company. The economist, Val Lambson, observed: The way capitalism works is that it sends signals through prices telling people
what they ought to be doing based on what's valued by consumers. When examining financial statements, one must be concerned when the reported income is not being earned in cash. The first IPO stock allotted to Ebbers was for Salomon's IPO of McLeod, Inc., before Ebbers was even a customer of the banking firm. The SEC alleged that Eckstein
then met with Livent's top executives. T F 5. According to Fastow, every sketchy deal he made was approved by accountants, attorneys, and the Enron board—the usual gatekeepers who guard against illegal action. Because the financial statements in those years did not specify the amount of the securitizations portion, it is safest to regard them all as
securitizations because these sales were also the sales in which "Enron retains certain interests" (Enron Annual Report, 1998). Tulsa World, www.tulsaworld.com. To my daughter Kate—Ph.D. student and budding ethicist—thank you for your significant contributions to the chapter on "Ethics at Work" and for the assignments and suggested solutions
to accompany that chapter. WorldCom needed to keep its stock price at high levels to continue its phenomenal growth" (First Interim Report, 2002, p. It is important to search the 10-Ks and 10-Qs, and to pay attention to the notes to the financial statements, and to look for the words securitization and factoring and for the phrase sales of accounts
receivable to pick up this acceleration of cash flow. Justice is named as one of the decisionmaking models offered by Fleming for business ethics. This is an example of either improperly timed revenue (if a later transaction with full economic substance
materializes) or fictitious revenue (if there is no intention of finalizing a proper transaction later on). March 9, 1998a. In addition, the company improperly disclosed the gain on a one-time event with the result of boosting the appearance of extra profits from ordinary, recurring operations. He did not get immunity, and as a result of his guilty plea to
the felony misprision charge, he got two years' probation, and a $2,600 fine. August 28, 2013. It has led to improved financial reporting and greater transparency, and the AICPA believes all investors in public companies should have equal benefit of the same protections" (Melancon, 2012). November 14, 2002. In addition, the family had sole use of at
least four glamorous condominiums in the United States and Mexico, all courtesy of Adelphia. (This is footnote #18 in original speech.) 059402 01 ch8 p292-324.indd 308 7/7/14 9:10 AM Chapter 8 • Tall Tales 309 control personnel, with focused responsibility on conflicts assessment. The Dodd-Frank Act made several changes to the whistleblower
provisions in the SOX Act in order to "clarify and improve OSHA's7 procedures for handling SOX 059402 01 ch1 p025-046.indd 40 7/7/14 8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud 41 whistleblower claims" ("Procedures for the Handling ...," 2011). (d) Understatement of expenses by improper use of restructuring
reserves. Schapiro, then chairman of the United States Securities and Exchange Commission (SEC), described the vast damage caused by the financial crisis and went on to point out: "One of the fundamental requirements for rational investing and efficient capital formation is the availability of high quality information. LR 19191. Case No. 0213533
(AJG), November 4, 2002. LR 19720. "How Pervasive Is Corporate Fraud?" Rotman School of Management Working Paper No. 2222608, Social Science Research Networks.) b. Dunlap was 59 years old when he was appointed CEO of Sunbeam in 1996. Fixed costs
increase as a percentage of sales when sales volume declines. 3. Identify major principles, rules, or values. The SEC would issue a series of emergency orders prohibiting short-selling of securities of financial institutions. Accordingly, Navistar could record the full rebate as income in the then-current period only if no contingencies existed on its
the Foreign Corrupt Practices Act. The Krispy Kreme of Using Inappropriate Accounting for RoundTrip Transactions In the case of Krispy Kreme, the "Summary of Independent Investigation" (2005) stated that although the amounts involved were not very large, the "most egregious" accounting errors they uncovered were those involving
round-trip transactions with franchise acquisitions (p. F Fill-In-the-Blank Questions Fill in the blanks with information and concepts from this chapter. Kant's standard test was that one ought to act as though a personal maxim were a universal moral law and that law could be stipulated for everyone without it leading to contradiction. The servicing
fees for years 1, 2, and 3 were $400, $300, and $200 respectively. It is likely that a price of WorldCom continued to fall, and blame was increases sharply. The stock price of WorldCom continued to fall, and blame was increases sharply.
School Forum on Corporate Governance and Financial Regulation. Signal #1: Increase in Inventory as a Percentage of Cost of Goods Sold When inventory could be overstated and that COGS could be understated. The OIG will continue to work tirelessly with
(although in some cases, like that of Sunbeam, a change in approach may not be properly disclosed). Gittelsohn, John, and Matthew Padilla. October 2010. Prepare Crafty's income statement for the first quarter with the round-trip transaction included. In addition, as a result of acquiring MCI, WorldCom had two billing systems. The $30 million
investment by LJM2 was meant to cover the 3 percent rule requiring an SPE to have at least 3 percent of its at-risk capital contributed by an independent entity in order for Enron to avoid consolidating the SPE into its own financial statements. Perhaps he had followed but didn't care. He was barred from ever again acting as an officer or director of a second consolidating the SPE into its own financial statements.
public company (LR 17710, 2002). Calculate the ratio of accounts receivable as a percentage of sales for years 1, 2, and 3 after adjusting for the sale of Blake's accounts receivable. in Amato, 2012). Dr. Jackson has appeared on a number of business news shows, including Bloomberg Television, The Street.Com, and CNN. GSEs are also at times
referred to as government-sponsored entities. The false categorization of the loan as a sale overstated both earnings and cash flow in Enron's financial statements and understated its debt. You may continue to serve as a director of Sunbaeam unless you choose to resign from that position. • Explain the main elements of Sarbanes-Oxley reform.
www.variety.com. 39-40). (c) Its gross margin will be overstated. The allowance for all loan losses was not increasing nearly as much as the delinquencies on pay-option loans were increasing nearly as much as the delinquencies on pay-option loans were increasing. (Quotes from Third and Final Report, 2004, p. July 21, 2005. 241, 242). This information includes: the most recent evidence of market declines, broker price
opinions ("BPO"), recent comparable sales, internal determinations of value, current project status and offers to purchase or sell. T 059402 01 ch9 p325-360.indd 351 F 351 Fill-in-the-Blank Questions Fill in the blanks with information and concepts from this chapter. If the Notes to the Financial Statements show the makeup of current liabilities,
check to see whether accruals for individual current liabilities decrease as a percentage of sales compared to previous periods. The Guidelines look to companies to "establish standards and procedures to prevent and detect criminal conduct." The scope of what this may require depends on the size of the organization, as the commentary to the
Guidelines suggests, with larger organizations expected to have more formal operations and resources than smaller ones. There were a number of start-ups, most of them running at a loss, just like LDDS, which was losing about $20,000 a month in 1984. To keep jobs in the town, the mayor went on a public campaign to point out the economic
stupidity of moving the plant. A further, especially egregious version of this accounting sleight of hand is when, in the period after an acquisition, a company decides that the value of the assets acquired is less than originally calculated and then creates a reserve for this decrease in anticipated, realizable value. dowjones.com/factiva. In one such
instance, "Vendor Rebate 2," McIntosh contacted Stanaway four days after the 2003 fiscal year-end to discuss the need to fill an earnings shortfall. Engineering fixes included engine design changes (e.g., modifications to engines not yet built) and service kits (e.g., modifications implemented after sale to address engine problems that arose in the
field). Hence, this creates the need for a reserve for the purported potential for the anticipated loss to be realized on those assets, and a corresponding increase is made to the allocation of the amount of the purported potential for the purported potential for the anticipated loss to be realized on those assets, and a corresponding increase is made to the allocation of the amount of the purported potential for the purported potential for the purported potential for the anticipated loss to be realized on those assets, and a corresponding increase is made to the allocation of the anticipated loss to be realized on those assets, and a corresponding increase is made to the allocation of the anticipated loss to be realized on those assets, and a corresponding increase is made to the allocation of the anticipated loss to be realized on those assets, and a corresponding increase is made to the allocation of the anticipated loss to be realized on those assets.
employees, fraudulently misstated its net income for the purpose of improperly managing its quarterly and annual earnings. The Company never received from the Automaker a sufficiently specific written quarantee of reimbursement. 059402 01 ch9 p325-360.indd 359 7/7/14 9:11 AM 360 Chapter 9 • Mortgage Mayhem From TierOne's 10-K 2006
NOTES: Note 5 Allowance for Loan Losses. Typically, once the unpaid interest on the loan reached 15 percent of the principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would cover both principal amount borrowed, the loan repayment would reset so that future payments would reset so that future paym
 "created by a party (the transferor or the sponsor) by transferring assets to another party (the SPE) to carry out a specific purpose, activity or series of transactions. Explain how Livent's improper deferral of expenses and Rite Aid's improper recognition of vendor rebates shifted the recognition of expenses from one period to a later period. What were
the main risks of pay-option ARM loans? Gadel and Micatrotto took full advantage of the lax culture that they had created by regularly billing Buca for a wide variety of personal expenses. A retrial began in October 2005 in Hartford, Connecticut (Mills & Voreacos, 2005). He eventually paid significant dollars to resolve the shareholder lawsuit, lost his
severance, and was left with huge legal bills. It is an additional signal when house prices begin to decline and provisions for loan losses do not rise in proportion to delinquencies or other signs of troubled loans. The Treasury purchased $187.5 billion of shares in Fannie and Freddie so that they would remain solvent (Shenn, 2013). Dr. Jackson has won
several awards for his teaching and is a respected speaker and consultant on aggressive financials. 129). • Independence of Analysts:
Several of the accounting scandals discussed in this book involved investment banking analysts who publicly gave certain company stocks "buy" ratings but left e-mail trails revealing that they believed those stocks were actually poor investments. Website. (c) CFFO would be overstated by $4,000. With which of the following gatekeepers did
WorldCom's Bankruptcy Examiner find fault? A grasp of ethics is also important for the establishment of what is known as an "ethical work climate" (Buchan, 2009). In 1997, Enron moved into yet another branch of energy and began trading coal. RELATED-PARTY TRANSACTIONS Management Agreement—The Company had a management
 agreement with its former parent company, Parasole Restaurant Holding, Inc. • Explain the major public and private sector roles in the dramatic growth of the mortgage lending industry and the securitization of mortgages. The U.S. Securities and Exchange Commission (SEC) findings explained how, for almost two years, Sunbeam's senior
management deliberately embarked on a series of deceptive activities to increase the perceived value of the company (AAER 1393).2 The following is a summary of the alleged tactics that Sunbeam used, beginning with the first quarter of 1997 until the second quarter of 1998, to accelerate future quarters' sales in order to boost current periods'
profits and give a misleading impression of sales growth: 1. www.fbi.gov) 059402 01 ch1 p025-046.indd 27 7/7/14 8:58 AM 28 Chapter 1 • Introduction to the Problem of Accounting Fraud Figure 1.1 Year-by-Year SEC Enforcement Statistics Enforcement Statis
 Manipulation 32 39 46 27 36 53 39 34 35 46 Securities Offering 109 99 60 61 68 115 141 144 124 89 Other 80 50 98 49 65 21 27 35 31 39 Total Enforcement Actions were classified as Issuer Reporting and Disclosure. It believes it will
easily sell this number of planes and adopts the policy of writing off the development costs over the sale of the 100 planes that it estimates it will be required to sell in order to break even. Signal #2: A Company with Large Intangible assets and a company is incurring a loss overall, it is
an indication that the intangible assets are impaired. "The divestiture forced AT&T to lease long-distance phone lines at deeply discounted rates to small, regional companies who could then resell the lines' data-carrying capacity, or bandwidth, to small businesses" (Jeter, 2003, pp. Pull agreed and placed the order with Push on December 29. New
York Post. The sales were simply not turning into 059402_01_ch3_p069-116.indd 91 7/7/14 9:01 AM 92 059402_01_ch3_p069-116.indd 92 7/7/14 9:01 AM 92 059402_01_ch3_p069-116.indd 92 7/7/14 9:01 AM 3 28,772 202,998 231,770 Q3 (40,419) 309,282 268,863 Q4 621,411 Total current assets 74,529 213,080 287,609 Q2 88,792 200,242 289,033 Q3 Q4 99,398 238,692 338,090 187,535 253,331
these contracts. A company's being late in publishing its balance sheet and statement of cash flows is a signal that the company is taking time to the statements as it has something to . In response to some of the criticisms, changes have been made to Section 404(b). (b) Enron disclosed that a significant portion of its CFFO came from securitizations of
its current assets. Like everyone else, Enron would be caught with a huge overinvestment in broadband capacity that was in oversupply. However, in publicizing its results, Sunbeam did not disclose that much of that growth came from the sales of discontinued products and from the guaranteed sales, as explained earlier in point 2. Ebbers was later
arrested and subsequently convicted "on all nine counts that he helped mastermind an $11 billion accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the special committee did not conclude that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the special committee did not conclude that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the special committee did not conclude that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the special committee did not conclude that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the special committee did not conclude that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom" (Crawford, 2005). It is important to note that the accounting fraud at WorldCom
Chapter 8 • Tall Tales investigators ... may uncover additional facts that will better illuminate the intent behind various individuals' actions and the underlying events" ("Summary of Independent Investigation," 2005, p. "The Energy Trading Flop," Houston Chronicle. http:// magazine.byu.edu. The amount of expenses moved from current periods to
future periods was tracked at Livent as the "Expense Roll." This manipulation permitted significant redirection in show expenses while also increasing profits. dartmouth.ed. Accordingly, it is hereby ORDERED that: Pursuant to Section 8A of the Securities Act and Section 21C of the Exchange Act, Respondent Beazer cease and desist from committing
or causing any violations and any future violations of Section 17(a) of the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 13a-11 and 13a-13 promulgated under the Exchange Act and Rules 10b-5, 12b-20, 13a-1, 
increase in the exact same proportion as the delinquencies on the pay-option ARM loan section of all loans. If a company overstates the reserves of a company that it acquires and increases goodwill by a corresponding amount in the period of the acquisition in order to release the reserves in a later period, which of the following will occur? INSIGNIA
RETURN TO SENDER Insignia is presented here mainly as an example of Improper Valuation of Revenue. In the next few days, Fannin, the general counsel, met with the external counsel, met with the external counsel, met with the external counsel. Dunlap then blamed the warm weather for its effect on sales of electric blankets. Enron constantly overstated its earnings and understated its debt with fictitious
accounting via mark-to-market accounting and contrived transactions with SPEs. 2. • KPMG "agreed to settle the SEC's charges against it in connection with the audits of Xerox Corp. (d) Future lease payments should not be discounted when revenue is recorded. This underestimation of loan losses corresponded with overstatements of investments in
loans and mortgage-backed securities and understatements of liabilities for repurchase of loans and for insuring investors against defaults by mortgage borrowers. • Jeffrey Skilling, 52, went on trial (with Kenneth Lay) in Houston, Texas in early 2006. At December 31, 2007 and 2006, the amount of long-term accounts receivable was $7,664 and
$7,466, respectively, which represents the balance due from these four customers under the extended payment terms. The Nature of Moral Reasoning: The Framework and Activities of Ethical Deliberation, Argument, and Decision-Making. 059402 01 ch4 p117-143.indd 119 7/7/14 9:02 AM 120 Chapter 4 • Hocus Pocus complicated and expensive
procedure whereby the computer records of goods or equipment shipped were actually backdated: Shortly before midnight on the last day of the quarter, the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that recorded and dated shipments was "brought down" so that the computer system that the co
Odlyzko and Kerry Coffman, two AT&T scientists, couldn't believe that Internet traffic was doubling every 100 days, so they undertook a research study to analyze its growth. As described earlier in this chapter, once Fannie Mae was given permission to buy conventional mortgages that were not government traffic was doubling every 100 days, so they undertook a research study to analyze its growth. As described earlier in this chapter, once Fannie Mae was given permission to buy conventional mortgages that were not government traffic was doubling every 100 days, so they undertook a research study to analyze its growth.
formation of new types of mortgage companies that competed with banks and savings and loans. Soon, however, other mortgage lenders 1 Fannie Mae and Freddie Mac, while both public companies, are regarded as having "an implicit government guarantee" (Pickert, 2008). "Enron Defendants Not Guilty for Charges," Economic Times Online.
Related-party transactions include dealings with principal shareholders, officers, directors, affiliates, and the relatives of shareholders or management. (b) Operating income will be stated as $40,000. Mills, Jane, and David Voreacos. As co-CEO with Hirko—and as Skilling's friend—Rice could do as he wished and had the final say, albeit with no
knowledge of the industry. 6 The fraud occurred at CUC before the company merged with Cendant. Corigliano apologized and took full responsibility for his actions. The company was usually responsible for the costs of running the schools, but the teachers were often paid directly by the school districts and not by Edison. In fact, one Enron vice
president reportedly said that when Enron's earnings were tight, "People were asked to look and see if there's anything more we can squeeze out of Mariner" (qtd. www.sec.gov 059402_01_ch7_p226-291.indd 286 7/7/14 9:09 AM Chapter 7 • Enron and the Tale of the Golden Goose 287 December 31, December 31, 2007 2006 Other assets Goodwill
 Unbilled receivables, net of current portion Notes receivable, net of current portion Intangible assets, net Patent costs, net Investment in affiliate Other assets Total other assets Total assets LIABILITIES AND STOCKHOLDERS' EQUITY Current liabilities Accounts payable Current portion of notes payable Current portion of capital lease obligations
Current portion of deferred revenue and advances Current portion Deferred revenue, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserve, net of current portion Deferred revenue—affiliate Contract loss reserved revenue—affiliate Contract loss revenue—a
income tax liability Other long-term liabilities Total liabilities Commitments and contingencies Stockholders' equity Common stock, $0.001 par value—100,000,000 shares authorized, 21,948,704 and 19,887,672 shares issued and outstanding Additional paid-in capital Treasury stock Accumulated deficiency Total stockholders' equity Total liabilities
and stockholders' equity 8,6827,6643,0153,4162,2744,502 - 7,466 - 1,641383 - 1,66731,220 $98,21288110,371 $90,052 $$3,553 - 112661,9643,1408,934 - 152961,9205,3112,26817918,9231,5622,007172921,3212,2917,4901024387 - 2,404 - 10,3152220110,354(552)(30,535)79,289 $98,21295,002 - (15,285)
79,737 $ 90,052 The accompanying notes are an integral part of these consolidated financial statements. "Instructor's Notes for Module 2: Management as 059402 01 REF p365-382.indd 368 Users of Accounting Information." In Core Concepts of Accounting Information." In Core Concepts of Accounting Information.
are those that limit human knavery. Federal Trade Commission. October 30, 2002. P. The situation was about to get worse: "By late 2007, the viability of the monoline insurers from which Merrill had purchased almost $100 million in hedges had come into question" (Financial Crisis Report, p. Chapter 8 AAER 1494. Also in the last quarter of 1996,
Sunbeam created a cooperative advertising reserve of $21.8 million, which the commission found was created "without any test of the reasonable amount of discussion would be a virtue
 Rigas, founder of Adelphia, is now serving a 12-year prison sentence (Gilliland, 2012). (This gave a misleading impression of Sunbeam's sales "growth" and its future profitability.) The SEC findings showed that such sales totaled $19.6 million in the first quarter of 1997 (AAER 1393, 2001). (The Fraud Trial, 2011, p. Available online via Academic
Search Elite database. If necessary, one could even interview the company's staff and customers, as was done in the due diligence tests by the underwriters of Sunbeam's debt offering in 1998. Describe the kinds of c onsequences they may have suffered. October 22, 2012. Madoff, 66, of Old Westbury, New York, faces a statutory maximum sentences.
of 10 years in prison. According to BR-6413, 2002, Adelphia added the following to its list of subscribers: • 15,000 subscribers of an unconsolidated affiliate located in Brazil. (b) Overstatement of sales. 059402 01 ch7 p226-291.indd 266 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 267 Signal #2: Vague References to
competing ethical systems. The allowance for loan losses on all loans held for investment was not increasing nearly as quickly as the reported delinquencies on the risky pay-option ARM loans were increasing nearly as quickly as the reported delinquencies on the risky pay-option ARM loans were increasing. 21). In certain instances, Beazer also purposefully did not recognize certain current period house cost to complete expenses, again resulting in
inflated profits for those periods. (Quotes courtesy of Harper Collins.) Chainsaw: The Notorious Career of Al Dunlap in the Era of Profit-atAny-Price. While awaiting sentencing, Lay died from heart disease during a vacation in Aspen, Colorado, in July 2006, at age 64 (Pasha, 2006). 11). As with Enron and WorldCom, many of the companies discussed in
Unfortunately, however, analysts had not questioned Sunbeam's numbers. Rhodes is responsible for teacher salaries and is considered to be the primary obligor for the salaries. New York: Pantheon Books. • Read extracts 1-4 from the Notes to Navistar's Financial Statements (10-K) for 2002 and 2003. Unusual securitizations or factoring of
receivables. 19) As the subprime mortgage lenders lowered underwriting standards, competition to remain the biggest lender may have been one of the forces that drove Countrywide deeper and deeper into high-risk subprime loans. "We had a lot of immaterial stuff that added up to being material," he said. Sullivan seemed to believe that a company
didn't need actual earnings to report profits of a given amount. No final, invariable rule can be laid down in defining fraud—according to Black's Law Dictionary, the act of fraud includes surprise, trick, cunning, and a range of unfair ways by which people are cheated. The frauds were not limited to any particular industry or sector of the economy, nor
were they limited to just a couple of varieties of sham reporting. • Examine the financial statements of Peregrine Systems for the following year-ends: March 21, 2000; and March 21, 2000; and March 21, 2001, given below. To the extent that the physical count revealed less inventory on hand than was reflected in its records, Rite Aid's official policy, of
course, was to write down its inventory amount in its records via a "shrink" expense on the assumption that the difference was due to theft or loss. By now, with all the acquisitions, too many companies had been added to the collection without being properly integrated into a synergetic whole. 7/7/14 9:15 AM 368 References "CGMA Report Reveals to the collection without being properly integrated into a synergetic whole. 7/7/14 9:15 AM 368 References "CGMA Report Reveals" and the collection without being properly integrated into a synergetic whole.
Gap in Rhetoric, Reality on Business Ethics," May 21, 2012, AICPA Press Release, www.aicpa.org. This was a $12 billion deal whereby WorldCom acquired UUNet at the same time. The agreements expire on December 31, 2005. During 1996 and 1997, Livent recognized $34 million of revenue on transactions that utilized side agreements that
required Livent to repay the revenues that it received. It does not turn into cash like an honest sale. The Powers Report (2002) went on to explain: On November 8, 2001, Enron announced that Swap Sub was not properly capitalized with outside equity and should have been consolidated. (Refer to Chapter 2, "Ethics at Work," for a description of the
utilitarian framework.) b. He was also ordered to pay Cendant and its investors over $3 billion in restitution ("Ex-Cendant Chairman... Sunbeam is presented in this chapter mainly as an example of: • Improper Expense Recognition via
the use of restructuring and other liability reserves (refer to Table 1.1.) 1 Background information in this chapter is mainly from Byrne (2003), Byron (2004), Laing (1997; 1998a; 1998b), Scherer (1996), and Schifrin (1998). Exhibit 9.1 Extracts from Consolidated Balance Sheets Countrywide Financial Corporation 10-K 20055 December 31 2005
2004 (in thousands, except share data) ASSETS Cash Mortgage loans and mortgage-backed securities pledged as collateral, at fair value Securities purchased under agreements to resell, securities borrowed and federal funds sold Loans held for investment, net of allowance for
loan losses of $189,201 and $125,046, respectively Investments in other financial instruments, at fair value Mortgage servicing rights, net Premises and equipment, net Other assets  
Total assets 5 $ 1,031,108 $ 751,237 36,818,688 10,314,384 668,189 37,350,149 10,558,387 1,303,007 23,317,361 13,456,448 70,071,152 11,455,745 12,610,839
1,279,659 7,518,245 1,75,085,370 39,661,191 10,091,057 8,729,929 985,350 5,608,950 128,495,705 Obtained from U.S. Securities and Exchange Commission. Likewise, it would be expected that the fixed-cost component of an expense would decrease as a percentage of revenues when revenues increase. Furthermore, with LJM1, Fastow caughten and Exchange Commission.
even Skilling and Lay off guard with the extent to which he profited from the SPE. He was the retired chairman of IndyMac which, "split off from Countrywide in 1997" (Vincent, 2003). (b) To cause EPE to obtain a loan from a bank and divert the funds to Enron. The consequences of violating any of the provisions of the act may be quite severe and
may carry "potential criminal and civil penalties" (SEC v. Suspicious track record of top executives, particularly when their previous companies reported swift earnings turnarounds that suddenly evaporated. ("Buca"), a publicly traded, Minneapolis-based Italian restaurant company. Explain why this could be a signal of "improper use of acquisition or
merger reserves." 32. Armed with the power to report virtually any fictitious profit it wished and to hide almost immeasurable amounts of debt, Enron burned through billions of dollars on foolhardy projects on several continents. Shenn, Jody. Cullinan, Charles P., and Gail B. The total sales for the new stores that opened in year 11 amounted to $30
million. Using the Consequentialist/Utilitarian Approach in the Business World Let us consider, for example, the case of an auditor who contemplates bowing to pressure from a client to give an unqualified audit opinion on a knowingly incorrect set of financial statements because the client wants to boost the company's stock price. The loan terms
       ity that the loan amount must be repaid on three specific repayment dates by the issue of shares in Khaa
                                                                                                                                                      addition, because of earlier price caps, a number of gas producers had closed down, and many industrial gas plants and utilities had experienced shortages of gas. The parent company may even want to avoid taking a large one-time
charge in its income statement to acquire the cookie-jar reserves. At the end of each quarter, Livent simply
                                                                                                                                                            certain expenses and the related liabilities from the general ledger. It was in the area of accelerating the recording of future sales that Sunbeam presents itself as the ultimate case study in pulling every trick in the book to boost
sales and profits. 059402 01 ch8 p292-324.indd 301 7/7/14 9:10 AM 302 Chapter 8 • Tall Tales foreign ownership restriction" (AAER 1494, 2002). Obtained from U.S. Securities and Exchange Commission. Not only was the demand grossly overestimated, but all the large companies, including WorldCom, Global Crossing, Qwest, AT&T, Enron, and
Sprint, were building and acquiring capacity to meet that fictitious demand. (A special purpose entity (SPE) is a business entity such as a partnership, trust, or joint venture created as legally separate from a company's normal operating activities.)
In accounting terms, if certain conditions are met, the SPE's debt need not be "consolidated" with the company's debt and its assets are also not added into the company's consolidated balance sheet. Metaethics addresses foundational issues and presuppositions of ethical frameworks. From 1999 until March 2005, Skrypek was Buca's Controller. Pay
special attention to the related-party transactions note and study all the company's financial statements in search of disclosures of any transactions between the company and its major shareholders, directors, or company officers (as well as their families or affiliates). The SEC noted quite pertinently that at that particular stage, it "was readily
apparent that 3 Rite Aid consented to the issuance of the order without admitting or denying the findings as set out in AAER 1579 (2002). the scheme allegedly perpetrated by JPMorgan Venture Energy Corp. In 2000, Enron Broadband's revenues were way behind predictions. (b) Whistleblowers are protected in Europe rather than in the U.S. (c)
Whistleblowing laws are stricter in Germany than in the U.S. (d) U.S. whistleblowing laws allow whistleblowers to go under the FBI protective custody program. It emerged that Borget had been incurring losses and concealing them by selling his losing oil futures at a "profit" to sham companies that he had set up in order to report false profits to
inflate his bonus. Possible overstatement of earnings via any method of overstatement of expenses. Why on earth would anyone have wanted to buy the ailing project back when he or she had already "sold" it due to its difficulties? CNN.com. September 26, 2002. In the third round-trip transaction, Krispy Kreme paid a
distribution to a former franchisee without reducing the repurchase price accordingly. Why did SSB's analyst recommend the deteriorating company so highly? Xerox's name for the accounting method under which it made this shift was the "margin normalization" system. Such aggressive policies often include the failure to record the impairment of
assets. (d) The packing case should not be included in Ace's December 31 inventory. Little did anyone suspect what was brewing on Wall Street. 059402 01 ch7 p226-291.indd 277 7/7/14 9:08 AM 278 Chapter 7 • Enron and the Tale of the Golden Goose • Kenneth Lay, 64, went on trial (with Jeffrey Skilling) in Houston, Texas, in early 2006.
Whether true or not, this devout deacon divorced 059402 01 ch5 p144-190.indd 154 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom to WorldCom to WorldCom to WorldCom Wizardry: From WorldCom Wizardry: From WorldCom to WorldCom Wizardry: From WorldCom to WorldCom Wizardry: From WorldCom to WorldCom Wizardry: From WorldCom Wizardry: From WorldCom to WorldCom to WorldCom Wizardry: From WorldC
goods grew quickly, and in 1981, under increasing pressure, Sunbeam believed that its best option was to be acquired by Allegheny International, Inc. As luck would have it, the stock prices of Internet companies and telecommunication companies are telecommunication companies and telecommunication companies are telecommunication companies.
company employees and that there were too few "outside" directors. In March 2006, Michael Rigas was sentenced to 24 months of confinement at home (Bray, 2006). www.ebscohost.com. Improper Use of SPEs: The SEC's Complaint (2011) against Basin Water, Inc. In addition, in the event that Whitewing lost
money on the resale of the assets it had purchased from Enron (at inflated prices), Enron had guaranteed that it would compensate the Whitewing structure with the issue of Enron stock to make up the shortfall. Second, the firms began offering letters of credit to guarantee payment to investors in the event of default by borrowers. If a company sells
or factors a material portion of its accounts receivable, what adjustments must you make to accounts receivable before doing your test to see whether the financial statements contain any signals indicating an overstatement of sales? (c) The SEC. 059402 01 ch2 p047-068.indd 49 7/7/14 8:59 AM 50 Chapter 2 • Ethics at Work This type of
utilitarianism is known as hedonism, encapsulated by the phrase "The greatest happiness for the greatest number" (Sinnott-Armstrong, 2012). Soon, Countrywide had many competitors who concentrated on these precarious, large subprime loans with riskier loan-to-value ratios, debt-to-income ratios, and credit scores, as well as lacking in the
documentation of income. Madoff Investment Securities LLC (BLMIS), pled guilty today to a two-count superseding information charging him with, among other things, conspiracy to commit securities fraud, tax fraud, mail fraud, ERISA2 fraud, and falsifying records of an investment advisor. The expense is recognized in the current period. Belson,
Ken. Review Sunbeam's signals of overstatement of sales (see Chapter 3) and identify which of those signals could have been found in an analysis of Basin Water's financial statements. Friends of Angelo: Countrywide's Systematic and Successful Effort to Buy Influence and Block Reform. Professor Perry later remarked, "Obviously, something needed
to be done. From an examination of Table 5.4, we see that for WorldCom, the amount of dollars reportedly invested in PPE grew steadily from $17.2 billion in the first guarter of 2002, at the height of the fraud. 059402 01 REF p365-382 indd 371
Taub, Stephen. Enron Online Moving into new trading markets usually meant that Enron had no comparative advantages, and there were often huge disadvantages to having absolutely no knowledge of the new industry. According to the SEC, Countrywide "originated over $490 billion in mortgage loans in 2005, over $450 billion in 2006, and over
$408 billion in 2007" (SEC Complaint, October 24, 2012, par. Why did the directors allow the chaotic list of acquisitions and the colossal loans to Bernie Ebbers? Do you think "pure, practical reason" offers a compelling incentive to choose the right course of action, or do you think external forces are necessary to keep people honest? (b) Hid $2.3
billion in debt. 2010. However, it is also the story of the collision and collusion of the forces that came together when fund managers who acquired Sunbeam hired a slash-and-burn chief executive officer. Stanaway and McIntosh also knew or should have known that including anticipated vendor reimbursements and engineering fixes without data
evidencing their effectiveness was not in compliance with GAAP. Wilczynski, Martin S. "Another Cendant Hung Jury." February 20, 2006. Securities and Exchange Commission Litigation Release, February 28, 2001. U.S. Bankruptcy Court 7/7/14 9:15 AM References 375 Southern District of New York. 2002-2003. PARAGRAPHS 21-35 FROM
COMPLAINT: Undisclosed Related Party Transactions Between Buca and Vendor in Which Gadel Had Substantial Involvement 21. 059402 01 ch3 p069-116.indd 81 7/7/14 9:02 AM 130 Chapter 4 • Hocus Pocus The Insignia
Scheme of Failing to Value Revenue Correctly The SOX Report (2002) listed Insignia Solutions PLC as an example of the failure to value revenue properly via providing inadequate allowances for returns. Guyon, Janet. • Led by the Division of Investment Management, we have adopted new rules that have already resulted in approximately 1,200 hedge
fund and other private fund advisers registering with the SEC. Signals of Enron's Fictitious Reporting Schemes of Using SPEs (or Unconsolidated Affiliates) to Understate Earnings Because SPEs are usually equity investments—investments in which the investments in which the investments in the investment in the investme
SPEs is often included but hidden among the other equity investments on the investor's balance sheet. 12 Civ. To discover this manipulation, search the financial statements for large one-time charges in the income statement or for reserves decreasing in later periods on the balance sheet. Edison's practice was to record the gross amount as revenues
and include the district-paid expenses as its expenses in its income statement. Therefore, I find it difficult to see how the governance structure of a financial services firm can satisfy this factor unless its oversight includes consideration of the effectiveness of the compliance and ethics program in addressing conflicts of interest. Borget was
unrepentant and actually accelerated his oil futures trading. According to Litigation Release 22014, "In February 2009, Basin Water restated its financial results. If Xerox's revenue to accelerate its recognition. 59). Tales of CEOs Gone
Wild (2004, p. Right action corresponds 7/7/14 9:17 AM 392 Glindex with the act that produces the greatest amount of pleasure. Big Company purposely overstated the reserve was understated by this amount. Ethics and the Federal Securities Laws The
debate about how law and ethics relate to each other traces all the way back to Plato and Aristotle. Nowell, Paul. "Enron's Top Executives Are Convicted of Fraud," Los Angeles Times. (b) When the sales-to-PPE ratio decreases after an acquisition. Of course, all the debt incurred by the SPEs—debt for which Enron was ultimately responsible—was kept
off Enron's balance sheet until it became absolutely clear that the SPEs could not repay their debts. In addition to the focus on natural human rights, issues such as animal rights and potential cruelty to animals could also be a concern. (b) No decrease in operating income, but a decrease in net income in the group's consolidated income statement in
the period of the acquisition. www.springer.com. According to the SEC release of May 1999, "After the shipment, the supervisors instructed a subordinate to 'drop the zero' or report only 10% of the inventory held by the reseller.... He was also a big donor to a variety of civic causes and colleges all over Mississippi. The term underwriting standards
refers to the credit risk standards that lenders require to be met before they will grant a loan to a borrower. Ebbers's version makes it appear that accepting massive loans from WorldCom was a magnanimous favor he did for the company; it was a gesture of all heart. The Commission contended that Sensormatic devised a 1 Sensormatic consented to
the issuance of the order without admitting or denying the findings contained in the order. Essentially, Enron would insure its customers against unusual weather conditions (Bryce, 2002, p. This understatement of expenses and liabilities of $10 million for the first quarter of 1997 was a significant part of the financial misstatements. Exhibit 7.1
provides a diagram from the Powers Report showing how Chewco and JEDI were financed. The rapid increases in delinquencies of pay-option ARM loans from 2004-2006 was a signal of the rapid future increases in delinquencies and loan losses that were likely to occur as the loans reset over time. Nash, Laura. 18-19) The following Monday, Sunbeam
put out a press release saying that there was no factual support for the accusation in the Barron's article that Sunbeam had largely invented its profits. Such loans often backed MBSs and CDOs. Credit rating agencies, 328 Credit Suisse First Boston Bank, 259 Criminal accounting fraud, 28-29 CUC International, Inc., 126-129 Cuiába Power Plant,
257-259 Curry, Wanda, 240 D Dabhol Power Project, 237-238 Davis, Gray, 246 Days' sales in inventory, 203 The length of time it takes a company to turn its inventory into sales. An examination of the outer world ascertains what that duty is. The case was labeled: "Hold for shipping to customer on January 5." The shipping documents show that the
sale to Ace's customer is "FOB Shipping." For the preparation of Ace's December 31 financial statements, which of the following is correct? The recording of sales when the customer has a right to return the product is a signal of the of sales. Describe Beazer Homes' method of overstating its revenue. www.lexisnexis.com. The artificially high prices in
this semi-deregulated market were making much more profit for Enron than market prices ever could. Canedy, Dana. "ExWorldCom CEO Ebbers Guilty." CNN Money. Similar requirements also exist for broker-dealers under FINRA rules.18 In my view in order to be adequate and effective these compliance and supervisory policies and procedures
must include processes to identify, assess, mitigate and manage conflicts of interest. Questions: a. Davis, Michael. July 9, 2013. The problem with a fictitiously recorded sale is that it remains as accounts receivable. Finally, audit firms usually audited the same companies year after year, developing friendships with management, growing complacent
and sometimes dropping their quard. Countrywide Financial Corporation 10-Ks. 2004-2007. One of his favorite fabrications had its origin in South America, where Enron owned 65 percent of a Brazilian company called Empressa Productura de Enerain Ltd. Marion Madoff is being left with approximately $771,733 to live on for the rest of her life. This
was the method the company used for the improper valuation of its revenue. For more details, refer to Sarno, Mueller, and Burns (2010) who present a well-written overview. When the company consistently meets sales or earnings estimates every quarter. The interest earned (or accrued) on this loan for the year was $54,000. All the Devils Are Here:
The Hidden History of the Financial Crisis. March 29, 2012. After this, Ebbers and his associates bought ReTel Communications, also in Tennessee. With LJM2, Fastow would not only dramatically expand his overstatement of Enron's earnings, but he would also fatten his own bank balance in various conflictof-interest dealings between Enron and
LJM2. The Third and Final Report (2004) on the WorldCom bankruptcy analyzed the inappropriate release of reserves to overstate earnings in two categories: (1) the manipulation of line cost accruals to boost profits by reducing reported line costs and (2) the improper release of reserves into profits to "close the gap" between
earnings targets predicted by Wall Street and actual earnings. (Shrinkage refers to the loss of inventory between the point of goods sold, but it is presented first because understating cost of goods sold by
overstating ending inventory values is a very common financial reporting fraud. Next, the company provided hardware for Microsoft's online service, MSN. As a legal entity, JEDI could, of course, borrow cash—and the resulting debt incurred would be JEDI's debt, not Enron's. In the press release announcing its results for the first quarter of 1997,
Sunbeam's sales showed growth of 10 percent compared to the first quarter of 1996. To make matters worse, WorldCom became embroiled in an expensive lawsuit with Digex shareholders. (d) Enron disclosed that it engaged in related party transactions with unconsolidated, specially constructed entities. "The Final Act: Financial Reporting
Implications of the Dodd-Frank Wall Street Reform and Consumer Protection Act." Heads Up, Vol. In addition, WorldCom gave Arthur Andersen misleading special "MonRevs"; namely, monthly revenue schedules that concealed the top-side journal-entry adjustments. The investment firm was ordered to pay a total of over $1.4 billion in "compensatory
and punitive damages" in respect of the sale of Ron Perelman's Coleman Company to Sunbeam in 1998. www.ips-dc.org. "Former Enron CEO Denied Release to Attend Son's Funeral," CNBC. In October 1987, Lay was in Europe and received an emergency call from Enron president John M. Sunbeam overstated its income by failing to maintain large
enough provisions for doubtful debts. (b) Having a loan-to-value ratio of 95 percent or higher. Unless a company operates in an industry where the use of SPEs is widespread, the financial statements and the MD&A should make very clear the nature of the SPE, as well as the reason for its use. (d) Inappropriate accounting for roundtrip transactions.
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(Essentially, Enron sold part of its own share of the Brazilian 059402 01 ch7 p226-291.indd 257 7/7/14 9:08 AM 258 Chapter 7 • Enron and the Tale of the Golden Goose company back to itself, like a dog chasing its tail.) Fastow then concluded that with its reduced ownership in Cuiába/EPE, Enron no longer needed to consolidate Cuiába/EPE into
its financial statements. March 15, 2006. Signal #2: CFFO Falling Behind Operating Income The second signal of inap- propriately recorded sales is when CFFO lags, or falls behind, operating income or net income. Theories of Ethics There are three major branches of ethics: metaethics, normative ethics, and applied ethics. 267). After serving three
months of his sentence, Abdelhak was released on parole (Becker, 2003). On a subsequent visit to Mississippi College, the deeply religious and conservative young Foster had a good feeling about the college and the town, with its many grand Victorian-era homes. Lehman regularly increased its use of Repo 105 transactions in the days prior to
reporting periods to reduce its publicly reported net leverage and balance sheet. Finally, Gadel and Skrypek's scheme to meet earnings targets through the improper capitalization of expenses. www.sec.gov. To Christine
Burdick-Bell who, in spite of her demanding schedule, is always available to answer a question or give valuable feedback on the text, I am sincerely grateful. (c) Changes to asset-backed securitization practices. 324) After firing Dunlap and Kersh, Langerman continued to investigate the depth of Sunbeam's problems. Without a powerful leader, profits
fell quickly and steadily. As poor as this aspect of corporate governance was, Thornburgh conceded, "In the 059402_01_ch5_p144-190.indd 166 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCo
approved without apparent due diligence. No wonder the stock market was a little skeptical. cpajournal.com. Gadel and Skrypek together had the ultimate responsibility at Buca for whether an item should be capitalized. While McDonnell Douglas launched its DC-10 project, Lockheed began its design and production of the TriStar. At this time, Globa
Crossing, AT&T, and all the other big telecommunication companies were overinvesting in broadband capacity and chanting the erroneous mantra "Internet traffic is doubling every 100 days" (Malik, 2003, p. Corigliano was sentenced to three years of probation. In January 2012, Mr. and Mrs. LJM Investments. (c) Valuation measurement based on
consistent company policies. As set out in AAER 1017, March 25, 1998. The Financial Crisis Inquiry Report (2011), explained how Merrill Lynch had been keen on subprime assets until the failure, in late 2006, of two mortgage-loan firms that had received extended credit from Merrill (p. 059402 01 ch2 p047-068.indd 50 7/7/14 8:59 AM Chapter 2 •
Ethics at Work 51 Kant went even further by saying that if you perceive telling the truth as a duty, you must always tell the truth for that reason in itself. (a) U.S. companies with European subsidiaries must follow the act, but the labor laws in their respective European countries do not recognize the importance of whistleblowers. As part of its
homebuilding and sales operations, Beazer regularly acquired large parcels of land upon which it constructed houses. On December 20, Zee Company, an office- supply company, and a supply company company
shareholders. "Judge Rules Brown Owes Rigas Family over $400,000," Potter Leader-Enterprise. 059402_01_ch5_p144-190.indd 180 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom Wizardry: From WorldCom Wizardry: From WorldCom Wizardry: From WorldCom Touch Complaint against Tyco International Case 06-CV-2942 Filed April 13, 2006* UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK 16. Nevertheless, the Company, through its senior accounting staff, deferred these start-up costs from the fourth quarter of 2002. Thank you to the following reviewers, whose comments helped to shape the final manuscript: Richard G. The Powers Report (2002) stated that if
Enron had agreed to make LJM1 whole (i.e., compensate it for any loss on its investment), "Enron would have been required to consolidate Cuiába/EPE, and could not have recognized the mark-to-market gains" (2002, p. April 25, 2005. "Rebecca Mark's Exit Leaves Azurix Treading Deep Water." Wall Street Journal. These efforts were continually
rebuffed by the Automaker. Mueller, Robert S. This proper accounting treatment would not have permitted Beazer to record the model home sales revenue and profit at the beginning of the lease term. Reprint. These sudden changes in gross margins were probably due, in part, to practices such as selling inventory in 1997 at higher prices than the
restructuring purported to anticipate because some inventory had been valued at incorrectly low amounts. Salomon is engaged by WorldCom on its exchange offering for MFS Bonds, receiving fees of approximately $1,500,000. LivePlay Company has incurred $300,000 in scenery production costs for the play Cat Trap. Glassman, Cynthia A. Beazer
would also retain a right to receive a percentage of the appreciation of the model home upon its sale at the end of the lease term (the "Appreciation Rights"). Two French companies, Vivendi and Suez Lyonnaise, were already operating water utilities for local governments around the world, and they were doing very well. A Wall Street commodity
trader is reported to have said that the metals company was worth only a fraction of what Enron had paid for it. www.research.stlouisfed.org. In its discussion of the auditors, the Third and Final Bankruptcy Report (2004) alleged that "the company has claims against Arthur Andersen due to its responsibility for the failure to detect any aspect of the
company's accounting fraud" (p. The indications of troubled loans include: (a) Loan delinquencies. Overstating inventory to reduce cost of goods sold, as well as other methods of understating cost of goods sold, affect similar key ratios. Beazer's Reporting Violations: Section 13(a) of the Exchange Act and Rules 12b-20, 13a-11 and 13a-13
Thereunder 20. In connection with such cooperation, Respondent has undertaken: To produce, without service of a notice or subpoena, any and all documents and other information requested by the Commission's staff at such times as the staff reasonably may
direct; To use its best efforts to cause its employees to appear and testify truthfully and completely without service of a notice or subpoena in such investigations, depositions, hearings or trials as may be requested by the Commission's staff; and That in connection with any testimony of Respondent to be conducted at deposition, hearing or trial
pursuant to a notice or subpoena, Respondent: i Agrees that any such notice or subpoena for Respondent's appearance and testimony may be served by regular mail on its attorney, David G. A significant decrease in allowances for returns as Allowance for returns may be understated. Through these management representation letters, Gadel and
Skrypek represented, among other things, the accuracy and completeness of Buca's financial statements. (b) Improper recognition of revenue on out-of-period shipments. Ebbers joined the college basketball team and soon was awarded a 059402_01_ch5_p144-190.indd 145 7/7/14 9:04 AM 146 Chapter 5 • WorldCom Wizardry: From WorldCom to
WorldCon basketball scholarship. Andrew Fastow To fulfill his ultimate vision of Enron as a trading company, Skilling realized he had to find a financial expert who knew his way around the system and who could wheel and deal for Enron. Conversely, at the origin of the reserve, it overstates expenses and understates profits in an apparently
nonrecurring manner in the period in which it was first created. • A criminal investigation into Xerox's accounting practices was c oncluded in October 2004, and U.S prosecutors did not file charges ("Xerox Cleared... 40. Which of the following was not a false revenue stream that was generated by Enron's use of off-balance-sheet entities Chewco
and Jedi, as identified by the Powers Report? Mulford, Charles W., and Eugene E. It is easy to get profits up in the current year by cutting R&D, but that will kill future growth and profits. Lay was now CEO of a huge company that, with over 37,000 miles of pipeline, controlled "the largest gas-distribution system in the country, running from border to
border, coast to coast" (McLean & Elkind, 2004, p. In the case, the issue was that it did not accurately and completely describe the realities of its operations in its MD & A. 059402 01 ch7 p226-291.indd 275 7/7/14 9:08 AM 276 Chapter 7 • Enron and the Tale of the Golden Goose Table 7.7 Debt-to-Equity Ratio: 1998-2000 1998 1999 2000 Total
Debt $20,159 M* $21,381 M $51,619 M Total Equity $ 7,048 M $ 9,570 $11,470 M Debt: Equity Ratio 2,860 2.234 4.500 *M = million. Kenneth Lay and a few other Enron employees paid a visit to Enron Oil and soon discovered that "the traders were keeping two sets of books, one for legitimate purposes . . . Furthermore, how does one proceed when
the virtues are at odds in a certain situation? Leading standards have recognized the centrality of ethics and have explicitly integrated ethics into the elements of effective compliance and enterprise risk management. Examine the following extracts from Blake Co.'s income statement and balance sheet for the previous three years. Such non-GAAP
sales increased Sunbeam's reported earnings; however, "GAAP does not permit the recognition of revenue in transactions lacking economic substance" (Cullinan & Wright, 2003), Douglass, Elizabeth. We were only seeing the tip of the iceberg,
however. Bush. Business ethics is a type of metaethics. Unemployment will be detrimental to Lucas and his daughters, who rely on Lucas's salary for all their needs. in Jenkins, 1997) Cost-accounting analysis shows that when a company closes down a segment, although it does lose that segment's revenues, it does not lose all of the costs that are
allocated to it in typical income statements. If Sunbeam had begun falsely reporting overstated sales and profits in 1997, without any dramatic plan at all, the numbers in the financial statements probably would have been questioned much sooner. To the extent that a company overstates the reserves, it overstates goodwill by a corresponding amount
25. Signal #2: Decrease in Current Liabilities as a Percentage of Current Assets or of Sales When the company first omits recording expenses and current liabilities as a percentage of sales. Ebbers—now living in Brookhaven, Mississippi, and running
nine hotels—was introduced to this business venture by David Singleton, a friend from Ebbers's prayer group at the First Baptist Church in Brookhaven. (d) Nihilism. Under this model, the matter of paramount importance is the fairness of treatment of all the individuals involved. In addition, as an executive officer of Buca, Gadel completed proxy
questionnaires each year in connection with the preparation of Buca's proxy statements. All in all, as a result of an independent investigation by KPMG Peat Marwick, Livent restated its financial statements for the years 1996 through the first quarter of 1998. Utilitarianism requires the identification of stakeholders who could suffer consequences due
to the choice of a particular action. But as the world learned in 2001, the laws of physics don't apply to fame. To test for an unrecorded liability, it is pointless to start with the list of current liabilities recorded by the firm and simply check those amounts. In other cases, because the entities depended on their Enron stock as a major asset, Enron had
guaranteed that if the Enron stock price fell below certain specified amounts, Enron would issue more shares or cash to the entities to compensate them. Consolidated Press Holdings, 73 Consulting fees, for auditors, 31-32 Consumer Financial Protection Bureau (CFPB), 40 Contingent sales, 80-81 Cookie-jar reserves, 82, 154, 158-159 Reserves that
are created by overstating a future liability in one period in order to release it in a future period, thereby implying that the company has less expense in the future period. First, coal was probably a better option than gas for India's electricity production. "NSU to Honor Ron and Kathy Assaf with President's Community Award at its Celebration of
Excellence." January 12, 2012. News Release. Within weeks of the firing of Dunlap, the stock price had fallen to below $10 per share. Galbraith explained that opportunists begin to ignore the reasons behind rising prices. Improper Valuation of Revenue INSIGNIA The following schemes involve improper expense recognition and a corresponding
overstatement of assets or understatement of liabilities or reserves: 6. Explain the major way in which Beazer's land inventory accounts scheme differs from Sunbeam's use of improper reserves. In fact, all the electric and gas utilities faced risks due to changing prices as a result of fluctuating weather conditions. The joint venture was named JEDI, and inventory accounts scheme differs from Sunbeam's use of improper reserves.
acronym for Joint Energy Development Investments, and a tongue-in-cheek reference to Andrew Fastow's admiration of the Star Wars film. The Commission found that "the suppliers' rebates obtained by Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.indd 82 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam beginning in the second quarter of 1997 059402 01 ch3 p069-116.
83 were made in contemplation of future purchases, and therefore should have been recognized as the related sales were made" (AAER 1393, 2001). His basketball team won the city championship in his senior year. 154-155) Fastow was doing well, but he wanted to do better. "Risk Modeling at the SEC: The Accounting Quality Model." U.S.
Securities & Exchange Commission. Easy Banking: Regulations Repealed Following the Great Crash of 1929, the Glass-Steagall Act of 1933 had separated commercial banking from investment banking from investment banking from investment banking from investment banking. Regulations Repealed Following the Great Crash of 1929, the Glass-Steagall Act of 1933 had separated commercial banking from investment banking.
massive and poorly hidden frauds? Dealings between Adelphia, the Rigas Entities, and the Rigas family itself became even more complicated and obscure by the mingling of funds among the various groups. The following is an extract from its income statement for the previous three years. 19 059402 01 FM p001-024.indd 19 7/7/14 8:57 AM
Acknowledgments It certainly "takes a village" to write a book, and this book could not have been written without the encouragement and support of many. She was apparently informed that "CUC's quarterly results would meet earnings expectations of Wall
Street analysts." Polverari was even told that some of the adjustments were made to achieve percentage targets for some expenses and that some of the adjustments were "to ensure that items such as receivables and cash were at levels he [the CFO] thought desirable." (Quotes from AAER 1275, 2000) The Commission found that for the fiscal years
ended January 31, 1996; January 31, 1996; January 31, 1997; and December 31, 1997, the top-side alterations aggregated $31 million, $87 million, and $176 million, respectively. By November 12, 1996, the stock price was up in the high $20s. For example, under the direction of Causey [Enron's chief accounting officer] and others, company personnel fraudulently
increased the value of one of the largest of Enron's merchant assets, Mariner Energy, Inc., by $100 million in the fourth quarter of 2000. Tett, Gillain. He was just what Ebbers needed: a serious and seriously smart sidekick—the brains to Bernie's brawn. 2006. Although just short of Sunbeam's own unrealistic targets, the reported results after all the
ploys to accelerate future sales were supposedly record results. As can be seen in Figure 1.1 (below), the SEC's Enforcement Actions cover a range of financial violations, such as insider trading, market manipulation, and securities offering violations to financial violations in addition to financial violations, such as insider trading, market manipulation, and securities offering violations in addition to financial violations. According to Bryce (2002), the potential for
reporting profits on such a long-term contract convinced Skilling to adopt mark-to-market accounting. • Angelo Mozilo, former CEO of Countrywide, settled an SEC civil fraud case for $67.5 million in October 2010. If Mariner had been a publicly traded company where shares could be sold at a moment's notice, there would have been valid, objective
guidelines to use when revaluing Enron's shares in Mariner. Sensormatic also overstated its revenues by shipping goods before the customer needed them and instructing the carrier to delay delivery. In future periods, they would just revenues by shipping goods before the customer needed them and instructing the carrier to delay delivery. In future periods, they would just revenues by shipping goods before the customer needed them and instructing the carrier to delay delivery.
surrounding Dodd-Frank continues, with some alleging that it does not do enough to stop future crises and others maintaining that it goes too far. Also, if a category of expense has a significant fixed expenses may not be
reported on the balance sheet. GREG A. There were colossal understatements of allowances for mortgage loan losses, whether by fraudulent intention or by an innocent but naïve belief that house prices could continue to increase forever. The managing partner asks Eva where Lucas is. At December 31, 1998, a total of $209 million of such guarantees
were outstanding.... He was certain that deregulation would eventually come to the gas industry and that it would unleash vast opportunities for making a fortune from natural gas. The fact remains that in 2002, after the SOX Act was signed into law, the corporate community heaved a collective sigh of relief and went back to business on Main
Street. "Broadband executives sat in meetings poring over reports of the pilots' comically pathetic results: the Care Bears Movie: Seven purchases—$8.40" (McLean & Elkind, 2004, p. 69). During this time, Gadel, Skrypek, and their subordinates regularly received and approved requests for the reimbursement of personal expenses, including requests.
accompanied by little or no supporting documentation. Use specific examples from each company. ("Clearing the Fog") 059402_01_ch9_p325-360.indd 331 7/7/14 9:11 AM 332 Chapter 9 • Mortgage Mayhem Of course, much of this $62 trillion was backed or covered by subprime loans, and most of the issuers of the CDSs had no hope of being able
to pay out the amounts that they had guaranteed if mortgage borrowers defaulted and housing prices dropped. Once again, Enron and WorldCom were symptomatic of the recurrent problems of inadequate and flawed systems of internal audit departments that came under the authority of the very
managers they were meant to audit. Signal #2: Growth of Existing Store Sales Less Than Growth in company Sales Another signal of this problem is when growth in existing store sales. 059402_01_ch7_p226-291.indd 241 7/7/14 9:08 AM 242 Chapter 7 • Enron and the Tale of the Golden Goose Never
one to miss an opportunity, Jeffrey Skilling turned to his newfound telecommunications division and came up with four big, bad ideas: 1. He has agreed to forfeiture of more than $143.1 billion, including all of his real and personal property. Eva also believes that Lucas will be back soon and that he will make up the missed work. He received two years
of probation and a small fine (Federwisch, 2007). Dunlap emphatically denied the divorce complaint. Moreover, the mere process of identifying the possible consequences to all the stakeholders would likely increase the decision maker's awareness of the wrongness of the unethical act, the risks associated with the wrong action, and the importance of
doing the right or ethical thing. "Key Witness in Enron Trial Makes a Few Concessions," Houston Chronicle. Table 7.1 Enron's Pretax Gains on Sales of Merchant Assets* Year Amount 1997 $136 M** 1998 $628 M 1999 $756 M 2000 $104 M * Derived from Enron's Notes to the Consolidated Financial Statements. To deal with the losses from the
Blockbuster debacle, Enron decided to spin a web of SPEs. A variety of these SPEs were used to confuse the situation in order to book a profit via a project known as Braveheart. Improper "Sales" of Accounts Receivable and Improper bisclosure of the Acco
receivable and improperly disclosing its "sales" of accounts receivable. The internal control deficiencies, in turn, resulted from senior management's failure to dedicate sufficient resources and attention to the adequacy of Navistar's accounting and reporting functions. Among other items, Gene Smith casually mentioned the capital expenditure audit
at which point Sullivan asked them to delay it a few months. • We conclude widespread failures in financial regulation and supervision proved devastating to the stability of the nation's financial markets. Soon, Enron began parking poorly performing assets in other Raptor structures to avoid recognizing losses on those poor investments. April 16,
2012. LivePlay has a second play running at another theater. For example, it had loans based on stated income, loans to borrowers with low credit scores or high debt-to-income ratios, loans with high LTV ratios, 80/20 or 100 percent loans, and pay-option ARM loans. In addition, the Complaint did not address Countrywide's calculation of the amounts
of the allowances for loan losses on loans held for sale in the years leading up to 2007 or the amounts of Countrywide's provision for representations and warranties on loans it had securitized and sold in the years leading up to 2007. Management expects the delinquency rate in the Company's pay-option loan portfolio to increase to a level consistent.
with the delinquency rate of the rest of the portfolio of loans held for investment as this new product seasons. 7/7/14 9:15 AM 376 References Hays, Kristen, and Anna Driver. Whenever a customary company perk is withdrawn, it typically causes a negative reaction. First, because Peregrine had given the banks recourse, and frequently paid or
repurchased unpaid receivables from them, Peregrine should have accounted for the financing arrangements as loans and left the receivables on its balance sheet. He certified that his examination of the firm's trading process establishment
of hotlines for anonymous whistleblowers. Ruby Company manages the daily operations for the human resources department of Jade Company. Kevin Hannon, a trader who had risen to the top of Enron's trading operations, was appointed Ken Rice's deputy. 4 The POB was replaced by the Public Company Accounting Oversight Board (PCAOB), which
was created by the SOX Act of 2002. We promptly told Enron to correct it" (Powers Report, 2002, p. With reluctance, Dunlap issued another (rather sudden) press release on March 19, 1998. Sunbeam knew that sales of these items would not be continued because the product lines had been dropped. After all the acquisitions, many companies had
been added to WorldCom's collection without any. The relevant notes are presented in Exhibit 9.4. Accounting Lessons from the Mortgage Crisis Going forward, we can take instruction from the mortgage-backed securities crisis that was at the heart of the financial meltdown of 2008. June 4, 2009. As early as mid-June 1997, an article in Barron's
questioned the validity of the sales growth in light of the increase in both accounts receivable and inventories (Laing, 1997). How did the golden goose become the cooked goose? How were credit-default swaps expected to act as hedges against the risk of investing in mortgage-backed securities? 059402_01_REF_p365-382.indd 369 "Munroe
Foundation Receives Largest Single Gift: Al and Judy Dunlap Give $5 Million to Munroe Pediatrics." July 26, 2005. Two plant closings stood out as particularly ill conceived. The entire cycle can then be repeated again and again. Two possible manipulations to look out for are changes regarding policies for the capitalization of software costs and the
capitalization of pre-opening costs. 059402_01_ch9_p325-360.indd 349 7/7/14 9:11 AM 350 Chapter 9 • Mortgage Mayhem 2. subsidiary made payments to Brazilian officials for the purpose of obtaining or retaining business for Tyco. Fannie Mae and Freddie Mac were established to accelerate the funding and issue of mortgage loans. Therefore,
without these transactions with unconsolidated entities, a significant portion of Enron's "profits" would not have existed. These sales should have been reported separately from continuing sales as an infrequent event, but they were recorded as regular ongoing sales. July 9, 2010. Mark in England: The Azurix Account Mark's status began to
diminish with the failure of many of her international power projects. • May 15,1997. However, the school district paid the teachers' salaries of $70,000 and paid Rhodes the net amount of $30,000 in respect of year 1 operations. "Less than fifteen minutes after leaving the boardroom [Clegg] returned to pick up his briefcase. Such improper expense
recognition understates both expenses and liabilities and overstates earnings. At the time, Fastow was a young banker—with a degree from Tufts University—living in Chicago with his wealthy wife, Lea Weingarten, who was originally from Houston. According to generally accepted accounting principles
(GAAP), financial service firms should normally carry the value of their financial instruments on their balance sheets at market price. Extract from Note 8 (2006): Following is a summary of pay-option ARM loan portfolio Total principal balance of pay-option ARM
loans with accumulated negative amortization \$32,866,475 \$26,122,952 \$29,074,810 \$13,973,619 Accumulated capitalized interest (from original loan-to-value ratio (2) Average original FICO score (3) Loans delinquent 90 days or more \$ \$655,453 75\% 78\% 718 90.65\%
financial statements, and intentionally false SEC filings" (qtd. www.benthamscience.com/open. • Loot the company's assets in favor of the major shareholders, directors, or officers. It was also problematic that the internal audit department ultimately reported to the CFO, Scott Sullivan, who was the major originator of the tall tales underlying
signal of CFFO lagging, or falling behind, operating income that would normally indicate an overstatement of revenue. www.thefreelibrary.com. "Nightmare Mortgages," Business Week. It is important to note that pre-Enron accounting rules also required many of Enron's unconsolidated SPEs to be consolidated into Enron's financial statements, but
Enron failed to consolidate many of its now infamous SPEs. If some companies broke the old rules requiring certain off-balance-sheet entities to be consolidated, some will likely be tempted to break the new rules as well. 059402_01_ch1_p025-046.indd 26 7/7/14 8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud 27 Accounting
leverage ratio. LR 17710. (Quotes from AAER 1579, 2002) Scheme #3: Improper Recognition of Vendor Rebates to Reduce Cost of Goods Sold Rite Aid's sales of the vendors' products. In the first guarter of 1997, Sunbeam sold products that it planned to
presents an example of the misuse of multiple-element contracts or contracts or contracts or contracts. • Ronald Assaf resigned after Sensormatic was acquired by Tyco. Signal #4: Precisely Meeting Analysts' Targets Yet again, when a company precisely meets analysts' earnings and revenue expectations quarter after quarter, it is often a sign that things may be too good to
be true. Cooper became convinced that operating expenses were being fraudulently booked as capital assets when Myers tried to stop the inquiry. Underestimation of allowance for Loan Losses Not Growing in Proportion to the Increase in Troubled Loans." Read the extracts from TierOne's financial
smaller than the allowances for loan losses in 2007 could be that even with the increased delinquencies, Countrywide may not have known of the size of the losses that would occur. • Betty Vinson, accounting executive, pleaded guilty to one count of conspiracy to commit
securities fraud and one count of securities fraud. As the new CEO of Enron Development, Mark set out to win power projects all over the world and to extend Enron's international reach. During 2006, Beazer overstated its cumulative reported net income of $389 million by "zeroing out" credit balances in its land inventory accounts
manipulation increased profits in a particular quarter by reducing the charge for 059402_01_ch6_p191-225.indd 194 7/7/14 9:05 AM Chapter 6 • Abracadabra 195 amortization is only appropriate once a production has begun. It becomes stronger still if a significant portion of the company's profit comes
from transactions with these entities, or if there are contingent liabilities in respect of these entities. "AT&T Nears $65 Billion Deal to Buy BellSouth," Wall Street Journal. Developing good character is crucial to consequentialism. He even began to cultivate an image in the press of an executive who did not shy away from cutting jobs or offending
colleagues. In another dangerous maneuver, Enron tried to pacify investors by proposing what was, in effect, death-spiral financing—an arrangement in which a borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the issue of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees to repay a loan amount in the form of the borrower agrees and the borrower agrees a loan amount in the form of the borrower agrees and the borrower agrees a loan amount in the borrower agrees and
unfocused growth of WorldCom with more than 70 uncoordinated acquisitions of other companies. All reports are that this really did apply to everyone. (a) One of the outside directors works for another dried fruit company, Raining Raisins. December 1, 2011. By early November, the stock was trading around $25 per share. Accounting fraud, which is
also called, or financial reporting fraud, is a particular type of fraud that involves the manipulation of financial statements. The total payments for legal fees to this firm were $315, $192 and $154 for the years ended December 31, 2007, 2006 and 2005, respectively. If she is a deontologist, she will act according to the duty she thinks is most
important. U.S. Securities and Exchange Commission Accounting and Auditing Enforcement Release, March 2, 2004. How much goodwill will be recorded in respect of the acquisition of Sub Co.? FOB shipping, 81 A sales agreement term specifying that ownership passes to the customer when the goods are handed over to the shipper for
transportation to the customer. Obviously, the entire exercise had been for the purpose of generating some mark-to-market revaluation profits based on the ludicrous "market value" claim determined by the "outside" sale of 13 percent of Cuiába/EPE to LJM1. 2013. Do you believe that trading a company's stock with the knowledge that the company's
earnings are overstated is unethical? The track record of the companies that Dunlap had managed before joining Sunbeam, most notably Scott Paper, made Andrew Shore a skeptic of Sunbeam's reported "turnaround" right from the start. 6) According to Lawrence and Wells (2004), "Under common law, three elements are required to prove fraud: a
material false statement made with an intent to deceive ..., a victim's reliance on the statement and damages." The Federal Bureau of Investigation (FBI) defines fraud as follows: "The intentional perversion of the truth for the purpose of inducing another person or other entity in reliance upon it to part with something of value or to surrender a legal
right" (www.fbi.gov). To get information on this kind of channel 059402 01 ch3 p069-116.indd 93 7/7/14 9:01 AM 94 Chapter 3 • The Sizzling Saga of Sunbeam stuffing, analysts and investors should scan the 10-Q and 10-K reports and conduct article searches via search engines such as Google and databases such as LexisNexis or ProQuest. GAAI
required TierOne to carry OREO on its books at the lower of the property's book value or fair value, less costs to sell the property. For the second quarter, the company reported restated revenue of $14.9 million, compared to $15.7 million previously reported. "Deregulation," Wall Street Journal. He needed a leader who had slashed costs in
companies, who had cut production plants and products, and who had reported a profit so quickly after a period of losses that it was almost too good to be true. In January 2007, Pember and Sabatino were sentenced to two years of probation and 200 hours of community service (Taub, 2007, Jan. Cases from the SEC Files: Topics in Auditing. The
Commission also found that in January 1998, managers ordered approximately $115 million in unsupported post-closing journal entries, reversing the company's merger reserves. (d) To protect consumers. Further, for Kant, in order for our actions to have moral worth, we must have the right motive, which is to fulfill our duty simply because it is our
them to pay a "$25 million civil penalty." The auditors agreed to a settlement "without admitting or denying the findings" (AAER 2237, 2005). If she is a consequentialist, she will determine right action by the consequentes and effect on the stakeholders, such as the impact it will have on her future employment, as well as the impact on employees,
shareholders, the board of directors, managers, and consumers. The specific mandate of slashing costs was almost too good to be true for Dunlap and he tackled the following: • Many of the contracts were
overvalued. The big stick was looming over every senior executive and manager. September 26, 2008. AHERF's failure to increase its reserve for bad debts caused it to understate its expenses and overstate its income. It did not disclose how accelerated sales in 1997 had drained its current quarter's sales as it disclosed its loss of 52 cents per share
(c) The failure to keep accurate records. On April 3, 2002, WorldCom laid off 3,700 people. It was actually LJM Swap Sub at $56 per share in June 2004. BR-6413. (b) Item I's inventory should be included in Bolt's December 31 inventory, and
Item II's inventory should be excluded from Bolt's December 31 inventory. In the first quarter of the fiscal year, Brace Company discovers that an asset is impaired and the asset will need to be written down by $4 million. (Note: Do not use restated amounts; use amounts as originally stated because analysts did not have restated figures until 2007.)
b. XXVIII, No. 5. When an expense that has a fixed-cost component remains a constant percentage of sales revenue decreases. However, instead of recognizing a charge (as discussed in the first version, in the other side of the entry is a
false reevaluation of the portion of the purchase price that is allocated to goodwill. Therefore, this fraud makes it look as though the company did generate cash in its operating activities, but that it spent that cash on investment banking from investment banking.
which prevented commercial banks from trading in securities. It was equally true that 50 percent of JEDI's profits did belong to Enron and ultimately would be distributed to it or reinvested in JEDI for eventual distribution to Enron. After reading the Enron chapter and the article below: "Andrew Fastow, Former Enron CFO, Talks Ethics with
Students," discuss what you think Fastow's has learned about maintaining ethical business practices. Signal #1: Decrease in Ratio of Sales to Assets (i.e., the asset-turnover ratio), which is the ratio of a business entity's total sales to the total amount that it has
invested in all of its assets). Pressure to achieve numbers. "Fannie Mae Early History." 2004. This deregulation marked what many believe to be the origin of the financial crisis of 2008. The SEC found that Xerox shifted revenue in the following ways: • Xerox shifted revenue from its servicing revenue stream to the box revenue stream, making it
appear as revenue received for physically transferring the equipment to the customer. Accordingly, the company has recorded a non-recurring pre-tax charge of $167 million to write-off the deferred pre-production costs, write-down to fair value certain V-6 diesel engine-related fixed assets that will be abandoned, accrue future lease obligations under
non-cancelable operating leases for certain V-6 diesel engine assembly assets that will not be used by the company, accrue for amounts contractually owed to suppliers related to the V-6 diesel engine program and write-down to fair value certain other assets. All Sunbeam had to do after this dramatic slash-and-burn action was report sales and profit
growth and all would be believed. Probably not," he said. (Quotes from AAER 1393, 2001) 8. However, "Within days of the announcement, the soon-to-be Enteron was a laughing stock." Apparently, the dictionary definition of enteron is "digestive tube." The name was rather "unfortunate, given that Lay's company produced natural gas." So the board
decided to adjust the name to Enron. (d) An increase net income in the period of the acquisition. 2 For a thorough discussion of the signals for this fraud, see the discussion in Chapter 5, "WorldCom Wizardry: From WorldCom to WorldCom to WorldCom to WorldCom to WorldCom." WorldCom to WorldCom to WorldCom to WorldCom."
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Reporting in Financial Statements 361 References 365 Glindex 383 7 059402 01 FM p001-024.indd 7 7/7/14 8:57 AM Contents Preface 17 Instructor Supplements 20 Chapter 1 Introduction to the Problem of Accounting Fraud? 26 Civilence 17 Instructor Supplements 26 Civilence 17 Instructor Supplements 27 Chapter 1 Introduction to the Problem of Accounting Fraud? 26 Civilence 17 Instructor Supplements 27 Chapter 1 Introduction to the Problem of Accounting Fraud? 26 Civilence 17 Instructor Supplements 27 Chapter 1 Introduction to the Problem of Accounting Fraud? 26 Civilence 17 Instructor Supplements 27 Chapter 1 Instructor Supplements 27 Chapter 1 Instructor Supplements 28 Chapter 1 Instructor Supplements 29 Chapter 1 Instructor Supplements 29 Chapter 1 Instructor Supplements 29 Chapter 1 Instructor Supplements 20 Chapte
Accounting Fraud 27 Criminal Accounting Fraud 28 The Extent of Accounting Fraud 29 Accounting Fraud 30 Enron and WorldCom 30 Stock Options 31 External Auditors 31 Boards of Directors 32 Investment Bankers 33 Internal Controls 34 The Sarbanes-Oxley Act of 2002 34 Internal Control
Requirements (Section 404 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 36 Responsibilities of Corporate Management (Section 302 of SOX) 37 Responsibilities of Corporate Management (Section 302 of SOX) 37 Responsibilities of Corporate Management (Section 302 of SOX) 37 Responsibilities of Corporate Management (Section 302 of SOX) 37 Responsibilities of Corporate Management (Section 302 of SOX) 37 Responsibilities (Section 302 of SOX) 37 Responsibilities (
of Ethics 48 The Three Major Normative Ethical Theories 49 Applied Ethics: Ethical Decision-Making Model 57 The Rights-and-Duties Approach to the Decision-Making Model 57 The Justice Approach to the Decision-Making Model 57 The Rights-and-Duties Approach to the Decision-Making Model 58 The Rights-and-Duties Approach to the Decision-Making Model 58 The Rights-and-Duties Approach to the Decision-Making Model 59 The Rights-and-Duties Approach to the Decision-Making Model 50 The Rights-and-Duties Approach to the Decision-Making Model 50 The Rights-Approach to the Decision-Making Model 50 The Rights-A
059402_01_FM_p001-024.indd 9 7/7/14 8:57 AM 10 Contents An Ethical Decision-Making Model for Accountants 58 The American Accounting Association Ethical Decision-Making Model 59 Key Terms 61 • Assignments 61 Former Chief Compliance Officer and Senior Managing Director of Bernard L. May for
the American Accounting Association from a model suggested by H.Q. Langenderfer and J.W. Rockness. In spite of his increasing debacles, in January 2002, the compensation committee authorized another $65 million loan to Ebbers. Further, the profit or gains on these so-called sales were included in operating income. I want you to understand that
this could happen to you, it could happen to you, it could happen to anybody." History of the Rite Aid Crisis Alex Grass founded Rite Aid, a mom-and-pop health and beauty aids store, in Scranton, Pa., in 1962. Although WorldCom's note did not reveal much, often the note will indicate that the company is capitalizing questionable costs. For example, the total expenses rolled
from the first to the second quarter of 1997 was [sic] approximately, there is a strong potential for abuse of mark-to-market accounting system. Interestingly, both men also shared the need to be generous with money gained dubiously. Recalculation of Accounts Receivable
for Comparison with Sales: Consider the following information: The SEC complaint* alleged that there was a plan for Peregrine to write off $26.65 million of channel receivables as "Acquisition Costs and Other" (par. 28) in fiscal 2001. Available online via EBSCOhost database. Some of these customers did return the goods to Sunbeam in later
quarters. For example, some may question spoused fidelity that is rooted in a general sense of duty, rather than in an authentic love that leads a person to stay faithful to his or her spouse. Moreover, to the extent these extremely risky loans were below the loan limits established by the government sponsored entities that purchased these loans
("GSEs"), they would have been reported by Countrywide as prime conforming loans. www.newsstore.fairfax.com.au. What are the constraints? It then increased to only 0.333 percent in 2006. Although he claims that he was 11 years old, he
lived in a "three-story redbrick row house on Garden Street in Hoboken" in New Jersey. Peregrine personnel parked transactions when Peregrine was unable to complete direct sales it was negotiating (or hoping to negotiate) with end-users, but needed revenue to achieve its forecasts. Instead of prorating them, Sunbeam applied these rebates to
decrease cost of goods sold in the period that it signed the rebate contracts. 630 (1958). Sunbeam issued a statement saying that net sales for $253.4 million." It
also stated that the shortfall "if any, would be due to changes in inventory management and order patterns at certain of the company's major retail customers." (Quotes from AAER 1393, 2001) The SEC maintained that the "release inaccurately implied that Sunbeam's lower sales to retailers stemmed from a generalized effort among retailers to
reduce inventory levels, rather than from Sunbeam's 1997 accelerated sales. The company, founded by John J. (a) In 2004, conventional conforming loans dropped to 38.2 percent. (A sunk cost refers to a cost that has already been incurred and the expenditure cannot be reversed by any future decision or action.) As Patrick Mondout explained, "Even
if the L-1011 [TriStar] was 'technically superior' to the DC-10, it cost more to purchase and more per passenger mile than its competitor." Furthermore, Lockheed's initial estimates were that the break-even point on the TriStar would be sales of 300 aircraft. Signal #7: A Company Guaranteeing the Debt of Its SPEs When a company guar- antees the
Enron also guarantees the performance of certain of its unconsolidated affiliates in connection with letters of credit issued on behalf of those unconsolidated affiliates. www.pennlive.com. Income is recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared. If Mac goes ahead and recognized when dividends are declared affiliates.
agreement, which of the following is correct? In addition, these loans were often second mortgages on the same home, making the LTV ratio even higher and the risk of loss or potential default even greater. Bentham's protégé, John Stuart Mill (1806-1873), defined happiness as the presence of pleasure and the absence of pain and believed that
New York Times. The technology for most of the plans had not been perfected (or even developed), there were not nearly enough customers to support the ostentatious plans, and the price of bandwidth would soon plunge. Schapiro (2010) summarized the factors that contributed to both the financial crisis and the demise of Lehman as follows: •
Irresponsible lending practices, which were facilitated by a securitization process that originally was viewed as a risk reduction mechanism; • Excessive reliance on credit ratings by investors; • A wide-spread view that markets were almost always self-correcting and an inadequate appreciation of the risks of deregulation that, in some areas, resulted
risk oversight by companies involved in marketing and purchasing complex financial products; • A siloed financial regulatory framework that lacked the ability to monitor and reduce risks flowing across regulated entities and markets; and • The lack of an adequate statutory framework for the oversight of large investment bank holding companies on
a consolidated basis. "AT&T to Buy BellSouth, Creating Telecom Giant," New York Times. Deloitte. The buyer, not the seller, must request that the transaction be on a bill and hold basis. www.cpajournal.com. With fixed purchase gas for years to
225.indd 197 7/7/14 9:05 AM 198 Chapter 6 • Abracadabra Signals of Fictitious Reporting Scheme #3—Understating Expenses via Capitalization of the Expenses Via Capitalization of the Expenses. For virtue ethics, the driving question is "What kind of
person ought I be?" The answers are inextricably related to one's notion of the human telos (or ultimate purpose) and what defines human flourishing. In addition, the firm paid "another $25 million in an administrative penalty" (Glater, 2005). Second, it had to have a minimum of 3 percent of its equity capital contributed independently of Enron.
Smith, Doug, and Nancy Rivera Brooks. Inventory that increases substantially as a percentage of cost of goods sold as measured, for example, by the inventory-turnover ratio. The relationship was terminated in 2000. 7 059402 01 ch4 p117-143.indd 126 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 127 One of CUC's primary methods of fictitious
revenue reporting was through the use of top-side adjustments. In fact, Rite Aid's net income for the thirteen weeks ended May 30, 1998, was $90.8 million, whereas CFFO for that same period was negative $9.0 million. "CIBC to Pay $2.4 Billion over Enron," Wall Street Journal. This combination of loans made Countrywide's business model
unsustainable once property values stopped rising—and the business model was disastrous when home values fell dramatically. He then used LJM1 to transfer $1.6 million of Enron shares and about $3.75 million in cash into LJM Swap Sub. Considering all these aspects together in Form 10-Q for the third quarter of 2007, the SEC stated the following
The company's Form 10-Q, filed on November 9, 2007, disclosed that Countrywide had taken a $1 billion impairment loss on its loans held for sale and mortgage backed securities, and had taken a $1 billion impairment loss on its loans held for sale and mortgage backed securities.
The final blast of the explosion for Dunlap and CFO Russell Kersh came a few weeks later in the form of an article by Jonathan Laing in Barron's magazine. In fact, in the late 1990s, these companies enjoyed soaring stock prices even when they had negative earnings! This was a situation ripe for exploitation. Ebbers's ego also continued to grow. 800
700 600 500 529 545 FY 2007 FY 2008 661 726 FY 2010 FY 2011 592 400 300 200 100 0 FY 2011 592 400 300 200 100 0 FY 2011." (October 1, 2009-September 30, 2011). It was starting to become clear that there was no communication between the different
departments at WorldCom, resulting in wasteful duplication of resources. www.bloomberg.com. If XYZ goes ahead and secures the backdated order and recognizes it as a bill and hold sale, which of the following is correct? It follows from what I have already said that, in my view, this training and other communication should include communication
about the responsibilities of everyone in the organization regarding identifying, escalating and remediating conflicts of interest. This would cause a great deal of friction within the company. The SEC found that Insignia Solutions allegedly "overstated its Revenue and Net Income... home-page. The SEC's findings alleged, "In FY [fiscal year] 1999, Rite
 Aid failed to record $8.8 million in shrink"3 (AAER 1579, 2002). 059402 01 ch8 p292-324.indd 322 7/7/14 9:10 AM Chapter 8 • Tall Tales 323 approximate market rates. Belden was sentenced (with Jeff Richter) in February 2007 to "two years of court-supervised release," and avoided prison ("Two Enron Traders Avoid Prison," 2007). Accounting
Fraud at the Turn of the Millennium At the turn of the millennium, the nation's attention was focused on the dangers of fictitious financial reports and the shortcomings of the financial reports and the shortcoming financial repor
convicted in January 2005 by a federal jury "of all 12 counts of an indictment: including conspiring to fraudulently inflate reported earnings at Cendant and the PowerPoint presentations are available online at www.pearsonglobaleditions.com/Jackson. (b)
Subprime loans increased from 2004 to 2006. Gatekeepers were ineffective. Grubman joined in spreading the hysteria about Internet traffic and broadband growth. Originally, Enron had issued 3.4 million restricted shares to LJM1. WorldCom gave Arthur Andersen misleading special "MonRevs" to: (a) Conceal the top-side journal-entry adjustments.
Gottlieb, Myron, 192, 193, 195, 198 Government-sponsored enterprises (GSEs), 328, 334, 335 Grass, Alex, 199, 210 Grass, Martin, 199, 203 Great Crash of 1929, 326, 329 Greenberger, Michael, 331 Gross margin percentage, 91, 93t, 203 Sales less the cost of goods sold expressed as a percentage of sales. Bennett, Coleman and Co. . Enron began to
lose colossal amounts of cash on ill-advised projects while it reported "estimated" future profits as current-period profits and hid the mounting debt it incurred to cover the huge amounts of cash it squandered. In certain quarters between 2000 through 2007, however, Beazer, acting through certain officers and employees, manipulated the amounts
recorded in the land inventory accounts in order to manage earnings. 059402 01 ch6 p191-225.indd 203 7/7/14 9:05 AM 204 Chapter 6 • Abracadabra • Franklin C. She had expected Wessex Water to be the silver bullet that would facilitate Azurix's entrance into the water world, after which it could easily buy out privatized utilities or win
contracts to manage utilities for municipalities. August 4, 2012. Williams, Pamela. Signal #2: Restructuring Reserves or reserves resulting from other one-time charges appear in the financial statements upon the arrival of a new CEO, it is an even stronger alert that future expenses are possibly being recognized early with
the creation of improper reserves. October 2, 2002. The plant's superintendent was a cantankerous man who liked to chastise his employees. Adelphia's overstatement of its number of cable subscribers in its 10-K reports: (a) Is an example of a revenue recognition practice that contravenes GAAP. As a registered investment adviser, on at least an
annual basis, BLMIS was required to file forms with the SEC that are used to guide the examination programs of investment advisors. Livent, Inc, was a Canadian theater company that originated in Toronto toward the end of the 1980s. The gathering included internal and external counsel, as well as Russell Kersh (CFO), Robert Gluck (controller), and
Phillip Harlow (external auditor from Arthur Anderson). Highland Holdings, a Rigas family general partnership, were two of the "Rigas Entities" used for many of the related-party transactions between Adelphia and the Rigas clan. Flood, Mary, and Tom Fowler. In Enron's annual financial
statements for 2000, the note titled "Price Risk Management Activities and Financial Instruments" contained a subsection identified as "Securitizations," which stated, "During 2000, gains from sales representing securitizations were $381 million and proceeds were $2,379 million ($545 million of the proceeds related to sales to Whitewing Associates
L.P.)." This meant that close to half of Enron's CFFO came from securitizations of its current assets. The traders were young, egotistical, belligerent, and partial to obscene language. They were rich beyond their wildest dreams—and totally unmanageable. What does Timothy Noonan, former COO and former interim CEO of Rite Aid, see as his
mistakes or failures in Rite Aid's legal and ethical crisis? "Fraudulent Financial Reporting: 1998-2007—An Analysis of U.S. Public Companies," COSO: Committee of Sponsoring Organizations of the Treadway Commission. (c) Virtue ethics, 26. "MF Global: Likely Among the 10 Biggest Bankruptcies Ever." Wall Street Journal. September 21, 2002
Krispy Kreme's internal investigation revealed each of the following accounting errors except: (a) The misallocation of compensation expenses to franchise reacquisition costs. Signal #4 for the scheme of improper use of merger reserves is the occurrence of large, one-time charges in the income statement around the time of the acquisition period.
059402 01 ch1 p025-046.indd 35 7/7/14 8:58 AM 36 Chapter 1 • Introduction to the Problem of Accounting Fraud Internal Control Requirements (Section 404 on the grounds that
compliance was extremely expensive and time-consuming. Larger volume led to lower costs per minute. In the First Interim Report (2002), the Bankruptcy Examiner described WorldCom's efforts to overstate its profits: We have found that as early as at least 1999, responding to the pressures on WorldCom's earnings, management undertook a
succession of measures designed to shore up the Company's income statement. Instructors may download and use each presentation as is or customize the slides. Not that there weren't ethical questions even early in his career. 101. November 1, 2002. 059402 01 ch2 p047-068.indd 53 7/7/14 8:59 AM 54 Chapter 2 • Ethics at Work 7. In August
the California utilities requested that the Federal Energy Regulatory Commission (FERC) conduct an investigation into trading abuses. Prepare the journal entry accounting for the revaluation of the investment 059402_01_ch7_p226-291.indd 283 283 in Saurus Company in the manner that Bronto Company accounted for it. Edward N. October 20,
1999. . At times from 2001 through 2005, Navistar overstated its pre-tax income by a total of approximately $137 million as the result of various instances of misconduct. Daniel J. . "U.S. Drops Criminal Probe of Former Countrywide Chief Angelo Mozilo." Los Angeles Times. The board ceased to exist in May 2002.4 The AICPA also had a peer review
system, but "no Big Five5 firm [had] ever failed a review" (Nanette Byrnes et al., 2002). August 12, 2010. It expanded quickly, trading its stock on NASDAQ in the United States after only a few years. Gadel had substantial involvement in High Wire Networks, Inc. Fitzpatrick, Dan. It is, therefore, unacceptable for a company to merely abide by the
letter of the law if this inadvertently allows for the dissemination of misleading information. For 059402 01 ch5 p144-190.indd 152 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom Wizardry: From WorldCom Wizardry: From WorldCom to Wor
earnings by decreasing depreciation expense in future periods for long-lived assets and, for current assets, by allowing Tyco to record larger profits as the assets were utilized. The Bankruptcy Examiner went on to observe, "WorldCom put extraordinary pressure on itself to meet the expectations of securities analysts. In its restatement, Peregrine
reduced previously reported revenue of $1.34 billion by $509 million, of which at least $259 million was reversed because the underlying transactions lacked substance. It seemed to be lost on Ebbers that his argument of helping WorldCom by taking the loans was merely tautological. Another Delaware company, HFS Incorporated, controlled
franchise brand names in the hotel, real estate brokerage, and car rental industries. When Peregrine booked revenue for the non-binding reseller contracts, and the customers predictably did not pay, receivables—some of them bogus—ballooned on Peregrine's balance sheet. The terms of the Agreement standing alone did not provide for
reimbursement in a manner sufficient to satisfy the requirements for start-up cost deferral pursuant to EITF 99-5. To diminish the amount of the line-cost expenses. At the end of its 2011 fiscal year, the FBI was
investigating 726 cases of corporate fraud in the United States (Figure 1.2). The Great Crash 1929. When questioned about the capitalization of expenses, Gadel acknowledged that some of his accounting methods were aggressive, but denied any wrongdoing. However, Dunlap's sojourn there lasted only about two years and ended badly as well. 43.
Chapter Outline • The Edison Lesson • The Adelphia Account • The BellSouth Warning • Krispy Kreme and the Missing Dough • Key Terms • Ethics at Work • Assignments • Case Study: BUCA, Inc. Enron Energy "hadn't done much more than quess at energy loads its customers would require" (McLean & Elkind, 2004, p. Improper Capitalization of
Expenses or Losses as Assets WORLDCOM 7. Murky Mortgage Corp. October 10, 2005. To avoid detection, he started working in the windowless audit library each day. 65) In the rush to jump on the bandwagons of IPOs, hot dot-coms, and other et-rich-quick schemes, many investment bankers and analysts lost their independ dence, their
impartiality, and their ability to provide their clients with sound and objective investment advice. To grasp the unpleasant yet enticing position that the Sunbeam management team found itself in, one must remember that the year was 1996. Simultaneously with the filing of the complaint, the Commission submitted to the Court, for its approval, a
partial settlement with Peregrine. In addition, Skrypek, as Controller, facilitated the fraudulent conduct that occurred. When a company overstates its earnings via the use of top-side adjustments, the general ledger balances do not reflect the amounts shown in the financial statements. We entered into employee agreements with both our Executive
Vice President and Chief Financial Officer and Chief Operations Officer in December 2002. The Commission found that in FY 1998 and 1999, Rite Aid allegedly "should have recorded an accrued expense of approximately $22 and $33 million respectively" (AAER 1579, 2002). Improper revenue recognition, 117-131 Incorrectly recording a transaction
in the financial statements, indicating that the company Is Involved in Business Transactions with Related Parties Any disclosures in the financial statements that the company is doing transactions with any
major shareholder, officer, or director of the company or any entity owned or controlled by these parties, should alert the reader to be very cautious. By mid-1999, the project had experienced several setbacks. Perpetrators of improper revenue in the
current period is only a "timing" error. AAER 2884. Investment Research Bureau, Inc., 375 U.S. 180, 186-87 (1963), quoting Silver v. It is also important to risk-assess and prioritize which conflicts of interest present the greatest risk to the organization so that resources can be allocated accordingly to mitigate and manage those conflicts effectively
both from a compliance risk and reputation risk perspective. Bentham thought that there was only one good (namely, pleasure) and one evil (namely, pleasure) and one evil (namely, pain). These rights or moral rights or mora
Playbill.com. Astoundingly, Ebbers had pledged or guaranteed hundreds of millions of dollars of WorldCom stock. With Xerox, the CFFO as adjusted for the "sold receivables" revealed that the amount by which CFFO lagged operating income was quite alarming.) In Enron's case, the securitizations occurred together with references to related party
transactions, specially constructed entities, and sales where some ownership interests in the "sold" assets were retained by Enron. Peter Madoff played an essential enabling role in the largest investment fraud in U.S. history. The leading form of consequentialism is
billion in cash. Xerox's bundled sales were improperly recorded in its financial statements because: (a) All of the revenue streams for its leases should have been recorded over the life of the leases. These criteria would affect the evaluation whether an entity is a variable interest entity and, if so, whether the reporting entity should consolidate the
entity being evaluated" (FASB News Release, Nov. The SEC named six senior Adelphia executives in its civil complaint; four of the six were members of the Rigas family (John Rigas and his three sons); the other two were James Brown and Michael Mulcahey, both vice presidents of the company. (b) Bill and hold sales recognize the revenue from a
sale, but fail to recognize the cost of goods sold. 342). Perhaps Price had not followed what had happened to Scott Paper after its reported quick turnaround profits and its rapid sale to Kimberly-Clark. Under this agreement, Blockbuster would persuade the movie studios to give it partnership licensing rights to stream movies directly into private
residences, using Enron's broadband network. The agreement included paying HNG $70 per share for shares that were trading at $48 at the time of the Golden Goose 229 companies. However, the Commission nonetheless found that
Edison committed violations by failing to provide accurate disclosure, thus showing that technical compliance with GAAP in the financial statements will not insulate an issuer from enforcement action. July 30, 2012. Mozilo, Angelo, 335, 336-337, 348 Muckleroy, Mike, 230 Mulcahey, Michael, 300 Multiple-element contracts, 123 Mutual Series
Investment Fund, 71 Myers, David, 166, 174 N NASDAQ (National Association of Securities Dealers Automated Quotations (NASDAQ), 35 National Commission on the Causes of the Financial and Economic Crisis in the United States, 39, 327 National Westminster
Bank, 259 Navistar International Corporation, 215-225 Net accounts receivable, 205 Net asset value, 169 The net amount of the fair value of a business entity's assets less the value of its liabilities and reserves. The Accountant. • John J. dukeemployees.com/deregulation2402.shtml. 059402_01_ch6_p191-225.indd 198 7/7/14 9:05 AM Chapter 6 •
Abracadabra 199 Rite Aid: "The Keys to the Kingdom" Rite Aid is presented mainly as an example of overstating ending inventory values to reduce the cost of goods sold. • Read Litigation Release No. 18205A for Peregrine Systems, Inc., given below. An action is moral if it is performed because it is right, not if it is performed because of its
consequences. However, here, when considering the effects of the decision on others, the most important issue to consider is that of the rights of those concerned; thus, following the rights. Signal #1: Increase in Accounts Receivable as a
Percentage of Sales Examine the accounts receivable-to-sales ratio as measured, for example, by DSO or by days' r evenues outstanding (DRO). After the meeting broke up, the external directors discussed the situation and concluded that it looked like the end of the line for Dunlap—and possibly for Sunbeam as well. (A primary obligor is the party)
that has the ultimate responsibility to pay a vendor or provider of services, the party that has the ultimate obligation to the payment is the primary obligor. 51). It was in this sector of subprime loans that could not be purchased by the
GSEs that Wall Street firms could finally securitize mortgages without competition from the GSEs. Wall Street began working on making securitized subprime bonds more appealing to investors. Galbraith, John Kenneth. Overstated reserves are created in order to use their later release to overstate future periods' earnings. This is a prime signal; if a
company is operating at a profit, why would it not be generating CFFO at a similar pace? This particular accounting operation was completely legal; the debt really was JEDI's and not Enron's. Improper use of restructuring reserves, 84-85, 94-95 Improper valuation of revenue, 129-131 Inadequate allowances for returns, 130 The amount that the
company has set aside in the income statement to allow for customer returns is insufficient. If a company sells a significant portion of its accounts receivable, what adjustments must you make to CFFO before testing whether the financial statement of earnings? She is worried about the repercussions of reporting her
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firm to the SEC. Additional paid-in capital. In view of significant financial losses to investors, corporate fraud does not really affect the U.S. economy and investor confidence. In its report on Deterring and Detecting Financial Reporting Fraud does not really affect the U.S. economy and investors, corporate fraud does not really affect the U.S. economy and investors, corporate fraud does not really affect the U.S. economy and investors, corporate fraud does not really affect the U.S. economy and investors, corporate fraud does not really affect the U.S. economy and investors, corporate fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy and investors fraud does not really affect the U.S. economy 
resulting from an intentional failure to report financial information in accordance with generally accepted accounting principles" (p. 6 Background information in this section is mainly from "Lockheed L-1011 TriStar," "Lockheed L-1011 Tr
production problems or that a big consumer needed more gas, the traders knew that they should invest in options contracts that gave them the right to buy gas in the future at today's price; in other words, they "went long on gas." Bolstered by their success in trading gas, the traders became more inventive financial instruments.
and started regarding themselves as the Enron elite. The investee's assets and liabilities are not consolidated into the investor's group balance sheet. If the reserve or allowance for doubtful debts decreases while the gross amount for receivables increases, consider that a red alert. See Accounting fraud Financial Services Modernization Act, 38, 330
Financial Stability Oversight Council (FSOC), 40 Finnis, John, 51 FirstPoint, 241-242 Fixed costs, 128, 147, 172-173 A category of a business entity's expenses that one would expect to remain constant for a range of volume of units produced or services rendered. The nature of the company's transition from prime conforming loans to prime
nonconforming loans and subprime loans can be seen in Table 9.1, extracted from the SEC's June 4, 2009, Complaint. Enron, of course, argued vehemently against prices were certainly not purely market driven. AAER 2941. 106). As
always, Fastow and his helpers made the actual flow of money rather difficult to follow through a dazzling maze of off-balance-sheet entities. Sensormatic: Madness at Midnight Sensormatic is presented mainly as an example of Improper Timing of Revenue Recognition via holding books open after the close of a reporting period. May 27, 2013. The
judge "declared a mistrial on the dozens of counts on which the jury could not agree" (Flood, 2005, July 21). WorldCom passed journal entries after the close of each quarter: (a) To reduce line costs incurred. xvi) This widespread concern over the lack of transparency in financial statements was certainly not unfounded. L. However, even without
consolidation, the portion of Osprey's debt that was guaranteed by Enron should have been disclosed in the notes to Enron's financial statements as a contingent liability. Skilling currently resides in a Federal Detention Center in Houston, Texas (Inmate Locator). With plants closed, businesses cut, and workers retrenched, combined with little R&D
and sparse maintenance, growth did not increase; inevitably, it fell. The proposed accounting standards update, ASC 810, "provides criteria for a reporting entity to evaluate whether a decision maker is using its power as a principal or an agent. In fact, Lay would eventually unload over $100 million of his Enron stock before it became worthless. Buca
is the holding company for two restaurant chains, Buca di Beppo and Vinny T's of Boston. • Banks and other lenders could make erroneous decisions based on the false information, which could have serious consequences. Ultimately, of course, it turned out that Enron was virtually worthless. • Recognize Adelphia's failure to disclose related-party
transactions and its improper use of non-GAAP transactions. Everyone repeated the chant "Internet 059402_01_ch5_p144-190.indd 155 7/7/14 9:04 AM 156 Chapter 5 • WorldCom Wizardry: From WorldCom to W
turn to gold. Some $62 trillion of that were credit-default swaps (CDSs), whose supercharged growth continues in spite of the crunch. A side letter was signed, giving the reseller generous rights of return. Because everyone had swallowed the fabrication that Internet traffic was doubling every 100 days, WorldCom's competitors were building up
massively expensive bandwidth and data networks. "Xerox Cleared in Criminal Investigation." October 20, 2004. United Press International. In the 1960s, it acquired Oster Co. and added blenders and electric blankets to the array of its then "high-tech" product range. After high school, he attended the University of Missouri, where he studied
economics and apparently became "captivated by theories of how markets and companies work." He went on to complete a master's degree in economics in 1965 and later earned a doctorate from the University of Houston. Marcus, David F., and Sara E. After borrowing this money, Osprey invested $1.5 billion in the specially created partnership of
Whitewing Associates. O ne form of consequentialism is egoism. Jr. 2006. www.theatlantic.com. It also began to accelerate future periods' sales into current periods via the wide array of tricks discussed earlier. A few years after that television interview, several WorldCom officers were found guilty of fraud. For example, sometimes the parent
company recognizes a big one-time expense or restructuring charge with respect to the acquisition. In their September 2012 article discussing the collapse 059402_01_ch1_p025-046.indd 37 7/7/14 8:58 AM 38 Chapter 1 • Introduction to the Problem of Accounting Fraud of Peregrine Financial,
Drawbaugh and Aubin commented: "When Peregrine Financial collapsed earlier this month, a nagging question resurfaced. There were a lot of other things going on." But were there warning signs that he probably should have paid attention to? Lublin. www.sec.gov 059402 01 ch9 p325-360.indd 357 7/7/14 9:11 AM 358 Chapter 9 • Mortgage
Mayhem At December 31 2008 2007 (Dollars in thousands, except per share data) Loans receivable: Net loans (includes loans held for sale of $13,917 and $9,348 at December 31, 2008 and 2007, respectively) 2,782,220 2,976,129 (63,220) Allowance for loan losses Net loans after allowance for loan losses (66,540) 2,719,000 2,909,589 FHLBank
 Topeka stock, at cost 47,011 65,837 Premises and equipment, net 35,316 38,028 Accrued interest receivable 16,886 21,248 Other real estate owned and repossessed assets, net Mortgage servicing rights, net Other assets Total assets 4,722 6,744 14,806 14,530 52,264 54,583 $
3,317,945 $ 3,537,766 From TierOne's 10-K 2008 NOTES: Note 5 Allowance for Loan Losses. Around this time, an Enron team led by a British trader named Louise Kitchen had developed the technology to launch Enron's trading business on the Internet—and so Enron Online was born and went live in November 1999. Required How much did total
sales for Greasy Patties Corporation increase in year 11 over year 10 in dollars and in percentage? January 13, 1999. Pearson published this exclusive edition for the benefit of students outside the United States and Canada. (c) Having reduced documentation or no documentation or no documentation. 225). The Company purchases the products at rates which
management believes approximate market rates. Perhaps the most infamous of the LJM2 deals concerned the formation of four SPEs called the Raptors (numbered Raptor I through Raptor IV). April 20, 1998. Sarno, John, Michael Mueller, and Jennifer Burns. *In early November, 2013, the bench trial for the Basin Water case was concluded, pending
decision by the court. Since his arrival at Enron in 1990, Skilling had been intrigued with the idea of being able to currently record future profits using mark-to-market accounting. www.rismedia.com. (Quotes from Eichenwald, 2005, pp. March 4, 2013. He has a very simplistic view: smaller is better" (qtd. Overstatement of revenue or understatement
of expenses. A repurchase transaction (repo) takes place when a firm sells securities for cash with the understanding that the buyer will return the securities for a specified future date. Why was it allowed to happen? Although creation of such a house cost to complete reserve is proper, in some instances, Beazer, acting through
certain officers and employees, utilized these reserves to manage improperly its earnings. After an investigation into Edison's accounting methods, the U.S. Securities and Exchange Commission (SEC) stated: The teacher salaries and non-instruction expenses paid directly by districts (collectively "District-Paid Expenses") comprise a substantial
portion of the expense of operating Edison schools. Purchase of Inventory—We entered into a vendor relationship with Parasole Restaurant Holdings, Inc., a company owned by two members of our Board, whereby we purchase bread products and a majority of the dessert products offered at our Minneapolis-Saint Paul metropolitan area restaurants.
While there have been sweeping changes to the financial reporting environment (and many agree that SOX has instigated some positive changes), others maintain that SOX may have gone too far in its attempts to clean up the U.S. business landscape. "It requires but little appreciation ... of what happened in this country during the 1920's and 1930's and
to realize how essential it is that the highest ethical standards prevail" in every facet of the securities industry. Of course, what has happened through the financial crisis I believe is yet another reminder of the fundamental need for stronger ethics, risk management and regulatory compliance practices to prevail. The board of directors realized that
bankruptcy was a possibility and they decided to ask Ron Perelman (of Revlon Cosmetics) if he would arrange for Jerry Levin (who had been the CEO of Coleman) to run Sunbeam for a while. 3). Disconnected: Deceit and Betrayal at WorldCom. Upper Saddle River, NJ: Pearson Education. collapsed in 2002" (Johnson, 2007). Enron was going to stream
movies directly into television sets in all homes. Russell Kersh, the chief financial officer of Sunbeam who had the ultimate responsibility for the accounting misstatements, could now just watch as the 059402 01 ch3 p069-116.indd 87 7/7/14 9:01 AM 88 Chapter 3 • The Sizzling Saga of Sunbeam fireworks of falsely stated profits exploded before his
eyes. Eventually, word got out of Enron's near miss, and Lay did what he would do again in 2002 on Enron's final collapse—he denied that he had ever known of the magnitude of the trading operation or its risks. Wins $102m in Subprime Loan Case," Boston Globe. In an examination of the magnitude of the trading operation or its risks. Wins $102m in Subprime Loan Case," Boston Globe. In an examination of the magnitude of the trading operation or its risks.
of alerts was revealed: • In 1998, Enron's consolidated balance sheet already showed a $4.433 billion investment in unconsolidated affiliates. • Lockheed merged with Martin Marietta Corp. The first customer was a realty company, Floyd Franks & Associates, which was owned by Ole Miss's former wide receiver, Floyd Franks
www.dealbook.nytimes.com. Scheme #1: The Use of Fabricated Invoices at Telcel BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in Telcel, and in 1997 BellSouth increased its investment in 1997 Bell
(Fannie Mae and Freddie Mac) to sell MBSs (mortgagebacked securities) backed by FHA and VA loans. Livent's irregular reporting schemes are particularly interesting because they were implemented not only to present a better-looking overall income statement and balance sheet, which inflated the stock price, but also to make particular shows
appear to be more successful than they really were. For example, by 1992, Enron had part ownership in a pipeline in Argentina, and by "early 1994 Mark also had power plants in the Philippines, Guatemala and Guam." Next, Enron Development was "busy laying a pipeline in Columbia . . . The sales-to-PPE ratio is the ratio of a business entity's sales to
the amount it has invested in PPE. Schapiro, Mary L. He realizes profits of $1,829,869. 32. However, if borrowers defaulted and house prices dropped, the CDSs would represent a gigantic liability for the underwriters. This ratio is used as a measure of an entity's ability to meet its interest obligations from the income that it generates. Before May
2000, prices had hovered in the range of $25 - $40 per megawatt hour. In an interview with an executive from Scott Paper, John Byrne was told that "by the end of 1994, it just became a volume-driven plan to pretty up the place for sale.... The Powers Report examined the extent to which Enron used the Raptors to manipulate its reported earnings
during the period from the third quarter of 2000 through the third quarter of 2001: "Transactions with the Raptors during that period allowed Enron to avoid reflecting on its income statements almost $1 billion in losses on its merchant investments." Without these manipulations, Enron's pretax earnings for that period would have been "$429 million,
a decline of 72%." Now the writing was on the wall for all to see (Powers Report, 2002, p. Documentary. www.ey.com. . This amount represents all of the investor funds paid into BLMIS from 1996—the start of Madoff's involvement in the conspiracy—through December 2008. Signals of the Fictitious Reporting Scheme of Understating Bad Debts
Here is an examination of some of the signals indicating that a company may have understated its reserve for bad debts. These registration statements incorporated by reference Buca's financial statements and certain other Commission filings. Maremont, Mark, and Rick Brooks. Sturc, and John D. Therefore, new utility companies and industrial
 plants increasingly used alternative energy sources—such as oil and coal—and avoided gas. In May 1991, Skilling persuaded Enron's audit committee to adopt mark-to-market accounting. For instance, a company that adheres to the rights-and-duties approach may believe that workers have a right to a fair wage even if this standard is higher than the
 legal minimum wage. The credit balances that resulted from the intentional over-allocation were then improperly held open in Beazer's general ledger—acting, in effect, as improper reserves. Bobbit advised them to inform WorldCom's new auditors, KPMG, who had replaced Arthur Andersen after the Enron debacle. In 2008, countless investors held
mortgage backed securities that were backed by mortgage loans. Calculate Brite's inventory turnover ratio for Q2, Q3, and Q4. Big River was designated as Chewco's sole member. • Enron's bizarre projects and how the company managed to burn through billions of dollars. Consider
 "accounts receivable as a percentage of sales" as a possible signal indicating that Peregrine overstated its revenue. These actions were intended to mislead investors and manipulate WorldCom's earnings to keep them in line with estimates by Wall Street analysts. Troubled debt restructurings are loans where the terms have been modified to provide
a reduction or deferral of interest or principal because of deterioration in the borrower's financial position. As part of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities, Beazer typically builds and furnishes between one and five model homes for each of its marketing activities.
Everyone knew the situation was precarious, but very few seemed to understand the seismic shift that was already underway. He summed up his advice by saying, "Sooner or later, you have to make the right choice. • James Brown, former vice president for finance, "pleaded guilty to conspiracy, bank fraud, and wire fraud, [and] was the government's
star witness at trial" (Crawford & Dunbar, 2004). Which of the following statements is correct? www.signonsandiego.com. EdisonLearning, Inc. If the CEO of a company that was sustaining losses suddenly and miraculously reported a profit in the financial statements without dramatically announcing a restructuring plan—a major plan to reorganize
the company in the form of downsizing or changing the company's capital structure or reorganizing the company's debt agreements—this would be a little suspicious. When creating a false reserve, companies often recognize the future expense in the current period as a(n) charge. is cut from the same cloth as Enron's infamous "fat boy" swindle,
which cost the state's ratepayers an estimated $1.4 billion in 2002. Based on this definition of a bubble, house prices in the United States in the early part of the 21st century clearly had foundations of sand—or even quicksand. Other intangible assets, investments and other, net of accumulated amortization of $24,015 and $1,398, respectively. Quite
coincidentally, he received an unexpected call from Sam Segnar, the CEO of InterNorth, asking if Lay was interested in a plan for InterNorth to acquire HNG. The TriStar program was continuing to suffer losses. Key Terms Discounted future cash flows 123 FOB destination 120 Holding books open 119 059402_01_ch4_p117-143.indd 131 Improper
revenue recognition 119 Inadequate allowances for returns 130 Premature revenue recognition 121 Slow shipping 120 Top-side entries 127 7/7/14 9:02 AM 132 Chapter 4 • Hocus Pocus ETHICS AT WORK Questions: a. "Crossing the Line: At Center of Fraud, WorldCom Official Sees Life Unravel," Wall Street Journal. On October 5, 1999, a $129
billion deal was made between WorldCom and Sprint for the purchase of Sprint. • Customers who received "Powerlink," Adelphia's Internet service. Bankruptcy Report #2: Second Interim Report of Neal Batson, Court-Appointed Examiner. 6. Peterson, Jonathon. Ebbers craftily decided that the best way to increase customers and bandwidth—without the bandwidth in the best way to increase customers and bandwidth—without the bandwidth in the band
getting the attention of the big players—was to buy the smaller companies. The business began to grow on the national level as customers all over America lined up to get their first taste of the mouth-watering confection. October 18, 2005. The SEC claimed that, in October 2001 and January 2002, Adelphia made a direct placement to Highland 2000
of $423 million of Adelphia class B shares and notes payable. Celebrates 75 Years." July 1, 2012. It produced 15,000 hair clippers and trimmers a day and its sales were growing. Silverpeak was deliberately chosen because its lines could transmit only a small amount of electricity, with the result that suddenly, California was facing an energy shortage.
and had to buy a large quantity of power at the last minute when prices increased dramatically. Between 1996 and 2002, as a result of these various practices, Tyco made false and misleading statements or omissions in its filings with the Commission and its public statements to investors and analysts. With 20/20 hindsight, he can look back and see
the red flags clearly. These loans were made to a group of Enron's off-balance-sheet entities known as the Whitewing structure and filtered through this structure and filtered through the securities are structured to the securities and filtered through the securities are structured to the securities and filtered through the securities are structured to the secu
the adequacy and effectiveness of those policies and procedures. One of the main goals of Dodd-Frank is to "promote the financial system" (Dodd-Frank is to "promote the financial system" (Dodd-Frank is to "promote the financial system" (Dodd-Frank is to "promote the financial system").
those closer to him were beginning to see him get meaner as he got bigger. However, the allowance for loan losses for all loans held for investment increased by only 38 percent from the end of 2006. September 11, 2007. "Enron Founder Ken Lay Dies," CNN Money. This was not universal, but these breaches stretched from the
ground level to the corporate suites. 11. Center for Audit Quality, Affiliated with the American Institute of CPAs. www.miamitodaynews.com. The family was then taken in by in-laws who lived on a small, meager farm. The assets and liabilities of the affiliate are
 not consolidated into the investor's group balance sheet. (c) To increase transparency. "Upon the filing of the Commission's complaint, and without admitting or denying the allegations in the complaint, Buca consented to the entry of a final judgment ...." (LR 20312, 2007). Downey, Kirstin. CNNMoney.com. • Respond to the Case Study questions. In
addition, Enron is a guarantor on certain liabilities of unconsolidated affiliates and other companies totaling approximately $755 million. While such debt would—for good reason—discourage future hostile takeovers, such large debt also presented significant problems for the company itself. Krispy Kreme consented to the entry of the order "without
admitting or denying the findings." As set out in AAER 2941. Muckleroy fooled the markets by buying 8 million barrels of oil, saying that Enron had a surplus. Leadership consistent with effective ethics and compliance program. 98). Insignia's financial statements reporting a
change in accounting policy, with respect to the method of recognizing the or any changes in estimates for returns, that lead to decreasing the allowance indicates a fictitious reporting scheme. 76, No. 213, pp. Refer to Table 7.4. Signal #2: Cash Flow from Operating Income When CFFO significantly lags behind operating
income, it is a signal that the profit generated may be fictitious or that its recognition has been accelerated. Enron employed misleading transactions, using the infamous prepays, which essentially took out loans on the strength of future contracts and recorded those loans as revenues. Published with permission. In sharp contract to Skilling's trading
operation (which was "asset-lite"), Mark's mandate was to build hard-asset projects such as pipelines, production fields, and other energy sources to supply power plants overseas. In terms of the contract, Ruby receives a fee of $100 per year for each employee on Jade's payroll, less the salary of Jade's bookkeeper, who works full-time on human
resource matters. Which of the following regarding Krispy Kreme's round-trip transactions is not correct? Livent's financial statements also contained some examples of improper capitalization. New York: Doubleday-Random House. • All the employees of the company being audited are stakeholders. Skilling and Mark-to-Market Accounting Once
Skilling had established a trading floor and staffed it with traders selling financial instruments, he started to declare that his division—Enron Finance—was the real business of Enron. The SOX Act also had its quirky side with some unexpected consequences. Countrywide was not the first mortgage lender to introduce the risky pay-option ARM loan. If
the parent pays more than the net value for the company, the excess of the purchase price over the fair value of the net assets is all allocated to goodwill. A new principles-based, converged revenue recognition standard will be adopted, as explained in Chapter 3 of this text. "Fiscal Year 2012 Agency Financial Report." U.S. Securities and Exchange
Commission. In the first round-trip transaction, Krispy Kreme agreed to pay an extra $800,000 for the repurchase of a franchise in return for the franchise in return for the franchise agreeing to purchase a similar amount of doughnut-making equipment from Krispy Kreme shortly before Krispy Kreme repurchase as similar amount of doughnut-making equipment from Krispy Kreme shortly before Krispy Kreme agreed to pay an extra $800,000 for the repurchase of a franchise in return for the franchise in return f
describes fraud as follows: In practice, fraud embraces all the multifarious means that human ingenuity can devise for one person to gain an advantage over another by false suggestion or suppression of the truth. In Adelphia's Annual Report for 2000, a note referred to members of the Rigas family who were "co-borrowers with entities under credit
facilities." A disclosure that intermingling occurs among a company's assets and liabilities and those of its directors, officers, or shareholders should be regarded as an alert that more related-party activity may be occurring than is being disclosed. • Apply the American Accounting Association Ethical Decision-Making Model to dilemmas in the
business world. Improper Classification of WriteOff of Accounts Receivable as "Acquisition Costs": According to the SEC, "[A]s part of the cover up, Peregrine personnel wrote off millions of dollars in uncollectible—primarily sham—receivables, to acquisition related accounts" (LR 18205A). —Albert Einstein According to a recent article in the Boston
Business Journal, "CPAs are sexy" (Pratt, 2013). In a civil settlement with the SEC that same year, and without admitting or denying the allegations, Dunlap agreed to a civil penalty of $500,000 and was prevented from ever again acting as an officer or a director of a public company (LR 17710, 2002). 059402 01 ch6 p191-225.indd 199 7/7/14 9:05
AM 200 Chapter 6 • Abracadabra Rite Aid conducted periodic physical inventory counts at many of its stores. • Sherron Watkins, Enron's now-famous whistle-blower, is a successful writer, speaker, and consultant (Partington, 2012). The next two signals apply to Xerox's specific methods of overstating revenue. Now assume further that you want too
play chess, but there are no chess players on hand, and the only person available is a child who does not know the game. Securities backed by seemingly safer parts of the pooled mortgages could earn AA or AAA ratings, even if the underlying mortgages as a whole were of a lower grade. It would have been evident that something was very wrong.
Signals of the WorldCom Fraud WorldCom Fraud WorldCom overstated its earnings in two major ways. In an attempt to deal with the morass of corporate problems and the huge public outcry, in July 2002, Congress passed the Public Company Accounting Reform and Investor Protection Act of 2002, also known as the Sarbanes-Oxley Act or the SOX Act. Many of the
capitalized invoices did not represent properly 059402 01 ch8 p292-324.indd 319 7/7/14 9:10 AM 320 Chapter 8 • Tall Tales capitalizable expenses. The term consequentialism often refers to all the utilitarian approaches, whether they refer to Mill's strict definition of the good to be maximized or to more flexible definitions. In determining whether
to accept the Offer, the Commission has considered these undertakings. In the first quarter of 1997, quarterly income was inflated "by approximately $2.1 million" (AAER 1393, 2001). Kant's concept of the categorical imperative encompasses a binding moral obligation that must be universal, rational, and impartial. To coax even more sales orders,
Sunbeam increasingly gave customers the right to return goods, yet did not increase the reserve for returns in its accounting records. Organizations are making meaningful changes to embrace this trend and implement leading practices to make their regulatory compliance and risk management programs more effective. "I realize it was very wrong,"
Corigliano reportedly told the judge. Cutting is likely to reduce revenues more than it reduces costs and that will lead to less profit. At the time of Countrywide's inception, securitization did not yet exist, and Countrywide depended on selling its low-risk loans to the GSEs in order to obtain further capital to make more loans. The men stared in silence,
many gas traders went "long" on gas, expecting the price to increase. After its investigations, in 2009, the SEC issued an Accounting and Auditing Enforcement Release against Krispy Kreme in which the Commission found: "In each of the second, third and fourth quarters of fiscal 2004, Krispy Kreme engaged in a round-trip transaction in connection
with the reacquisition of a franchise" (AAER 2941, 2009). It has, however, continued to be plagued with problems (Jore, 2013). Examining this approach in the accounting context, let us consider the case of a manager who knows that the earnings in the financial statements of Company X are overstated and this manager sells his or her shares to a
member of the public who does not know that the earnings are inflated. Al Dunlap was appointed CEO of Sunbeam on July 18, 1996, and the massive restructuring reserves were created in the last quarter of 1996. One of Enron's most spectacular abuses of mark-to-market accounting involved its investment in a private oil and gas exploration
company named Mariner Energy, Inc., that Enron acquired in 1996. 059402_01_ch2_p047-068.indd 48 7/7/14 8:59 AM Chapter 2 • Ethics at Work 49 The Three major normative ethical theories, or schools of thought, according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is most important in the pursuit of morality—namely according to what is morality accordi
it was that all of the institutional gatekeepers failed in their corporate gatekeeping duties. May 12, 1998c. Alliemae. Statement of Income 2002-2003. www.postgazette.com. Children usually go to schools linked to their home addresses; local governments decide how much money they can spend on roads, firehouses, and public safety based on how
much property tax revenue they have; house prices are tied to consumer spending. Misclassification of "prepays" as sales (see Table 1.1 on p. This signal, in itself, should have broadcast a warning to anyone examining that set of Rite Aid's financial statements. For a start, the UUNet Internet employees believed that they were the "technocrats" and they were the "technocrats" and
far superior to the "low-tech" MCI telephone operation proletariats. 212, 213) Using the Rights-and-Duties Approach in the Business World Using this approach to the ethical evaluation of alternatives in a decision-making model, a manager under pressure to publish fraudulent financial statements in order to keep his or her job should consider all
the people whose rights may be affected by this decision. Association of Certified Fraud Examiners. Sometimes items that WorldCom had originally paid. The most egregious entries were in the second quarter of FY 1999. October 24, 2013.
Edison Schools, Adelphia, BellSouth, and Krispy Kreme are presented as example of the failure to record expenses by means of improper deferral. Extract from Speech: Conflicts of Interest and Risk Governance Carlo
V. Under the justice approach, we also can better understand why insider trading is unethical: The parties involved do not have equal information. March 18, 2011. Raub, Timothy. (d) Using bill and hold sales. When WorldCom filed for bankruptcy in the United States at
that time. • Identify and explain the signals in the financial statements that could alert you to the possibility that a company may be overstating its earnings by improper use of acquisition or merger reserves. *** In 2000, the securitizations amount was specified as $2,379 million, which was greater than the amount of the sales of merchant assets and
investments. (a) Overstatement of ending inventory values. Morgan Stanley then approached Sunbeam's internal counsel, Blaine Fogg, who investigated further. However, although Enron owned a great deal of fiberoptic lines, it did not have the connection facilities or the lines to transmit data all the way to its
 customers. 059402 01 ch7 p226-291.indd 284 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 285 FINANCIAL STATEMENTS6 UNITED STATES SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549 Extracts from FORM 10-K Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of
1934 For the fiscal year ended September 31, 2006 BASIN WATER, INC. By 1997, WorldCom's acquisition frenzy became quite manic. Ebbers and Grubman, the telecom analyst, added to the hype, arguing that MCI was worth the inflated price
 "Chainsaw Al" Dunlap as CEO in 1996. This indicates that the parent company has now decided that the net assets acquired were of less value than was originally estimated. That combination of factors was more than a signal; it was a siren. (a) A decrease in the amount of the group's operating income in its consolidated income statement in the
period of the acquisition. Miller, Matt. 059402_01_ch3_p069-116.indd 102 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 103 Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below. Sunbeam 103 Act of 1934, Making Findings, and Imposing a Cease-and-Desist Order ("Order"), as set forth below.
 implements. Ernst & Young LLP. Soon there was an oversupply of gas on the market and Enron, like the other pipeline businesses, had a huge problem. He pointed out, "The prepay technique was a powerful tool employed by Enron to maintain its investment credit grade rating." In fact, the Examiner cited William Brown, who managed Enron's
corporate finance group, as saying that "he understood the amount of any given prepay transaction was determined by the targeted cash flow Enron wanted to show the Rating Agencies." (Quotes from Bankruptcy Report #2, 2003, p. To add to the mix, the traders developed the practice of tranching, which refers to a process of carving up or
separating a pool of mortgages into different classes, or tranches, of securities which absorb different default losses. (c) Bolt should recognize sales in its income statement for both Item I and Item II. Meanwhile, the U.S. telecom industry was in denial. in "SEC Files Amended Complaint," 2003). In order to circumvent GAAP, and deceive its outside
auditor, Beazer, acting through certain officers and employees, caused the model home sale-leaseback written agreements with the Investor Pools to omit any reference to Appreciation Rights and recorded the model home transactions as sale-leasebacks, recognizing home sales revenue in fiscal 2006. Jackson, published by Pearson Education © 2015.
30. The next day WorldCom announced to the world that it had uncovered a massive fraud that had overstated profits by $3.8 billion over the last few years. Al Dunlap arrived to take the helm of Scott Paper in April 1994 and he slashed more than 11,000 jobs in less than one year. September 28, 2007. For instance, a utilitarian framework could
theoretically permit violence toward a marginal group in the name of protecting the majority. 169-170). When Foster returned home to Edmonton for the summer, it was clear to his old high school pal, Bernard Ebbers, that Foster was back to his peak. 31-1999 Mar. As a result of acquiring MCI, WorldCom had two billing systems, so employees would
switch existing customers to the other system and get commission for the new account. In a nutshell, according to the virtue ethicist, possessing the right set of virtues is central to morality because what makes an action right is that it is the action that a virtuous person would take. Are They Living Happily Ever After? Specifically, the Company
recorded $2,500 as gain on sale to affiliate upon the receipt of the shares of Empire common stock by estimating the fair value of such stock based upon concurrent sales of Empire. Although California's electricity situation emerged from crisis
mode in June 2001, concerns about the adequacy of its power supply persist, and the specter of Enron lives on. United States District Court, D
statements contained in press releases and filings with the Securities and Exchange Commission" (Chimicles & Tikellis LLP, 2004). Provides in-depth discussion questions and exercises to encourage a more comprehensive grasp of the material. As a holding company, AHERF did not assume liability for the preexisting debt of its acquired entities
March 2, 2004. www. aicpaconferencematerials.com. Failure to Record Asset Impairments LOCKHEED 13. "Speech by SEC Chairman: Remarks at the National Conference of the Society of Corporate Secretaries and Governance Professionals." Chicago, IL. Thornburgh, the Bankruptcy Examiner, faults primarily Ebbers as well as two members of the National Conference of the Society of Corporate Secretaries and Governance Professionals."
compensation committee for the loan fiasco. (d) Ending regulations that prohibited institutional investors from investing in mortgage-backed securities that were not backed by GSEs. 23. (Refer to the WorldCom Wizardry: From WorldCom wizardry: Fro
merger reserves.) Signals of CUC's Scheme of Reporting Fictitious Revenue The major signals for overstatement of revenues are the same as those discussed in the analysis of Sunbeam's accelerated revenue reporting. Sunbeam was also accused of issuing misleading press releases, as well as conducting ambiguous and deceptive press conferences
and conference calls with analysts. In addition, gas users could contract in advance to make withdrawals (purchases) of gas from Enron at specified prices for future years. This is similar to slicing a pizza into smaller and smaller slices; yes, there are more slices, but they are being reduced to mere slivers. When CUC precisely analysts' earnings and
revenue expectations quarter after quarter, it is often a sign that things may be too good to be true. Enron's Fictitious Financial Reporting Schemes As its plans and projects imploded one after the other, Enron fought to remain afloat the only way it knew: by receiving cash up front in the infamous prepays, reporting false earnings, and keeping its
huge debts off the balance sheet—in short, by fabricating its financial statements. 4 Statement of Financial Accounting Standards No. 48. Why did Sunbeam hire a CEO with a reputation for slashing, burning, and "dumbsizing" companies? Coscarelli, Joe. 059402 01 ch8 p292-324.indd 307 7/7/14 9:10 AM 308 Chapter 8 • Tall Tales rioritized. For
example, WorldCom's line-cost expense was misclassified as PPE. Peregrine misled investors by not including the write-offs in its pro forma operations. Self-dealing, 297-298 Sensormatic Electronics Corporation
118-122 Shelton, E. • Adelphia filed for bankruptcy in June 2002. Through Enron Online, the Enron traders saw the prices that buyers and sellers were offering, and with that advantage, they made a great deal of money on the products they really understood. Apart from Enron's trading income, which was extremely volatile, nothing in Enron's
 financial statements indicated any recurring true operating income to handle this large debt. T 059402 01 ch3 p069-116.indd 97 F 9. Right action corresponds with the act that produces the greatest good for the greatest number. In reality, certain Buca vendors made contributions to the Paisano Partners Conference with the express understanding
that they could bill the contribution amount back to Buca. Business Week summed it up as follows: "Still, in many people's minds the rising importance of consulting has contributed to a decline in auditor skepticism. Signal #1: Decrease in Expense as a Percentage of Sales  
As with any understatement of expenses, you should test each category of
expense as a percentage of sales to see whether it represents a decreasing percentage compared to previous quarters or periods or whether the expense is a smaller percentage of sales than the average for the industry. MacIntyre, Alasdair. Should he have left the company then, he asked. Wessex would have to cut its customer rates by 12 percent. In
 those circumstances the company may record gains and losses on transactions with the SPE and liabilities of the SPE are not included in the company's balance sheet even though the company and the SPE are closely related. • Ignorance or uncertainty? The Bankruptcy Examiner calculated that the remaining assets in the Whitewing
structure had "an estimated aggregate value between $700 million and $1 billion" (Bankruptcy Report #2, 2003, p. According to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting, members of WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting, members of WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounting to the later Indictment against Sullivan and Buford Yates, WorldCom's director of general accounti
increase WorldCom's reported earnings." The staff was told "to make journal entries crediting line cost expense accounts on WorldCom's balance on the general ledger, the staff was further instructed "to debit, in amounts corresponding to the line cost expense accounts." In order for these entries to balance on the general ledger, the staff was further instructed "to debit, in amounts corresponding to the line cost expense accounts." In order for these entries to balance on the general ledger, the staff was further instructed "to debit, in amounts corresponding to the line cost expense accounts." In order for these entries to balance on the general ledger, the staff was further instructed "to debit, in amounts corresponding to the line cost expense accounts." In order for these entries to balance on the general ledger, the staff was further instructed "to debit, in amounts corresponding to the line cost expense accounts." In order for these entries to balance on the general ledger, the staff was further instructed "to debit, in amounts corresponding to the line cost expense accounts." In order for these entries to balance on the general ledger, the staff was further instructed "to debit, in amounts corresponding to the line cost expense accounts." In order for the staff was further instructed "to debit, in amounts corresponding to the line cost expense accounts."
costs, deferred tax liability, and other long-term liabilities." After certain entries were booked in WorldCom's general ledger, it had the "net effect of reducing line costs by approximately $828 million, and thereby increasing WorldCom's publicly reported earnings for the third quarter of 2000 by the same amount." (Quotes from United States of
America v. Reaches $500 Million Settlement In 3 Mortgage-Backed Securities Class Actions." Litigation Resource Community. The Bankruptcy Examiner described the scam: The Examiner understands that, beginning in the first quarter of 2001, Mr. Sullivan directed that hundreds of millions of line-cost expenses be capitalized, subtracting them from
what otherwise would have been expenses against the company's earnings for the successive quarter, and disguising most of those reductions by transferring them as additions to the company's fixed assets. This step will often reveal an unanticipated result of major importance. That gave Cooper a little more leeway to go beyond the Internal Audit
Department's narrow operational audit and into the realm of a financial audit. Worse was coming. Furthermore, the same SEC Release claimed that Fastow also "received a share of Chewco's profits as kickbacks from Kopper." Special Purpose Entity #3: LJM1 Emboldened by the ease with which he had manipulated JEDI and Chewco to enhance
 Enron's balance sheet, Fastow concocted another SPE that he dubbed LJM, a name based on the initials of the first names of his wife, Lea, and children, Jeffrey and Matthew. Our backbone doubles every 3.7 months. By a startling fluke, two months after the sale of his McLeod shares, Ebbers saw to it that WorldCom employed SSB as its investment
bank when it merged with MFS Communications Company. A shift toward riskier loans • 80/20 loans • Undocumented loans • Nonconforming loans • Subprime loans Riskier loans could also be revealed by disclosure of
an increase in the percentage of loans made to borrowers with low FICA scores or to b
of the franchise. Balive, Marcelo, with Javier Castano and Plinio Garrido. Finally, High Wire occasionally submitted invoices to Buca in the round amount of $100,000 with no description of the goods or services provided. 9 % p e r c e n t o f Countrywide's loan originations were conforming. It is easy to find this signal. In this ploy, the parent company
at the time of the acquisition, creates a purchase acquisition accounting reserve. Payments to Independent Contractors 31. "Looking at it in retrospect, yes," he admitted. (a) To increase the number of audit firms. XYZ Co. is an equipment leasing company. • Business schools from coast to coast established courses in business ethics and corporate
governance issues. This was a large carrot that caused many executives, even those who despised Dunlap from past experience, to join him again for the Sunbeam turnaround. The PCAOB "ended more than 100 years of self-regulation by the public company audit profession" ("The Sarbanes-Oxley Act at 10," 2012). On that date, in an agreement
 letter, WorldCom formally protected its interest in Ebbers's WorldCom stock as security for his loans. According to Kant's deontological view of ethics, if that murderer asks you if you know the whereabouts of the person in hiding, you are duty bound not to lie. Homeownership, 327-328, 335 Housing bubble, 326-334, 347 Housing market, 38 Houston
Natural Gas (HNG), 227, 228-229 Hudspeth, Robert, 145, 157 Human rights, 57-58 I IDB Communications, Inc., 150 IFRS (international financial reporting standards), 35 Impaired asset, 207 An asset whose carrying value is less than its fair or recoverable value. www.boston.com. Hiltzik, Michael. • Corporate Crime Enforcement: More generally,
SOX legislation also increased penalties for other corporate crimes beyond the certification of false financial statements. Further, regarding Swap Sub, the CEO of Arthur Andersen, which was Enron's external audit firm, stated in Congressional testimony on December 12, 2001, "When we reviewed this transaction again in October 2001, we
determined that our team's initial judgment that the 3 percent test was met was in error. For instance Rule 206(4)-7 under the Investment advisors and investment companies. Juris, Stephen. Gilley. Another form of these improperly-booked
rebates were so-called "signing bonuses" that Navistar demanded and received from certain suppliers in exchange for awarding new business. Instead, Edison has inaccurately stated in its Management Discussion and Analysis [MD&A] that it 'receives' all Per Pupil Funding" (AAER 1555, 2002). Tillson, Tamsen. CNNMoney. (b) Caused it to overstate
its earnings. Second, the payment arrangements as set out in the contract were outrageously favorable to Enron but were not really feasible considering that in India, the government often had to forgive many unpaid electricity bills. Finally, it is important to think proactively when it comes to conflicts of interest. Understatement of expenses via
deferral of expenses. Regarding the use of certain of its land inventory accounts, describe and explain how Beazer Homes created a cookie-jar reserve that it later reversed into earnings. (a) Enron disclosed that it guaranteed the performance of certain of its unconsolidated affiliates in connection with letters of credit. In 1996, then-President Billian that it guaranteed the performance of certain of its unconsolidated affiliates in connection with letters of credit. In 1996, then-President Billian that it guaranteed the performance of certain of its unconsolidated affiliates in connection with letters of credit. In 1996, then-President Billian that it guaranteed the performance of certain of its unconsolidated affiliates in connection with letters of credit.
Clinton appointed attorney Brooksley Born as head of the CFTC. 17) What deceptive companies especially like to do is recognize the future expense in the current period as a special charge. 059402 01 ch3 p069-116.indd 71 7/7/14 9:01 AM 72 Chapter 3 • The Sizzling Saga of Sunbeam The History of Al Dunlap Al Dunlap's history—both his
personal background and his business history of downsizing businesses that later suffered—was the first warning sign that alerted analysts, such as Andrew Shore of the PaineWebber, Inc. http:// magazines.aba.com/timag. "That's why there's an ethics program at Tuck." Fastow, by most accounts a brilliant man, is proof that the road to ignominy isage.
most often not well marked. • Bernard Ebbers, former WorldCom CEO, was convicted of securities fraud, conspiracy to commit securities fraud, and false filings on March 17, 2005. Joseph L. While Enron's management certainly manipulated the reporting of its debt, they never controlled the debt itself; indeed, eventually it mastered all of them. In
 addition, due to certain laws and regulations in some states, additional funding may be required. This general signal of the quality and track record of company leaders should be combined with an analysis of whether the business plan outlined by management is likely to produce the reported results as published in the financial statements. At that
point, Enron wanted CALPERS to enter into a second, even larger joint venture. T 11. Noked, Noam. It could be anyone's. In 2003 Peregrine restated its financial results for those quarters. It serves to describe the company's financial
statements. 059402 01 ch5 p144-190 indd 150 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to the companies. "Adelphia
Auditor Agrees to Pay $50 Million Into Investors' Fund," New York Times. T 059402 01 ch1 p025-046.indd 44 6. It told the story of how, in 1994, Professors Lee Tom Perry and Eric L. He realizes profits of $2,155,000. (b) Edison's recognition practices contravened GAAP. Notre Dame, IN: University of Notre Dame Press. In anticipation of the
institution of these proceedings, Respondent has submitted an Offer of Settlement (the "Offer") which the Commission has determined to accept. "Study Predicts Foreclosure for 1 in 5 Subprime Loans," New York Times. Stanford Encyclopedia of Philosophy. By the end of Q3 of 2012, LivePlay had amortized an accumulated amount of $75,000 of the
scenery production costs of $300,000. Mark also lobbied over the head of the local MSEB in India, and in December 1993, the Indian government signed a contract for the first phase of the 20-year project. The back-dated order would be for goods with a selling price of $10,000 and a cost of $4,000. 21609. Lockheed Martin Website. Or on the other
hand, the same framework could also be critical of someone spending $4 on gourmet coffee in the United States when the $4 could save lives if given to provide electrolytes to children in impoverished countries. However, the company obtained additional funding, and in January 2006, Nasdag agreed that Insignia could "continue to be listed on the
exchange" (Graebner, 2006). Dunlap walked into the meeting and began a "monologue on himself and the company." He then turned to the gathering of company officers and began ranting and raving, admonishing them for the "demise of Sunbeam!" He kept repeating that the "old Sunbeam is over today. Chapter 7 "Annual Partnership Meeting."
October 26, 2000. Masters, Brooke A., and Ben White. On August 3, 2005, he was sentenced to ten years in prison and ordered to pay $3.27 billion to Cendant (Haigh, 2005). Exhibit 4.1 Extracts from Peregrine's Quarterly Financial Statements (in Thousands) 1999–200110 Mar. (d) Brace can write down the asset by $4 million evenly over three
 years, beginning in the year that it discovered that the asset was impaired. The results are beneficial for the whole. What the world didn't know was that WorldCom's merger with Sprint was its last hope for continuing its Ponzi-type scheme. After the September meeting in the Hattiesburg coffee shop, Ebbers, Singleton, Fields, and Waldron contacted
friends and acquaintances. Maybe word had leaked that some managers were in shock about what they considered to be economic suicide: the closing of plants that they regarded as efficient low-cost/high-profit facilities. What is the amount of revenue that 059402_01_ch8_p292-324.indd 313 313 Ruby Company should report on its income statement
for last year in terms of EITF 01-14? In 1996, the Telecommunications Act was passed, allowing for more competition in the local telephone market. Be very cautious when notes are unclear as to one or more of the entity; • The name of the entity; • The 
nature of the entity—whether it is a partnership, a trust, a joint venture, or an established corporation. What do you do? Revenue for servicing the equipment. You remind her that under Dodd-Frank, a whistleblower: (a) Is eligible to receive money from a $453 billion SEC fund. To identify the nature of virtue, Alasdair MacIntyre sought a common
thread in five different views of the nature of virtue over the ages. Not everyone believed that the failure of Azurix was entirely Mark's fault. . T 059402 01 ch4 p117-143.indd 132 6. Which of the following is not one of the cardinal virtues? On December 20, 2006, an article in the New York Times cited a report that projected a high foreclosure rate
for subprime mortgages. (a) Smaller public companies will be exempt from Section 404(b) of the SOX Act—remains another difficult issue with no easy answers in a free market economy. "Inside the Countrywide Lending Spree," New York Times. Identify some
of these signals in Tyco's financial statements (given below) and explain how your findings could have been misusing reserves-that could have been misusing reserves-that could have been misusing reserves-that could have been misusing reserves. The Business Journal. They did not have children,
but both were dog enthusiasts and their German shepherds were their pride and joy. Without admitting or denying the allegations in the Commission's complaint, Tyco has consented to the entry of a final judgment permanently enjoining it from violating Section 17(a) of the Securities Act of 1933, Sections 10(b), 13(a), 13(b)(2)(A), 13(b) (2)(B), 14(a), 13(b)(2)(B), 14(a), 14(a)
and 30A(a) of the Securities Exchange Act Rules 10b-5, 12b-20, 13a-1, 13b-21, and 14a-9. "Supreme Court Rejects Former Enron Chief's Latest Appeal," DealBook. This caused problems for some U.S. companies with European subsidiaries because very few countries in Europe have laws that protect whistleblowers
Under GAAP, TierOne was required to assess probable losses associated with its impaired loans and record those losses in its allowance for loan and lease losses the resources in a productive and efficient way. An accountant from
Arthur Andersen, Enron's auditors, apparently commented later, "No one pounded the table and said these guys are crooks. Panella said, "During today's plea, Peter Madoff admitted to his role in a fraud scheme that harmed the savings of inventory piling
 up. Cameron, explained that downsizing must be an improvement process, not a target: "If they merely cut positions and lack of competitiveness, the problems are still going to be there even after downsizing
sometimes necessary, when it is done badly, it is a most unproductive and futile method of trying to improve a company. www.cnbc.com.ChristianScience Monitor, Scherer, Ron. October 18, 2002. Think about your own life in light of these two positions. In addition, the board's compensation committee came under scrutiny for its "generosity" to the
CEO, Bernard Ebbers. The improper use of special purpose entities (or unconsolidated off-balance sheet entities), which it used to: • Understate debt • Overstate earnings via: • Related-party sales • Loans disguised as sales 226 1 General background information in this chapter is from Bankruptcy Report #1 (2002), Bankruptcy Report #2 (2003),
Bankruptcy Report #3 (2003), Bryce (2002), Eichenwald (2005), Erron Timeline (2005), Gruley and Smith (2002), McLean and Elkind (2004), Powers Report (2002), and Swartz and Watkins (2003). "Former Enron CEO Skilling's Sentence Cut to 14 Years," Reuters. 43, No. 4, 488-518. "If they had, they might have seen that Sunbeam was coming
apart." (Quotes from Schifrin, 1998) During a meeting with financial analysts on May 11, Sunbeam announced another downsizing plan. The next month Buford Yates, Betty Vinson, and Troy Normand pleaded guilty to charges of fraud, conspiracy, and securities fraud. The Smartest Guys in the Room: The Amazing Rise and Scandalous Fall of Enron
In company memos, Enron officials admitted the company often did not have the power it was selling and then buying back." (Quotes from Berthelson & Martin, 2003) Another loophole pounced upon by unscrupulous suppliers and traders was based on the regulation cap that existed for the price of Californian power—but not for power from outside
California. Fastow now had an ownership interest in LJM1, and he could get financing for the SPE via Enron's stock and Enron's guarantees of loans. Beazer also understated its cumulative net loss for the first two quarters of fiscal 2007 by $1 million. Signal #1: Assets and Liabilities of Unconsolidated Affiliates or SPEs Increasing Significantly
When the amount of the assets and liabilities of unconsol- idated affiliates or SPEs grows significantly, it is an indication that the company could be using off-balance-sheet entities to hide its debt or overstate its earnings. SEC Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002. Hedonism uses pleasure (and/or pain) to judge the
consequences of an action. Forbes's case ended in a mistrial. Undeterred but without full access to the accounting computer system, the internal audit team became creative and surreptitious in their search for the information they needed. Signal #6: Retaining Partial Ownership in Assets Sold When a company has sales in which it retains any of
the ownership interests in the asset sold, it is a signal that the company may actually be obtaining a loan and classifying it as a sale. The most common form of death-spiral financing is a loan in which the terms specify that the amount must be repaid at a specified date by the issue of the borrower's shares. The compensation committee, again, did the
unbelievable for their (rather tarnished) golden-boy Ebbers. "Clearing the Fog." April 17, 2008. The auditor could be sued or face other legal action for fraudulently issuing an audit opinion. In Sensormatic's case, it is normal for the company to operate at a profit even if it is not generating a CFFO at a similar pace. At the time of Big Company's
acquisition of Small Company, Big Company believed that Small Company's reserve for doubtful debts was correctly stated at $30,000. Rigas, was also a provider of local telephone services. Also, overstating the amount of the purchase price attributed to goodwill means a company can understate its assets and create false reserves to release back
into earnings as previously described. They refused and left. The golden goose appeared to be sleek and plump. Consolidated Statements of Operations (in thousands, except per share amounts) Year Ended September 30 2007 2006 2005 As Restated Total revenue Home construction and land sales expenses Inventory impairments and option contract
abandonments Gross (loss) profit Selling, general and administrative expenses Depreciation and amortization Goodwill impairment Operating (loss) income taxes (Benefit from) provision for income taxes Net (loss) income $3,490,819 2,944,385
611,864 \$ 5,356,504 4,061,118 44,175 \$ 4,992,973 3,766,517 5,511 (65,430) 454,122 33,594 52,755 (605,901) (35,154) 7,775 (633,280) (222,207) \$ (411,073) 1,251,211 629,322 42,425 — 579,464 1,343 2,450 583,257 214,421 \$ 368,836 1,220,945 548,161 36,068 130,235 506,481 5,021 1,712 513,214 237,315 \$ 275,899 8 Extracted from 10-K
filings for Beazer Homes, USA, Inc. In addition to misleading financial statements, Adelphia also disseminated other misleading information. However, the plan faltered when gas producers were not as keen to lock themselves into long-term selling prices. www.bizjournals.com. Explain why sudden unexplained increases in gross margin as a
percentage of sales could be an indication that a company is understating its cost of goods sold. Following this announcement, the company's shares fell 35 percent, from $3.88 to $2.53, in one day. Adjustments that increase goodwill in a later period with respect to an earlier acquisition. Edison Schools is presented in the chapter as an example of: (a)
Failure to disclose related-party transactions. On December 31, 2012, Power Company shares to P2 for a 90 percent share in P2. In fact, "some of the $900 million of the money Fastow had raised [for Azurix] was paid right back to Enron." Even though Azurix burned
through cash with its own ill-fated projects and mismanaged development costs, some claimed that Enron was not particularly supportive of Azurix and that—in the battle to gain control of Enron—the "entire expensive episode had all been a grand conspiracy" to depose Rebecca Mark. LR 22014. To add to the cunning subterfuge, when the value of
Enron stock owned by JEDI fell by approximately $94 million in 2001, "Enron did not record its share of this loss" (2002, p. On August 28, a further seven-count indictment was filed against Sullivan, charging him with conspiracy to boost earnings by hiding operating expenses. In an attempt to avoid such takeovers, the two companies merged in 1985,
and Lay became CEO of the new conglomerate, which took the name of Enron. 13 Extracted from 10-K filings for Peregrine Systems, Inc. Andrew Shore was vindicated and congratulated. His attention was particularly riveted on the natural gas segment of the energy sector. This level of vaqueness about offbalance-sheet entities should have been a
strong alert that Enron may have been concealing something. In order to defer expenses, Livent moved expenses from one asset account to another where the
                                                                                                                                                                                                                                     could be delayed. For several years Enron kept growing through reckless and unsuccessful global projects by: (a) Constantly overstating its earning and understating its debts.
Sensormatic overstated its earnings by creating false reserves in one period and reversing those reserves into earnings in future periods. Ruby's other administrative expenses were $10,000. Both were driven and troubled, yet charismatic. Profits that are made via trading depend on the volatility of prices and on betting successfully on the direction of
the price changes. (a) Operating income would be overstated by $6,000, and sales would be overstated by $10,000. Release No. 17627. 059402_01_ch9_p325-360.indd 352 (b) Is a financial instrument that gives the holder of the instrument that gives the holder of the instrument that gives the holder of the instrument from the writer of the instrument if investments in specified loans suffer defaults or
losses. In an interview after the trial, jurors revealed that "Lay's credibility was severely damaged by evidence that he quietly sold $70 million in Enron stock . . . The best hope for reform, Shreve *Originally published on Oct. Venue is proper in this Court pursuant to Section 22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Section 27 of the
Exchange Act [15 U.S.C. §78aa]. Furthermore, the exposé assumed that, at the time, Sunbeam had also written down property, plant, and equipment values to reduce future depreciation expenses and observed that earnings were boosted by a drop in Sunbeam's allowance for doubtful debts and discounts. Signal #4: Notes to Financial Statements
Reveal Capitalizing of Costs That Are Usually Expensed A fourth signal of misclassifying expenses as assets occurs when the notes to the financial statements indicate that the company is capitalizing costs that other companies—in the same industry—expense. T T F 8. This was, however, the opposite of what the European press was saying after
WorldCom outbid BT. As mentioned earlier, although SPEs often take the form of partnerships, they can also be structured as corporations, trusts, or joint ventures. 14). In 1996, Sunbeam was sustaining losses. The House Cost to Complete Accounts. Bad debts that are not written off represent operating profit that is recognized in the income
statement but that should be expensed because the profit will not be liquidated. 21327. Signal #4: Related Party Transactions with Unconsolidated SPEs When the note to the financial statements on "Related Party Transactions" refers to transactions with unconsolidated affiliates.
especially specifically constructed entities, such as partnerships or trusts, it is a signal that the company may be using the SPEs to hide debt or generate fictitious profits. 4 By convention, 90 days is usually used as the approximate number of days in a period of one quarter (or three months). The situation was further complicated by the fact that
Kopper later transferred his controlling interest to his partner but continued to run Chewco. There are several accounts of Kenneth Lay sitting on a tractor as a child and gazing at the downtown buildings he saw in the distance, daydreaming about inhabiting that remote world that seemed so elusive. In 1997, he told Red Herring, "WorldCom is at the
intersection of everything we like—no carrier in the world can offer the integrated set of facilities that it does. There were regulations that prohibited institutional investors, such as pension funds and insurance companies, from investing in mortgage-backed securities that were not backed by GSEs. As a result, investors had little appetite for free-
enterprise mortgage-backed securities. Enron's energy trading—especially its gas trading on the manipulated California electricity market—generated profits. It comprises the value of beginning inventory plus net purchases or cost of goods
manufactured minus the value of ending inventory. In addition, the SEC requires disclosure as to whether at least one financial expert on that committee. Sunbeam created big write-down of assets and for future losses or liabilities in order to boost future profits. Available
online via ProQuest database. In spite of all their attempts, there was nothing Enron executives could do to resuscitate the project. As leaders in your organizations, that responsibility starts with you. The company currently "has 694 stores across the United States and in 20 foreign countries" ("Krispy Kreme Doughnuts Inc. 059402 01 ch6 p191-
225.indd 216 7/7/14 9:06 AM Chapter 6 • Abracadabra 217 SUMMARY FROM AAER 3165 1. In its examination of company management, the committee members stated, "It appears that Livengood was too focused on meeting and exceeding Wall Street expectations and gave too little attention to establishing the appropriate tone from the top" (p.
The number of the shares to be issued depends on the market value of the Khaan shares on each repayment date. Which of the following gatekeepers or gatekeeping functions was not identified by WorldCom's Bankruptcy Examiner as having failed WorldCom in some way? Yet, Enron's accounting, cash-flow reporting and disclosure of transactions
were inappropriate. abuse of, 296-298 note, in financial statements, 269-270, 299 Repurchase (Repo 105) transactions, 333 Reserves cookie-jar, 82, 154, 158-159 decrease in, 95 false, 159-160, 169-170 improper use of restructuring, 84-85, 94-95 inventory, 203 understatement of, for bad debts, 204-206 warranty, 218-220 Residual values, 123-124
Restructuring charges, 209 Restructuring plan, 75 A major plan to reorganize a company's debt agreements. If housing prices continued to go up, there would be an asset in the form of the house to back loans of up to 100 percent of the value of the
house. Schapiro, Mary L., Chairman. $15 million to be controlled by limited partnerships, and Enron itself was to invest 3.4 million shares of restricted stock valued at about $246 million. Documents from the first quarter of 2000—Rite Aid overstated its net income and that
former senior management failed to disclose material information, including related-party transactions in 1999 (AAER 1579, 2002). As the company began to attract a vast amount of investment money, John Sidgmore, from General Electric, was appointed CEO. Cumulative translation adjustment Treasury stock, at cost Total stockholders' equity
198,353\ 134,112\ \$2,003,766\ \$523,430\ \$\ 36,024\ 200,886\ 86,653\ 1,731\ 325,294\ 8,299\ 17,197\ 884\ 262,327\ 614,001\ \$\ 19,850\ 49,064\ 36,779\ 74\ 105,767\ 4,556\ -1,257\ -111,580\ --160\ 2,342,235\ (917,104)\ (22,151)\ (3,950)\ (9,425)\ 1,389,765\ \$2,003,766\ 110\ 480,957\ (64,863)\ (678)\ (666)\ (3,010)\ 411,850\ \$523,430\ (continued)\ 059402\ 01\ ch4\ p117
143 indd 140 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 141 Extracts from FORM 10-K12 For the fiscal year ended March 31, 1999 PEREGRINE SYSTEMS, INC. When Sunbeam lost White, it lost an extremely talented and capable manager and a crucial amount of "company energy" (gtd. As set forth above, Beazer made untrue statements of
material facts in registration statements, periodic reports filed with the Commission and other investor disclosures or omitted to state therein, in the light of the circumstances under which they were made, from being materially misleading. "No Bottom Yet for Flailing Financials."
321Gold.com. "No question, your reputation gets damaged," he said. October 10, 2012. Dunlap's next job was at Max Phillips and Sons, where he was allegedly fired after less than two months for his ill manners and insolence toward his boss. Given that Enron was involved in all aspects of the gas business, Enron's traders had extremely useful
information to trade on. "Ex-WorldCom Exec Gets a Year in Prison." August 9, 2005. For information on investigations of suspected bribery or corruption involving a company, search news reports in the U.S. press and the press of the foreign countries in which the company operates. In order to continue to meet or exceed analysts' expectations for its
quarterly net income and EPS, Beazer began reversing many of its previously created, improper reserves. July 29, 2012. In Table 7.6, an examination of Enron's times-interest-earned ratio over the period 1998 to 2000 clearly reveals that Enron had too much debt. At Zettler AG, a security monitoring company Tyco acquired, adjustments were made to
Zettler's books that overstated its liabilities and resulted in Tyco's operating income in subsequent reporting periods being increased by approximately $6.6 million. On June 6, 2006, Beazer issued and sold a $275 million aggregate amount of its 8.125% Senior Notes due 2016 in a private placement to qualified institutional buyers pursuant to Rule
144A and in offshore transactions pursuant to Regulation S. U.S. Securities and Exchange Commission, May 1, 2003. 28-32) How Wall Street Embraced Sunbeam's Downsizing at the time was that it was effective and that Dunlap had
the world's leading reputation for downsizing. ii. Graebner, Lynn. When asked specifically about relationships with vendors like High Wire and EDP, Gadel responded that no problems with these relationships existed. 059402 01 ch6 p191-225.indd 193 7/7/14 9:05 AM 194 Chapter 6 • Abracadabra company officials had a special computer program
designed that would enable accounting personnel to "override the accounting system without a paper or transaction trail." The Commission also maintained, "This process had the effect of falsifying the books, records and accounts of the company so completely that the adjustments appeared as original transactions, and no trace of the actual original
entries remained in the company's general ledger." (Quotes from AAER 1095, 1999) By means of the previously mentioned schemes, Livent's financial statements understated expenses in three ways: • They erased expense invoices from the accounting system. Gruley, Bryan, and Rebecca Smith. Chapter 2 Arel, Barbara, Cathy A.
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059402_01_ch4_p117-143.indd 121 7/7/14 9:02 AM 122 Chapter 4 • Hocus Pocus customers and will turn into cash, the next period as accounts receivable instead of turning into cash. The analyst and short-seller Richard Grubman picked
up this delay as a signal of problems at Enron. The company understated some expenses to different assets (and moved expenses to different assets or theatrical shows) to amortize them more slowly and defer recognition of the expenses. UUNet, 151, 156 Uzzi, Donald, 79, 87 7/7/14 9:17 AM
Glindex 401 V Variable costs, 76, 173 Variable interest entities (VIEs), 266 Vendor rebates, 200-201, 217-218 Vendors, on accounts payable list, 197 VIE (variable interest entity), 266 Vinson, Betty, 165, 166, 174 Virtue ethics, 49, 51-53 An agent-centered normative ethics, 49, 51-53 An agent-centered normative ethics, 49, 51-54 Virtue ethics, 49, 51-54 Virtue ethics, 49, 51-55 Virtue ethics, 49, 51-55 Virtue ethics, 49, 51-55 Virtue ethics, 49, 51-55 Virtue ethics, 49, 51-56 Virtue ethics, 
of the executives who were found guilty in recent financial frauds had considered their own families' future suffering or public humiliation—it is possible that some of them may have paused long enough to remember the reasons society made
laws against issuing fraudulent financial statements in particular and against fraud in general. Action Co. by $10,000 at the time of acquisition and to overstate goodwill by a corresponding amount. It is even more alarming because the "Merchant Investment" note in 1998 shows that the majority of the
merchant investments, totaling $1.859 billion, were held through unconsolidated affiliates, including partnerships. Goldsmith, Jill. He "'was the most unpleasant, personally repulsive businessman I ever met in my life' said a New York image consultant who Dunlap had wanted to hire" (qtd. Just two years later, CFO Magazine gave Fastow an award for
capital structure management. It becomes clear that Enron's own stock was invested in these partnerships from the statements, an alarming number of new affiliates were added to the list of "Unconsolidated Equity Affiliates," including the
now infamous Whitewing structure that hid enormous debt and losses from Enron's financial statements. He had to find a way around the GAAP rules. Signals of the Failure to Record Asset Impairment of an asset. He said he wasn't the
one directing the fraud, "but maybe I should've been doing something about it and said, 'We are not going to do it.'" There is no doubt, he said, that he made some bad decisions. in Jenkins, 1997). • John Tate, former COO of Krispy Kreme, left the company in August 2004 "to pursue another opportunity" (qtd. One model that is particularly useful for
the accounting profession is the American Accounting Association Decision- Making Model. FCPA violations often consist of bribery, (a) In which the amounts involved are not in themselves material. Understatement of Reserves for Bad Debts and Overstatement of Accounts Receivable ALLEGHENY 11. 059402 01 ch4 p117-143.indd 124 7/7/14 9:02
AM Chapter 4 • Hocus Pocus 125 profit. • Scott Sullivan, former WorldCom CFO, pleaded guilty to three fraud-related counts on March 2, 2004. AAER 1495. (c) As "assets from price risk management activities" and "liabilities from price risk management activities fro
sheet. in 1995 to form one of the largest aerospace companies in the world. April 9, 1997. As the issuance of mortgages, CDSs, MBSs, and CDOs mushroomed during the 1990s, the Commodity Futures Trading Commission (CFTC) increasingly thought that it should oversee the trading of CDSs on the grounds that these derivatives amounted to futures
contracts. If the parent company is not paying for supernormal profits, what is it paying for when it pays more for a company than the value of its net assets? The vehicle that Krispy Kreme used to implement its round-trip transaction stunts was the reacquisition of franchise rights. Which of the following reserve accounts was not examined by
WorldCom's Bankruptcy Examiner? The SEC also began an investigation of Sunbeam in June. One should keep a skeptical watch to see whether these profits materialize. The loans, which were disguised as sales, overstated Enron's sales, earnings, and CFFO. Der Hovanesian, Mara. "Bank of America Must Face Mortgage Fraud Trial: Judge,
Bloomberg. This reserve, called a "house cost to complete" reserve, was established to cover any known and unknown expenses that Beazer might incur on the sold house after the close, such as outstanding invoices, unbudgeted cost overruns, minor repairs or final cosmetic touchups. Lay married his college sweetheart, Judith, in 1966, and within a
few years, they were the proud parents of a son and daughter. In addition, the investigation uncovered several accounting practices at Adelphia that were similar to the improper accounting practices at Enron. However, the cost of bandwidth depended on the
volume. Key Terms Acquisition 146 Economic goodwill 153 Fixed cost 147 Goodwill 153 Fixed cost 147 Goodwill 153 Improper capitalization of expenses 161 Merger 156 Net asset value 169 Sales-to-PPE ratio 170 ETHICS AT WORK Questions: a. "John Rigas Guilty of Conspiracy: Adelphia Founder, Son, Found Guilty on Some
Charges That They Looted Cable Company," CNN/Money. Mark believed that this privatization would lead to deregulation, as had happened with the gas industry, and there would be a great deal of money to be made in water. Case No. 02-13533 (AJG). What Is Accounting Fraud? (c) Decreasing its reported CFFO. Some of the main areas of corporate
governance reform as a result of the SOX Act of 2002 included the following: • Independence and oversight of external auditors • Audit committees • Independence of boards of directors • Independence of analysts
 • Corporate crime enforcement 6 Information in this section is mainly from Glassman (2005). Upon default of loans on which the full interest had to be paid monthly, little or no loss would be incurred on foreclosure as long as house prices did not fall. In 2007, Deloitte & Touche "agreed to pay $167.5 million to settle a case with a trust that was
formed after Adelphia Communications Corp. If the allowance for home loan losses does not increase when the value of the houses decrease, it is a signal that the company may be
                                                                                                                                                                                                                                 the allowance for loan losses. Which ethical theory discussed in this chapter is most likely to take intention into account? Bronto then used markto-market
accounting to revalue its shares in Saurus through its income statement to the market price on the grounds that the put-option "hedge" gave it the certainty that the value of the shares would not fall below $50,000. (United States of America v. Let me close with a few brief observations for senior managers and independent directors, www.fasb.org
"Ten Things about Financial Statement Fraud—Third Edition: A Review of SEC Enforcement Releases, 2000-2008," Deloitte Forensic Center. The ratio did not deteriorate over the period, but the 059402 01 ch7 p226-291.indd 274 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 275 Table 7.6 Times-Interest-Earned Ratio:*
1998-2000 1998 1999 2000 NI** $ 703 M*** $ 893 M* $ 979 M Interest Expense*** $ 550 M $ 656 M $ 838 M Income Tax $ 1,428 M $ 1,653 M $ 2,251 M 2.596 2.520 2.686 NI before I&T***** Interest * Times interest earned is most often calculated as net income before interest and taxation
expenses, divided by the interest expense. "How to Fix Corporate Governance," Business Week. 059402 01 ch8 p292-324.indd 298 7/7/14 9:10 AM Chapter 8 • Tall Tales 299 Signals of Adelphia's Fictitious Reporting Scheme #1—Improper Use and Misleading Disclosure of Related-Party Transactions Here is an examination of some of the signals
indicating that a company may have engaged in improper related-party transactions. New York: Crown Publishing/Random House. Neither Gadel nor Skrypek took any remedial action based on the issues raised at the meeting. In retrospect, these justifications were just a manifestation of his lack of character, he admitted. He also bought huge
ranches and other properties, as well as a 60-foot yacht that he appropriately called ACQUASITION. 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 34. May 15-16, San Francisco; May 28-29, New York City. Support your answer. The Lehman Bankruptcy Examiner (2010) described Lehman's accounting for Repo 105
transactions as follows: Lehman accounted for Repo 105 transactions as "sales" as opposed to financing transactions based upon the overcollateralization or higher than normal haircut in a Repo 105 transactions as "sales" as opposed to financing transaction or higher than normal haircut in a Repo 105 transaction and Moral Intensity on a
Financial Reporting Decision," Journal of Business Ethics. The Powers Report (2002, p. (a) The packing case should not be included in Ace's December 31 inventory balance. To Linda Harrison, the development editor, thanks
for the helpful and insightful feedback. There were just too many potential problems. However, it did not take long before "the new o wners said that they had uncovered accounting irregularities" (Simon, 2002). understated its allowance for returns" for the first and second quarters of 1996.9 Insignia had a standard practice of recording an
allowance for returns—in respect of inventory at resellers—that exceeded an estimated 45 days of sales: "In effect, Insignia understated the amount of inventory held by its resellers, this would cause it to understate its allowance from its gross revenue to arrive at revenue." Therefore, if Insignia understated the amount of inventory held by its resellers, this would cause it to understate its allowance from its gross revenue to arrive at revenue."
revenue. See supra n. "SEC Charges Adelphia and Rips Family with Massive Financial Fraud." June 24, 2002. T F 9. Anderson, Sarah, Scott Klinger, and Sam Pizzigati. "India's Woes Reflected in Bid to Restart Old Enron Plant." New York Times. September 9, 2003. 059402 01 ch6 p191-225.indd 206 7/7/14 9:05 AM Chapter 6 • Abracadabra 207 As
gas prices soared in the 1970s and demand for air travel fell, it became clear that there was only enough traffic for one of the new plane designs. He already had the ambiguous traits of coming across either as painfully shy or as powerfully driven and charismatic. Additionally, these side-letters stated that Navistar would refund the rebate accordingly
if the Company failed to make sufficient future purchases. In his role as CCO, Madoff created false and misleading BLMIS compliance documents, as well as false reports that were filed with the U.S. Securities and Exchange Commission (SEC) that materially misstated the nature and scope of BLMIS's Investment Advisory (IA) business. Just a few
months after moving to Enron, Skilling contacted a company of headhunters to locate such a person. The logic behind this signal, of course, is that companies invest their capacity to produce goods and services and earn revenue with these goods and services. Wall Street analysts often recommended to investors shares of
companies that have an investment banking relationship with their firm; yet privately, analysts deride the same companies. The FCPA was passed in 1977 to combat improper dealings by U.S. companies operating in foreign countries, and the act is enforced by both the Department of Justice (DOJ) and the SEC. The Commission's findings quoted
Insignia's own revenue recognition policy as stating that revenue is "recognized upon shipment of $1.2 million to a reseller. 059402_01_ch2_p047-
068.indd 62 (c) Requires the decision maker's own primary principles or values. Signal #4: High Interest Expense in Relation to Income—it is an indication that the company may not
be able to continue to pay its interest and, ultimately, may not be able to repay its debt. In total, they received approximately $7.5 million (net) cash during the term of the investment, plus an additional $3 million cash payment at closing" (2002, p. At least when the Titanic went down . . . Therefore, the signals for the various methods of understating
cost of goods are considered together. Signal #4: Cash Flow from Operations Lagging Behind Operations costs to fixed assets. Latham & Watkin's Litigation Department. Comment on the above ratios. "Rigas
Brown Case in Judge's Hands." June 23, 2012. However, the combination of what amounted to the gutting of the company with the restructuring plan, together with Wall Street's lukewarm reaction to it, caused some of the management to become skeptical. 059402_01_ch9_p325-360.indd 333 7/7/14 9:11 AM 334 Chapter 9 • Mortgage Mayhem It
must be emphasized that, in May 2012, the SEC ended their investigation of Lehman and did not recommend any action against them. At McIntosh and Stanaway's insistence, R&Q included these "below-the-line" items in its warranty reserve calculation, and these components consistently reduced the warranty reserve. "Testimony Concerning the
Lehman Brothers Examiner's Report," U.S. Securities and Exchange Commission. Undeterred, Fastow simply got Barclays Bank to provide the $11.4 million via ostensible "equity loans" (ownership capital that is at risk). For instance, inventory as a percentage of cost of goods sold increases when cost of goods sold in understated. The warranty
reserve-setting process should have been governed by accounting rules related to contingent liabilities. First, when Salomon initially allotted IPO shares to Ebbers, besides not being one of its good customers, he was not a customer at all. 5. In fact, the Web weavers were already spinning another yarn. Whether or not the plot existed, Jeffrey Skilling
retained his position as future king of Enron, and at the end of 2000, Rebecca Mark was cut loose. Each period this huge debt led to large interest expenses relative to Enron's income. The turmoil was not confined to Ebbers's boardroom. SKRYPEK, Defendants. InterNorth's borrowing of hundreds of millions of dollars to acquire HNG for $2.4 billion,
combined with other debt, meant that the newly formed Enron began its life with over $4 billion of debt. 31). A number of prescription medications had been ordered but not collected by Rite Aid customers. • The new case studies presented at the end of the chapters give students the valuable opportunity to examine original documents and look for
evidence of accounting manipulation in a real-world company. May 1, 2013. When patents are issued, the Company amortizes the patent cost over the life of the patent, usually 17 years. The remaining approximately $79 million resulted from improper accounting for certain warranty reserves and deferred expenses. He had also heard stories of
turmoil within Sunbeam. November 25, 2005. August 2, 2009. Concerning Arthur Andersen, the Examiner's Third and Final Report went further than earlier reports and concluded that Arthur Andersen allegedly failed "to carry out the kinds of substantive tests that were warranted by the risks." Even though it was "significantly deceived," Andersen
lacked due "professional skepticism" (p. There was little liaison between the companies, and much of the work was duplicated. It estimates that the second play, Dogs, will run until December 31, 2014. PARAGRAPHS 17-22 FROM AAER 3165: Vendor Rebates 17. He is a certified public accountant who holds an inactive license to practice in
Minnesota. To coax even more orders for sales, Sunbeam increasingly gave customers the right to return goods, yet Sunbeam did not increase the for in the its accounting records. For this reason, lenders charge higher interest rates for future borrowing, exacerbating the problem of the high cost of capital. Haigh, Susan. Brown, former vice chair and
chief counsel, was found guilty of playing a major role in the Rite Aid dase. Although Rite Aid did understatement of cost of goods sold, which refers to the cost of inventory sold during the period. Signal #3: Write-Off of Costs Previously Capitalized One must be on the alert
for aggressive capitalization of costs when a company writes off costs that were f ormerly capitalized. This signal becomes an even greater alert if there is evidence (as disclosed in notes to the financial statements) that the company has created SPEs and that the company is also involved in related-party transactions. Death-spiral financing refers to
an arrangement with another party that if certain circumstances occur, the company must compensate the other party for a required amount in the form of the issue of the company's own stock. Schapiro (2010) describes the summer of 2008 as follows: That July, against the backdrop of the growing subprime crisis, the federal government seized
control of what was then the second-largest bank to fail in United States history. Sunbeam apparently did not realize that there is a crucial difference between a downsizing and a dumbsizing. The point, of course, is that if Ebbers had not pledged vast quantities of company stock for personal loans and guarantees, neither he nor the WorldCom shares
would have had to be rescued. On October 1, 2012, in its books and records, LivePlay transfers the scenery assets of $225,000 from the Cat Trap to the Dogs production in order to avoid fully writing off the asset in its 2012 financial statements. • 6,000 Adelphia home-security subscribers. Collateralized debt obligations consist of home loans pooled
with other loans, such as car loans, such as car loans, credit card debt, and student loans, which are carved into tranches and securitized by the investment banks. 58). Internal e-mails sent in March and April 2006 show that senior officers at Countrywide were aware of the risks associated with these essentially 100 percent loans, which are carved into tranches and securitized by the investment banks. 58).
under exceptions to underwriting compliance guidelines. Causey, Richard, 277 CDO (collateralized debt obligation), 234, 330 CDS (credit-default swap), 330–332 Cendant Corporation, 174 Center for Audit Quality, 27 CFFO (cash flow from operations) CFTC (Commodity Futures Trading Commission), 41, 331 CFTF (Corporate Fraud Task Force), 40
Channel stuffing, 83 Persuading customers to place a later period's orders in the current period total costs by the greatest amount, which is not achieved by just cutting production facilities and employees or cutting R&D and marketing costs. in Wilczynski, 2013). 84) In
the first quarter of 2000, Enron decided to sell its Rhythms shares and unwind the Rhythms put option. Washington D.C. October 1. 059402_01_ch7_p226-291.indd 231 7/7/14 9:08 AM 232 Chapter 7 • Enron and the Tale of the Golden Goose In 1987, on the advice of Skilling, Enron launched its Gas Bank. (Qtd. An Overview of Krispy Kreme's
Operational Problems Apart from the accounting errors, the company was beset by other problems, which included the following: • Growth was too rapid, with the addition of too many new franchised stores at the expense of existing franchises. In one instance, "Vendor Rebate 1," a supplier executed a form rebate letter drafted by Navistar, and
dated October 19, 2004, that said the supplier was providing the Company a $2.1 million rebate based on "2004 volume and piece price productivity improvements." However, the very next day, October 20, 2004, the parties executed a side-letter arrangement that specifically stated that half of the rebate was based on pulling forward productivity
improvements expected to be achieved in 2005. Ebbers paid $4 million for 059402_01_ch5_p144-190.indd 167 7/7/14 9:04 AM 168 Chapter 5 • WorldCom Wizardry: From WorldCom Wizar
059402_01_ch7_p226-291.indd 265 7/7/14 9:08 AM 266 Chapter 7 • Enron and the Tale of the Golden Goose 2014. There are what Sterba has called "in persona" right is the right to have a loan repaid or the right to have a promise kept. April 15
2007. Muola, Paul, and Mathew Padilla. From the fourth quarter of 2001 through the fourth quarter of 2002, the Company incurred substantial start-up costs relating to the Agreement, including expenses developing the engine, constructing a plant in Huntsville, Alabama, and leasing engine assembly assets. In addition, any news reports of large
warehouses being built to house the company's inventory (as was the case with Sunbeam) or of a company's major customers building warehouses or "reclamation centers" to store unsold or returnable inventory should be taken as huge red flags that companies may have accelerated current sales at the expense of future sales. Large amounts
allocated to goodwill on the acquisition of companies that do not have a supernormal return on assets, and the acquisition is not followed by supernormal returns on assets. Sunbeam recorded rebates on future purchases as deductions from the current period's cost of goods sold expense. Following the announcements of the additional loss provisions
TierOne's stock price dropped more than 70 percent. After that, the Lays never really regained their financial footing. Then in the financial records, the company would recognize this revenue at the time of the shipment to its own warehouse. The trick, however, was that Enron had no intention of consolidating the SPE. However, there were plans to
move the plant to Mexico to save on labor costs, even though transport costs would be higher and moving the factory would cost millions of dollars. If you ask the child to learn chess, he or she will probably refuse. New York: Portfolio. University of California Office of the President: News Release. 059402 01 ch7 p226-291.indd 291 7/7/14 9:09 AM
Chapter 8 Tall Tales Learning Objectives After studying this chapter, you should be able to: • Describe Edison Schools' inadequate disclosure in the management discussion and analysis (MD&A) section of its financial statements. 059402_01_ch7_p226-291.indd 263 7/7/14 9:08 AM 264 Chapter 7 • Enron and the Tale of the Golden Goose Basic
Prepay Structure Current Pay Future Delivery Future Delivery Future Pay Futur
buck. (c) Stipulated that securities that were backed by a pool of loans had to be categorized into different tranches, or classes, that absorbed different tranches, or classes, that absorbed different tranches, or classes, that absorbed different default losses. A company is required to release fiscal reports in order to clearly and truthfully reveal its financial condition. Management expects the delinquency rate in the Company's pay-option
ARM loan portfolio to increase as this product seasons. Tyco International, Ltd. The reversal of the reserve creates net income that can be used to meet earnings shortfalls. Why or why not? www.deloitte.com. In May 2006, the jury "convicted Skilling of one count of conspiracy, 12 counts of [securities] fraud, five counts of making false statements and
one count of insider trading. In addition, JEDI was required by Enron and Chewco to pay Chewco a management fee from 1998 to 2003. The customers weren't paying ahead of time for sales that were recorded ahead of time, and worse still, their inventories of Sunbeam products were building up steadily. Provides short, end-of-chapter questions to
ascertain that students have understood the material. It's a process by which they agree to abide by SEC rules and provide critical systemic risk information that can give regulators better insight into their practices. A 2007 article in the New York Times reported, "Last year, for example, the profit margins Countrywide generated on subprime loans
that it sold to investors were 1.84 percent, versus 1.07 percent on prime loans." According to former Countrywide employees, "[T]he company's commission structure rewarded sales representatives for making risky, high-cost loans." According to former Countrywide employees, "[T]he company's commission structure rewarded sales representatives for making risky, high-cost loans." According to former Countrywide employees, "[T]he company's commission structure rewarded sales representatives for making risky, high-cost loans." According to former Countrywide employees, "[T]he company's commission structure rewarded sales representatives for making risky, high-cost loans." According to former Countrywide employees, "[T]he company's commission structure rewarded sales representatives for making risky, high-cost loans." According to former Countrywide employees, "[T]he company's commission structure rewarded sales representatives for making risky, high-cost loans." According to former Countrywide employees, "[T]he company's commission structure rewarded sales representatives for making risky, high-cost loans." According to former Countrywide employees, "[T]he company's commission structure rewarded sales representatives for making risky, high-cost loans." According to former control of the company of
borrower took out a loan for 80 percent of the purchase price, with the result that at the time of purchase price, with the result that at the time of purchase price, with the result that at the time of purchase price, with the result that at the time of purchase price of the house. Ebbers's basketball scholarship, however, ended after one year, when his Achilles tendon was torn by a broken bottle during a
fight with some local thugs. The announcement represented the first crack in the armor of Sunbeam's façade as a company whose sales and earnings were growing rapidly. In June 1999, even though Azurix was in 059402 01 ch7 p226-291.indd 238 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 239 a state of disarray and not
developing enough new business, its initial public offering (IPO) raised $695 million (Smith & Lucchetti, 2000). At a conference in Las Vegas in mid-2001, Skilling quipped at California's expense: "What's the difference between California and the Titanic? In fact, the company's true earnings were approximately $15 million. http:// blog.aicpa.org. (c)
80/20 loans. The justice decision-making approach in the business world treats all persons in the same category in the
                                                                                                                                                              manner. These transactions were nonbinding sales of Peregrine software with the understanding—reflected in secret side agreements—that the resellers were not obligated to pay Peregrine. The Justice Approach to the
Decision-Making Model The third approach presented by Fleming for analyzing ethical dilemmas in the decisionmaking model in order to identify the right or the moral action is the justice approach. Wall Street was enthralled at the thought that this slash-and-burn downsizing specialist would quickly boost Sunbeam's stock price as he had boosted
previous companies' share prices—irrespective of what had happened to those companies after the guick boost. To test for the lack of accrual in Livent's case, (a) It is compulsory to check which regular vendor is not on the accounts payable list. Also, the higher the debt relative to profits and to equity, the higher the risk that the debtor will default on
Accounting Oversight Board (PCAOB), 34, 35, 37 Public Oversight Board (POB), 32 Put option, 255 A financial instrument that gives the owner the right to sell an ownership interest, usually an equity interest in another company sells ten airplanes in the following year and the cost office on a specified price on a specified future date.

If the company sells ten airplanes in the following year and the cost office on a specified price on a specified future date.
goods sold is $2 million per airplane excluding development costs, how much must the company recognize as its total cost of goods sold for the year? Like the period just before the Great Depression of 1929, "those simpler souls who had thought the market might go up forever" (Galbraith, 1997, p. 14. Conversely, the cap on customer rates would
decrease customers' incentives to use less power at times when the utilities were paying more for power. (d) This would have no effect on operating income but would increase CFFO by $6,000. As Peter Madoff has admitted today, he was one of the chief architects. All students are required to take at least one mini-course that explores the complex
ethical and social challenges of business. In later periods, Beazer eliminated these cost to complete reserves, resulting in inflated profits for those periods. In its press release on January 28, 1998, Sunbeam maintained that the increase in its sales was a "clear indication that [Sunbeam's] strategy is working." The SEC subsequently concluded that
Answer the following questions with T for true or F for false for more practice with key terms and concepts from this chapter. In October, the committee authorized another $25 million guarantee with respect to Ebbers's personal bank loans. One might wonder whether the financial statements had been fraudulently reported, or at least one might
question whether they had been erroneously reported. Sensormatic's own at the end of the current period to Sensormatic's own at the end of the current period to Sensormatic's own at the end of the current period. Describe the most important characteristics or qualities of an effective internal audit department and explain whether or not these qualities were missing in
practices of the company. Company Overview. Net income, 124-125 New York Stock Exchange (NYSE), 35 NI (net income), 124-125 O59402 01 GLINDEX p383-401.indd 395 Nitec Paper Corp., 73 Nonconforming loans, 335-336 See also Subprime loans Non-consolidation rule, 265 Non-GAAP financial measures, 298 Measures that are not included
in the income statement, balance sheet, or statement of cash flows from operations that are calculated in accordance with GAAP. Winokur, Jr. www.sec.gov. At this point, however, because of the company's increasing conviction that it
understood and into areas where it had little expertise. (Prepays refer to transactions in terms of contract to a third party for the amount of the future cash
selling price, less a discount. In its income statement, Rite Aid should have applied the rebate only to purchases relating to goods that it had already sold. Smith, Randall. In the second quarter of 2001. Internal Audit is the third line of defense and is
responsible for providing independent verification and assurance that controls are in place and operating effectively to address conflicts of interest. Further, Enron recognized the up-front amount of $10 million paid in 1997 as revenue for that period instead of spreading the fee for the guarantee over the life of the guarantee. Together with an
additional five investors, the nine of them incorporated LDDS with about $600,000 capital. A credit-default swap: (a) Is a form of derivative financial instrument. This signal of an overstatement of sales (and the accompanying profit) is easy to spot. Cooper, having decided not to accept Andersen's answer, reported it to Max Bobbit, head of the auditional five investors, the nine of them incorporated LDDS with about $600,000 capital. A credit-default swap: (a) Is a form of derivative financial instrument.
committee, on March 6, 2002. Those who remained and accepted their unfeasible target numbers had to find ways to meet them. i. 059402_01_ch5_p144-190.indd 177 177 27. Because the top-side entries were not entered in the company's general ledger, something had to be done to align retained earnings with the 059402_01_ch4_p117-143.indd
127 7/7/14 9:02 AM 128 Chapter 4 • Hocus Pocus annual financial statements. Buca improperly capitalized at least $4.67 million in repair and maintenance expenses, as well as general and administrative expenses, but it "expected sales to exceed
those of the first quarter of 1997." It also blamed the shortfall on "changes in inventory management and order patterns." Sunbeam's customers had so much inventory from 1997's accelerated sales that it was catching up with them in 1998. "SEC Settles Action with BellSouth," Triangle Business Journal. 20. 7. "WorldCom's Finance Chief Says He
Lied." Los Angeles Times. In addition, accounting-related litigation is on the upswing. Act so that you treat humanity, whether in your own person or in that Countrywide did not disclose the extent of the changes to its underwriting guidelines
Choose a known vendor and trace that vendor to the list of accounts payable that supports the amount listed on the final record, the balance sheet. If an investor puts down 20 percent of the original outlay. This agency remains
committed to protecting worker benefit plans from those who would defraud them for personal gain." According to the superseding information to which Madoff pled and other court filings: Madoff was employed at BLMIS from 1965 through at least December 11, 2008. In early April, Shore received a tip-off that Sunbeam's head of domestic sales,
Donald Uzzi, had been fired. • Identify and explain the signals in financial statements that could have alerted one to Enron's use of special purpose entities (SPEs) to overstate earnings and understate debt. This management agreement terminated during 1999. 30 $10,000 $ 2 Required a. March 19, 2012. (a) The structure of its internal audit
department. He wore a wire when talking to other principals in the case. The real story of Enron goes back to May 1985, when InterNorth—the company that owned the biggest and best gas-pipeline network in the United States—merged with Houston Natural Gas (HNG), whose ancestry went back to the Houston Oil Company that had been formed in
1901. The company was "taken private" in fall 2003 ("Edison Schools Leaving Publicly Traded Stage," 2003). On November 10, 2009, TierOne filed another Form 8-K reporting an additional loan loss provision of $120.2 million for the third quarter of 2009. "Flying by Their Seats." July 29, 1985. Explain why these adjustments should be made. (d)
Being a stated income loan. According to the Financial Crisis Inquiry Report (2011), AIG's model for its CDSs "did not estimate the market value of the underlying securities" (p. 059402 01 ch8 p292-324.indd 321 7/7/14 9:10 AM 322 Chapter 8 • Tall Tales certain management and administrative services. This act—sponsored by Senator Paul
Sarbanes (D-Md.) and Congressman Michael Oxley (R-Ohio)—was intended to restore what Senator Sarbanes called the "fundamental integrity" of U.S. markets. There would be repaid.
Rite Aid simply put through journal entries decreasing cost of goods sold and decreasing accounts payable by a corresponding amount. Signal #2: Change in Policy for Capitalization of Costs. Be on the alert for notes to the financial statements that indicate that there has been a change in policy regarding the capitalization of Costs.
AND STOCKHOLDERS' EQUITY Current Liabilities: Accounts payble Accrued expenses Current portion of deferred revenue, net of current portion Other long-term debt, net of current portion. Bernard J. One of the things that had swayed some of the
mangers in their decision to work for Dunlap in spite of their aversion to him was that he had done with Scott Paper. According to an article in Forbes magazine, "Seven months ago Al Dunlap declared victory in
turning around ... Sunbeam.... When he turned 11, "his family moved to Hasbrouck Heights, New Jersey, a middle-class community of peaceful, tree-lined streets and modest homes." Both Dunlap's sister and his high school football coach reported that he had always had a temper, "an aggressive one," according to his coach. Signal #1: Lower Asset-
Turnover Ratio Compare the asset-turnover ratio and the fixed-asset turnover ratio of the company to that of the company to that of the company to that of the company itself in previous periods. ** Prior to FY 2011, this category was reported as Issuer Reporting and Disclosure and included FCPA actions, which are now tracked separately from Financial Fraud/Issuer
Disclosure actions. • There were various speculative trading on the bet that electricity prices would fall when, in fact, prices rose astronomically. WorldCom is presented mainly as an example of: • Improper accounting in connection with business combinations via improper use of acquisition or merger reserves
and improper asset valuation • Improper capitalization of expenses 1 Background information in this chapter is mainly from Jeter (2002), Krim (2002), Second Interim Report of Dick Thornburgh (2003), and Third and Final Report of Dick Thornburgh (2004). Buca essentially funded High
Wire's operations, despite the fact that High Wire provided most of its services to companies other than Buca. After that gratifying deal, Sullivan was promoted to CFO, the name of LDDS was formally changed to WorldCom, and the three cohorts were gearing up to rock the financial world. Frequently, segments are closed without this analysis being
done, and the result is often that the company is surprised to find that it has less profit, not more, after the segment is closed. and another in which to record their ill-gotten gains" (Swartz & Watkins, 2003, p. Reuters. 059402 01 ch3 p069-116.indd 99 Chapter 3 • The Sizzling Saga of Sunbeam 99 (b) Cash flow from operations (CFFO) would be
overstated by $10,000. Failure to Record Expenses or Losses and Understatement of Liabilities LIVENT 9. • Identify the conditions under which "bill and hold sales" can legitimately be recognized in accordance with Generally Accepted Accounting Principles (GAAP). In a subsequent CNBC interview, Robert Hudspeth, the former WorldCom vice
president, explained how—as WorldCom crumbled—Ebbers became obsessed with small and trivial details such as travel expenses, meals for employees, or smoking breaks (Faber, 2003). "No Contest for Ex-AHERF Chief: Sherif Abdelhak Defends Himself, Stating He Intended to Keep the 059402 01 REF p365-382.indd 373 "Lockheed L-1011".
TriStar," Airliners. Holdings of less than 20 percent, where the investor has a passive interest in the investee. The Economist. To illustrate the validity of this technique, let us examine an extract from Sunbeam's income statements in Table 3.1 and an extract from its balance sheet in Table 3.2. If we divide accounts receivable at the end of any quarter
by the addition of the sales for the four quarters ending on that date (i.e. the trailing twelve months' sales), we see the trend of accounts receivable growing as a percent of sales in the first quarter of 1997 to almost 49 percent of sales in the first quarter of 1998. 059402_01_GLINDEX_p383-401.indd
Enforcement Division, 27 Litigation Release, 27 response of, to Dodd-Frank, 40-41 Securitization, 234, 270-271, 327-328, 335 The pooling of loans and the trading of portions of these loans on securities markets in the form of collateralized mortgage obligations or mortgage-backed securities. The code of conduct and ethics hotline were more form
than substance. (b) Weather derivatives. The CUC managers utilized a variety of means to achieve their goals" (AAER 1275, 2000). Pursuant to his plea agreement with the government, Madoff agrees not to seek a sentence of other than 10 years in prison. In the third quarter of 2001, "Enron finally terminated the vehicles. This is the saga of the
analysts and journalists who watched and applauded while the auditors overlooked the false profits reported by a company that had the guts ripped out of it after the appointment of Albert J. [in millions] Table 6.1 Summary of Rite Aid's FY 1998, and 1st Quarter FY 2000 Overstatements of Pre-tax Income* 202 Chapter 6 • Abracadabra
7/7/14 9:05 AM Chapter 6 • Abracadabra 203 Another frequently used measure is the number of days' sales in inventory, which refers to the length of time it takes a company to turn its inventory into sales. Nonperforming loans are loans that are 90 or more days delinquent on which interest recognition has been suspended until realized because of
doubts as to the borrower's ability to repay 059402_01_ch9_p325-360.indd 358 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 359 principal and interest. The complaint alleges that, by various means, certain Peregrine officers and employees fraudulently concealed the revenue inflation scheme. If the nondisclosure of the sale of accounts receivable
does not affect earnings, does this reduce the responsibility of management to properly disclose the sale of accounts receivable? (Buca 10-K 2001; pages F-14,F-15) From BUCA's 10-K 2002 NOTES: Note 10 10. 6). The Examiner also believes that SSB aided and abetted those breaches.... In the fiveyear period ending July 30, 2002, the SEC filed 515
enforcement actions against "164 entities and 705 individuals" (SOX Report, 2002, p. 059402_01_ch5_p144-190.indd 168 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldC
employees from the banks allegedly misled their own banks as to the amounts Enron would pay for the dismantling of the SPEs. Astoundingly, Fastow constructed yet another SPE, named Southampton, which he controlled and used—together with other Enron employees and the banks' employees—to buy out the interests of Credit Suisse and
NatWest in the LJM1 set of partnerships. June 30, 2003. Explain why or why not within the context of the justice approach to ethical decision making. The reserve for bad debts decreases as a percentage of accounts receivable. Serendipitously, Dunlap's next position truly seemed to be a perfect match with his genetic makeup. (LR 17762, 2002)
Fastow's audacity was unbelievable, and it did not end there. Bishop, Toby, and Frank Hydoski. 059402_01_ch5_p144-190.indd 149 7/7/14 9:04 AM 150 Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom The acquisition of ATC in 1992 seemed like a good move. October 15, 2004. Do you think that a conflict of interest exists if an
investment bank sells mortgagebacked securities (MBSs) to its clients while the bank itself invests in credit-default swaps (CDSs) that essentially bet on the default of the same MBSs that it sells? Dunlap, Albert J., with Bob Andelman. "Anatomy of a Fall: Keys to Success Left Kenneth Lay Open to Disaster," Wall Street Journal. Interest income has not
been offset. By 2006, Countrywide had turned its prior business model on its head: a mere 31.9% of its originations were conforming, 45.2% were non-conforming, 8.7% were subprime, and 10.2% were home equity. Since the financial crisis of 2008, however, there has been an increase in SEC enforcement actions in respect of the disclosure of
mortgage loans and in the understatement of reserves for loan losses and the corresponding overstatement of investments in loans and investments in loans and investments in mortgage-backed securities. Gadel, however, stated that WorldCom's compensation
committee alleged it was Ebbers's idea that WorldCom lend him money to avoid the sale of his WorldCom stock to repay his outside loans. Underestimation of allowance for loan losses: In the text, as well as
extracts from the SEC Complaint against TierOne. The Company purchased bakery products in the amount of $181,000, and $92,000 in 1999, and 2000, respectively. Which of the following methods of fictitious accounting were used by Rite Aid to understate its cost of goods sold? During 2002, the company deferred certain pre-production expenses
related to the launch of the Ford V-6 diesel engine program in accordance with Emerging Issues Task Force Issue No. 99-5, "Accounting for Pre-Production Costs and expenses had been deferred. • Employees of the company have a right to truthful
information about the company. * Obtained from U.S. Securities and Exchange Commission. 33). Moore, Matthew L. Buca is a publicly traded company incorporated in Minneapolis. www.latimes.com. • We conclude over-the-counter derivatives contributed significantly to this crisis. The EBS farce had caused
Enron to lose more than $1 billion. Accompanied by reported increases in profits, the plant and warehouse closings didn't have to be logical—they just had to be dramatic—and they were. Enron's $250 million in cash. inadequate disclosure in
293-295 059402 01 GLINDEX p383-401.indd 394 Mariner Energy, 247-248 Mark, Rebecca, 236-239, 278 Mark-to-market accounting, 232-235, 247-248, 256, 263 The revaluation of an asset or a liability on an entity's balance sheet to its market or fair value and the corresponding recording of the increased or decreased amount as income on the
income statement or as other comprehensive income. By the end of 2008, millions of Americans were unemployed, billions of dollars in mortgages and mortgages and mortgages and been lost, Lehman Brothers had collapsed, and the American International Group (AIG) had to be bailed out by the federal government. At first, these lenders
concentrated on making loans that adhered to strict underwriting criteria that were required for the loans to be sold to the GSEs; these loans were known as GSE conforming loans. Ebbers wanted the company to grow as big as possible, Grubman seemed to want a leadership role in the telecom-analyst sector, and Sullivan
worked on producing high reported earnings and high stock prices. Interestingly, Skilling turned down Princeton University, in Dallas, for his undergraduate degree. • We conclude the government was ill prepared for the crisis, and its inconsistent response added to the uncertainty and panic in the
financial markets. As such, Skrypek knew, or was reckless in not knowing, that EDP's High-Wirerelated charges were not genuine capital expenses. If possible, use examples from your work or internship experience to support your view. It would then sell the contract at a discount and receive cash up front. April 29, 2013. Morgan Stanley's attorneys
and Sunbeam's internal and external counsels insisted on a press release disclosing that the company's 059402 01 ch3 p069-116.indd 83 7/7/14 9:01 AM 84 Chapter 3 • The Sizzling Saga of Sunbeam sales in the first quarter of 1998 might not meet analysts' expectations. Signal #1: Increase in Accounts Receivable as a Percentage of Sales The land of the sizzling Saga of Sunbeam sales in the first quarter of 1998 might not meet analysts' expectations. Signal #1: Increase in Accounts Receivable as a Percentage of Sales The land of the sizzling Saga of Sunbeam sales in the first quarter of 1998 might not meet analysts' expectations.
eading sign of an overstatement of sales is when accounts receivable increase as a percentage of sales, which is often measured as DSO. May 10, 2013. 1997. Concerning the manipulation of line costs, it must be noted that by 1999, both local and international line costs had mushroomed out of control. January 5, 2006. nytimes.com. However, because
Azurix had initially been funded by the off-balance-sheet entity, Marlin, Enron was still on the hook for Marlin's loans that had been used mainly on Azurix. Salomon allocates 205,000 shares to Mr. Ebbers in the Qwest IPO.," 2007). Finally, it did not disclose that Pay-Option ARM loans, including reduced documentation Pay-Option ARM loans, were
included in the category of prime loans. The Company has recorded its investment in Empire at approximately $4,500, while the amount of underlying equity in the net assets of Empire is approximately $3,000. The 80/20 loan is a mortgage loan whereby the borrower takes out a loan for 80 percent of the purchase price and a second loan for 20
percent of the purchase price, leaving the borrower with no equity in the house at the time of the loan. The article went on to say that "Albert Dunlap all but gutted Sunbeam Corp. In August 2009, OTS directed TierOne to obtain updated appraisals. • The book features an extensive list of references for each chapter, inviting further research and
reading on the various topics covered. On February 27, 1997, Insignia announced that it was restating its financial statements for the first two quarters of 1996. 7/7/14 9:15 AM References 377 Roberts, Johnny, and Evan Thomas. We simply look at the income statement, extract the sales figures, look at the 059402_01_ch3_p069-116.indd 90 7/7/14
9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 91 balance sheet and extract the accounts receivable amounts, and then calculate accounts receivable as a percentage of sales. The handling of this acquisition later caused special criticism by the Bankruptcy Examiner. Sunbeam, nevertheless, recorded these sales as current-period sales even
though they did not meet the criteria. The Start of Enron The company that once represented the pinnacle of corporate success—and the company that became the golden goose for so many—is now a symbol of all that can go horribly wrong in the corporate world. The next highest bid was less than $200 million. This case concerns fraud and other
misconduct by two former officers of Buca, Inc. "Mozilo Settles Countrywide Fraud Case at $67.5 Million," Reuters. As a result of the inexplicably poor terms and other difficulties with the merged companies decided to replace Segnar sooner rather than later. In a June 2006 private placement, Beazer also issued $103 million
of junior subordinated notes. As a result, Chewco should have been consolidated into Enron's consolidation status, JEDI also should have been consolidated into Enron's consolidated into Enron's consolidated into Enron's consolidation status, JEDI also should have been consolidated into Enron's consolida
stock exchange, it would be able to raise cash readily by issuing stock. "Cendant Conviction Upheld," USA Today. Why did Wall Street not question how product lines, and fewer workers? 059402 01 ch7 p226-291.indd 243 7/7/14 9:08 AM 244 Chapter 7
Enron and the Tale of the Golden Goose Finally, in mid-2001, the character from expectations, Enron would not have other contracts that would increase in value by compensating amounts. In addition, his "management fees" from this SPE
came to $2.6 million. Securities and Exchange Commission Litigation Release, June 3, 2010. To achieve that end, Peregrine filed materially incorrect financial statements with the Commission concerning the quarter ended June 30, 1999, through the quarter ended December 31, 2001. Because such entities operate for a specific purpose, in pre-Enror
accounting, the SPEs were allowed to be excluded from consolidation with the sponsor's group financial statements if the equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of the SPEs' total equity interest of a third-party owner was a minimum of 3 percent of a third-party owner was a minimum of 3 percent of a third-party owner w
the Tale of the Golden Goose 249 voting equity rights of the SPE and controlled the SPE and
Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom Tyco International Consolidated Statements of Cash Flows 1998 CASH FLOWS FROM OPERATING ACTIVITIES: Net income (loss) Adjustments to reconcile net income (loss) to net cash provided by
(It is worth noting that Enron was notorious for hiring ex-Arthur Anderson employees who had worked on Enron auditor of the same company for more than five consecutive years. Laing believed that "the earnings from Sunbeam's supposed
breakthrough year appear to be largely manufactured." The article speculated that much of the supposed earnings had come from releasing back into earnings the overstated reserves that had been created upon Sunbeam's restructuring charge in 1996. Because of his close personal involvement in High Wire, Gadel knew, or was reckless in not
knowing, that Buca's payments to EDP for High Wire employee salaries and office space were not legitimate capital expenses. Buca, in turn, would characterize the inflated invoices as capital expenses and office space were not legitimate capital expenses. Buca, in turn, would characterize the inflated invoices as capital expenses.
saga in California, a little background information is necessary. Galbraith thus viewed leveraged transactions as frequent catalysts in boom-bust cycles. Because the connection fee was fully offset by a simultaneous increase in the purchase price ADT allocated to the dealers' security monitoring contracts, the connection fee transaction lacked
economic substance and should not have been recorded in Tyco's income statement. Acceleration of revenue via improper use of multiple-element contracts through misclassification, what would the bad debt expense have been in the period
following the acquisition? (Acquisitions can also make a corporate group's revenue appear to be growing when, in fact, the parent company and the acquisitions can also make a corporate group's revenue appear to be growing when, in fact, the parent company and the acquisition can also make a corporate group's revenue appear to be growing when, in fact, the parent company and the acquisition can also make a corporate group's revenue appear to be growing when, in fact, the parent company can use its stock as currency for the next acquisition, which can
again be used to overstate profits after the acquisition period. It could be argued that leading up to the financial meltdown, many people honestly might not have anticipated the possibility of a sharp drop in the price of houses. Lay, Skilling, and Fastow The three men who would steer Enron to eventual ruin were all in place by the beginning of 1990.
These deferred start-up costs were not in compliance with GAAP. Falsely creating such reserves for the acquiring company. WorldCom reclassified $3.8 billion of line-cost expenses as capital assets, thereby presenting those costs as assets on the balance sheet
instead of as expenses in the income statement, in order to falsely overstate the earnings that it reported. In addition, CUC manipulated membership subscriptions and suspiciously met analysts' earnings targets on a regular basis. The following tables present summarized information concerning the assets, liabilities and results of operations of
Empire for the most recent periods for which information is available: Dec 31, 2007 Assets $ 9,460 $ 101 Liabilities Revenues Net loss Six Months Ended Dec 31, 2007 Year Ended June 30, 2007 $ — $ (11) $ — $ (33) From BASIN's 10-K 2007 NOTES, Page 27 Note 15: RELATED PARTY TRANSACTIONS The Company paid legal fees to a legal firm
whose partner is a director. (NatWest) Limited Partners $7.5 MM $64 MM Note ENE shares (3.4 MM) Enron Corp. in Byron, 2004, pp. The FASB tentatively requires that the new standard will be effective "for annual reporting periods beginning after December 15, 2016," for public companies (Revenue Recognition Project, 2013, p. Relationship
Morality. As these loans grew—and grow they did—significant amounts of Ebbers's WorldCom to Sell his WorldCom stock to pay the
loans, such a large volume of selling would put considerable downward pressure on the WorldCom stock price. 059402 01 ch7 p226-291.indd 271 7/7/14 9:08 AM 272 Chapter 7 • Enron and the Tale of the Golden Goose Table 7.3 Guaranteed Liabilities Extracted from Notes to Enron's Annual Reports: 1998-2000 December 1998 December
1999 December 2000 Guaranteed Liabilities for Letters of Credit on behalf of unconsolidated affiliates $209 M* $ 303 M $ 264 M Guaranteed Liabilities on behalf of certain liabilities of unconsolidated affiliates $100 M $1,863 M 
Interim Report, 2002, p. Still unwilling to face the reality of extinction, Enron contrived yet another structure to help the Raptors extend their artificial lives a little longer. Doubuzinskis, Alex, and Dan Levine. There were also problems with the invoicing system and the computer system. As a result of basically buying Sunbeam out of bankruptcy, Price
and Steinhardt, the fund managers, had an enormous amount of stock and an enormous amount of control over Sunbeam, even after it went public. In most cases, company personnel achieved this using their own versions of hocus pocus. How Enron Lost A FORTUNE Some of the imprudent projects that caused Enron to lose billions of dollars
included the infamous Dabhol Power Plant in India, the Azurix water debacle in England, the massive Enron Online venture that went spinning out of control, and the hugely incompetent Enron Broadband Services (EBS), among others. Management actively studies trends of warranty claims and takes action to improve vehicle quality and minimize
warranty claims. • Examine the summarized Financial Statements of Beazer Homes for 2004-2007, given below. November 4, 2002. Consolidated Balance Sheets (in thousands, except share amounts) September 30 2007 2006 As Restated ASSETS Cash and cash equivalents Restricted cash Accounts receivable Income tax receivable
Inventory Owned inventory Consolidated inventory Consolidated inventory Residential mortgage loans available-for-sale Investments in unconsolidated joint ventures Deferred tax assets Property, plant and equipment, net Goodwill Other assets Total Assets LIABILITIES AND STOCKHOLDERS' EQUITY Trade accounts payable Other liabilities
Obligations related to consolidated inventory not owned Senior Notes (net of discounts of $3,033 and $3,578, respectively) Junior subordinated notes Warehouse Line Other secured notes payable Model home financing obligations Total Liabilities Stockholders' Equity: Preferred stock (par value $0.01 per share, 5,000,000 shares authorized, no shares
issued) Common stock (par value $0.001, 80,000,000 shares authorized, 42,597,229 and 42,318,098 issued, 39,261,721 and 38,889,554 outstanding) Paid in capital Retained earnings Treasury stock, at cost (3,335,508 and 3,428,544 shares) Total Stockholders' Equity Total Liabilities and Stockholders' Equity 059402_01_ch3_p069-116.indd 110 $
454,3375,17145,50163,981 167,5704,873338,033 - 2,537,7913,137,021237,3822,775,173781109,143232,94971,68268,613102,690 118,07314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,70314,1162,606,299140,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,754330,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,008557,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857,00857
1,551,422 103,093 94,881 89,264 117,079 2,984,204 — 43 42 543,705 963,869 (183,895) 1,323,722 $ 3,930,021 529,326 1,390,552 (189,453) 1,730,467 $ 4,714,671 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 111 Beazer Homes USA, Inc. He interpreted "mean" as "strong," and he titled his memoir Mean Business: How I Save
Bad Companies and Make Good Companies Great. Using this slow shipping strategy, the company could record a few extra days' sales in a particular quarter. • Sensormatic, Xerox, CUC, and Insignia are presented in this chapter as examples of various forms of Improper Revenue Recognition (see Table 1.1 on p. Buchan, Howard. Furthermore, the
SEC declared, "As members of Sunbeam's management knew or were reckless in not knowing, these misstatements and omissions rendered Sunbeam's press release materially false and misleading." The SEC also found that although Sunbeam had ostensibly met its earnings targets for the third quarter of 1997 by relying on accelerating future
periods' sales, "management publicly denied the contention of certain analysts that Sunbeam relied on channel stuffing to achieve its revenue targets." (Quotes from AAER 1393, 2001) When it came to the fourth quarter of 1997, all the tricks (as previously described—and more) were still not enough to meet Sunbeam's unlikely targets. In 1970,
Fannie Mae issued the first mortgage-backed securities (MBSs) in the United States when it sold securities backed by its FHA and VA loan programs and guaranteed the payment of principal and interest. When the purchase prices were deregulated, prices fell and 059402 01 ch7 p226-291.indd 230 7/7/14 9:08 AM Chapter 7 • Enron and the Tale
of the Golden Goose 231 companies were stuck with these take-or-pay contracts to purchase gas at prearranged fixed prices that were above-market. "2004". These are clear indications that a company may be sprucing up its reported financial statements—and that one cannot rely on the financial statements for analyzing the profit, the cash-flow
generation, or the debt of the company. Whitewing then paid "$1.6 billion to purchase assets from Enron." Continuing with its tricks, "Enron recorded the proceeds of its sales of assets to the Whitewing Investment Entities as cash flow from operating activities." (Quotes from Bankruptcy Report #2, 2003, p. In fact, the assistant controller later met
with Gadel and Skrypek on the issue, and suggested that Enron had expanded its investment in SPEs to an outrageous degree
"Enron ... Why is a decreasing sales-to-PPE ratio a signal of possible overstatement of assets? (2) The ratio of the lower of the amount of all loans secured by the property. On the last day of the first quarter of the year, Crafty contrives with 7/7/14 9:10 AM 314 Chapter 8 • Tall Tales Tricky
Company to sell 100 printers to Tricky Company for $1,000 each. The SEC findings also alleged that during the auditors that would have "disclosed the improper recognition of revenue on out-of-period shipments." Furthermore, the employee was apparently told to "follow orders
or quit" (AAER 1027, 1998). For example, in June 2001, Peregrine's senior treasury management's approval and encouragement, created a false $19.59 million invoice and sold it to a bank. Peluso, Romano. One of the signals of Xerox's fictitious reporting is the lagging of CFFO behind net income, and it should be flagged through
the following activities: (a) Reduction in CFFO, from 25% of net income in 1995 to 18% in 1997. According to the SEC, in April 2006, Mozilo wrote in an e-mail, "Since over 70% [of pay-option ARM customers] have opted to make the lower payment it appears that it is just a matter of time that we will be faced with much higher resets and therefore
much higher delinquencies" (qtd. Houston Chronicle. Calculation of Accounts Receivable as a Percentage of the Trailing 12 months' sales for fiscal
2000-Q3, 2000-Q4, and 2001Q1. In general (although not in the case of WorldCom), these kinds of aggressive capitalizations of expenses occur in the areas of: • direct response advertising costs. This has come to be known as the "Volcker Rule" (Sarno, Mueller, & Burns, 2010). (Quotes from Byron, 2004, p. Back in California, the price of electricity
was out of control. These two companies merged in December 1997, taking the name of Cendant Corporation, which carried on the same period was negative. Rhodes Co. manages a school for the Old
England School District. According to the SOX Report (2002), round-trip transactions are transactions.
Complaint against Tyco, given below. The entire sham that was WorldCom may have been set in play by Ebbers following his high school basketball teammate to Mississippi College, but it was about to be unraveled by a different kind of team altogether—a team of trustworthy internal auditors. Although a Buca assistant controller advised Skrypek
that he was uncomfortable with the practice of searching for items to capitalize at the end of each quarter in view of earnings targets, neither Skrypek nor Gadel did anything to change the practice. March 29, 2003. There were many adjustments that they could not enter, however, because such adjustments "would have left a trail of 'red flags' for the
auditors." Therefore, senior 1 Livent submitted an offer of settlement and consented to the entry of the order without admitting or denying the findings as set out in AAER 1095 (1999). In May 2007, the Company entered into an agreement to acquire certain water rights and related assets. (First Interim Report, 2002, pp. United States Department of
Labor. Mortgage lenders and investments bankers were making enormous profits selling these loans, and investment banks were making money securitizing them. Possession of IDB WorldCom, and investment banks were making money securitizing them. Possession of IDB worldCom, and investment banks were making money securitizing them.
when a review of financial statement notes reveals the following: • A company invests significant amounts in unconsolidated SPEs. • That company engages in significant related-party transactions with these entities. 106) While the SEC Complaint (June 4, 2009) alleged that attributes of the loans underwritten were not properly disclosed, it did not
make any allegations regarding the fact that the loan losses in 2007 were much greater than the amounts provided for in the allowances for loan losses in the financial statements in the years leading up to 2007. • There was no objective way of calculating Enron's real profit. Form 8-K. It is difficult for a manufacturer suddenly to increase the
company's gross margin percentage; it is also suspicious if the gross margin fluctuates downward suddenly. The FCPA is essentially comprised of two sections: the antibribery regulations and the accounting regulations and the accounting regulations. Each Beazer subdivision under construction had at least one land inventory account associated with it in Beazer's general ledger. It
had nothing to do with how we were measured for our bonus. (a) Inventing fictitious customers. Even Kenneth Lay agreed that Azurix had been a tremendous waste of money and that Mark had to resign. 16. Patent Costs The Company capitalizes costs of patent applications. He conjured up a buyer—his own LJM1—and sold a 13 percent stake in
Cuiába/EPE to LJM1 for the sum of $11.3 million. These write-offs knew, or were reckless in not knowing, that certain written-off receivables should not have been recorded as revenue in the first place. This, in turn,
allowed the low-risk institutional investors to invest in non-GSE mortgage-backed securities. Consulting Fees—The son of a member of our Board of Directors performs architectural and design-related services for us. By the second quarter of 2000, Enron Broadband's revenues were way behind predictions. In November 1998, as a result of the
investigations, Sunbeam "issued substantially restated financial statements for the six quarter of 1998. Adjustments that increase in a later period, with respect to an earlier acquisition, are further signs that a company may be creating false reserves. U.S. Securities and Exchange Commission
The Nature of Moral Reasoning: The Framework and Activities of Ethical Deliberation, Argument, and DecisionMaking. In November 2002, the Commission filed a civil injunctive action against Ilse Cappel, the former senior treasury manager at Peregrine (Litigation Release No. 17859A). The jobs I had were the greatest jobs you'd ever want to have,
he said. The "due diligence" study by Morgan Stanley on Sunbeam picked up information on overstocked customers and slowmoving sales in the first quarter of 1998. Most of this was paid for with WorldCom stock. Again, in my view it would be difficult for a financial services firm to satisfy this standard if any of its business unit heads or senior
managers has not shown a commitment to proactively identifying and remediating conflicts of interest in the business model of the organization. Such sales are often known as "guaranteed sales," where the customers can return goods if they are unable to resell them or they can get a reimbursement if they cannot achieve a certain resale selling
price or a guaranteed markup. • Walter Forbes, former CUC chairman and CEO, stood trial with Shelton. T 059402 01 ch6 p191-225.indd 212 F 7/7/14 9:06 AM Fill-in-the-Blank Questions Fill in the blanks with information and concepts from this chapter. Perelman had lost close to $1 billion when Sunbeam collapsed. • The company moved away
from its core competency, such as adding new items to the menu and selling doughnuts that were not cooked on-site. Management fees of approximately $222,500 were charged in 1999. BellSouth is presented mainly as an example of Improper Accounting for Foreign Payments in Violation of the Foreign Corrupt Practices Act (FCPA). In addition to
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the top-side entries, entries recorded in the financial statements but not in the general ledger or other formal accounting revenues to current periods' revenues. The complaint also alleges that, as part of the cover up, Peregrine personnel wrote off millions of dollars in
uncollectible—primarily sham—receivables, to acquisitionrelated accounts in Peregrine's financial statements and books and records. (a) Increasing the deferred revenue amount on the balance sheet. I would like to examine each of these factors in turn, and explain how I believe it relates to effectively managing conflicts of interest. Soon, rumors
began to spread throughout the MBS and CDO markets that AIG and many of the monoline insurers did not have the capital to make good on their so-called "guarantees." This made it even more difficult for mortgage lenders and investment bankers, including Bear Stearns, Merrill Lynch, and Lehman Brothers, to sell their ownership interests in
mortgages and MBSs. Fear that the CDS hedges might fail, and knowledge that house prices and the value of their investments in MBSs were falling, made it impossible for Bear, Merrill, and Lehman to get the shortterm financing on which they had relied. 15. Explain how a company's overstatement of its restructuring reserve may not cause it to
understate its operating income in the period that it overstates the reserve. www.super70s.com. 155). The first is caused when informal networks are destroyed, information sharing is restricted, and experienced employees depart. Pipeline companies paid regulated amounts to the gas producers and, in turn, received regulated prices from industrial
customers and gas utilities for piping the gas to them. The second is caused by declining morale, loss of loyalty and commitment, and the departure of the severance pay, and Dunlap sued and settled for $50,000. By 1999, that had jumped to
51%." It may be a matter of debate whether keeping the audit 059402 01 ch1 p025-046.indd 31 7/7/14 8:58 AM 32 Chapter 1 • Introduction to the Problem of Accounting Fraud client because of the audit fees alone was enough to make some auditors compromise their audits or whether the double incentive of consulting fees was a deciding force.
• WorldCom emerged from bankruptcy in April 2004, doing business as MCI. As the Supreme Court stated almost five decades ago, [a] fundamental purpose, common to [the federal securities] ... statutes, was to substitute a philosophy of full disclosure for the philosophy of caveat emptor and thus to achieve a high standard of business ethics in the
securities industry...... Greed, ego, and hubris all played an underlying role. "Dealing with the SEC's Focus on Protecting Whistleblowers from Retaliation." Client Alert. This was when the scheme started. According to reports, Grass was a model prisoner (Scolforo, 2005). If such a trend continues over time, at least one of two things has happened—
and they are both bad. March 16, 2002. "Losing Home—Immigrant Families' Path Through Foreclosure and Beyond," New America Media. Although it was drawn up and passed quite rapidly, it took several years, countless squabbles, and many millions of dollars for the various facets of the SOX Act to be implemented. • The material is well organized
and complex material is presented in a logical, easy-to-follow manner as the chapters systematically examine the Top 20 Methods of Fictitious Financial Reporting Scheme of Failing to Account for Asset Impairments
Lockheed had an accounting policy in which it capitalized the TriStar's development costs with the intention of writing them off as the planes were sold. However, when debt grows substantially and the times-interest-earned ratio does not improve, there is cause for concern that the company will be unable to maintain or repay its debt. These
adjustments were used for "closing any gaps between targeted and projected actual earnings." They also spread the irregular amount over a number of months and over a number of months and to be provided for repayment of the loan;
Enron obligingly provided this cash collateral.4 The Powers Report (2002) later concluded: The existence of this cash collateral for the Barclays funding was fatal to Chewco's compliance with the 3% equity requirement.... Although he was down-to-earth around town, with his down-home clothes and his unpretentious truck, he was always on the
prowl for companies. Vincent, Roger. On March 2, 1998, when Dunlap's new employment contract was announced during a conference call, a Bear Stearn's analyst, Constance Maneaty, questioned Dunlap on whether his generous new options package would be a drag on earnings in the future. In January 2003, the Bankruptcy Examiner reached the
following conclusions on the prepay transactions: Collectively, the Prepay Transaction may have been Enron's single largest source of cash during the four-year period prior to the petition date, providing Enron with $5 billion of cash. (c) Will likely be ignored by the SEC. When the future payment or loss occurs, the amount is offset against the
reserve, and it is not reported as an expense in that later period. To ascertain when the risks of ownership passes to the buyer, one should refer to the terms of the deal to see whether the sales contract specifies FOB shipping, where
ownership passes when the goods arrive at their final destination. Soon there would be a way to make real money with broadband. Signal #2: Increase in PPE with Decrease in Revenue — When the PPE amount on the balance sheet increases while revenue actually decreases, this is a double red flag that something is likely to be seriously wrong with
the company. • Richard Causey (former Enron chief accountant) entered into a last-minute plea bargain agreement toward the end of December 2005, just a few weeks before the start of the trial of Lay and Skilling. The Company purchased bakery
products in the amount of $169,000, $181,000, and $92,000 in 1998, 1999, and 2000, respectively. 3 For more information, see page 266 of this chapter. In Enron's "Notes to the Consolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annual Report, the note titled "Unconsolidated Financial Statements" in its Annu
unconsolidated affiliates was alarming—the total liabilities grew from $8.3 billion in 1997 to $20.6 billion in 2000. Many companies began to bend the equity capital (except for 3 percent), and for which they had further obligations for the entities' debt. The
Projects of Rebecca Mark Rebecca Mark Rebecca Mark was a glamorous Harvard MBA graduate who had worked with John Wing from the division that later became Enron Development. The interest must relate to the period beginning with construction costs and ending when the asset is complete and ready for service. AAER 1678. di Florio Director, Office of
Compliance Inspections and Examinations 1 NSCP National Meeting October 17, 2011 Today I would like to address two related topics that are growing in importance: the heightened role of ethics in an effective regulatory compliance program, and the role of both ethics and compliance in enterprise risk management. university of california.edu/news
Intangible Assets Net intangible assets are as shown in the following table as of the dates indicated: Deferred stock based compensation Fair value of warrants, net Service agreements and contracts Customer relationships Covenant not to compete Trade name Loan costs, net Intangible assets, net December 31, 2007 2006 $ 189 $ 394 916 1,210
1,299 — 560 — 295 — 157 — 37 $ 3,416 $ 1,641 The amortization period of intangible assets are as follows: customer r elationships—15 years; covenant not to compete—three years; trade name—two years; and fair value of warrants issued to a joint
venture partner—five years. 68). The problem was that when one excluded the gains from sales of its merchant assets and its trading profits, there was not enough traditional recurring income for its "logistic" operations to sustain its stock price. The potential buyers of broadband capacity were the big telephone companies that did not like Enron very
much and believed that Enron's entry into their business was going to become a comedy of errors; they had no incentive to trade with Enron. 274) 059402 01 ch5 p144-190.indd 160 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom Wizardry:
reserves to falsely reverse into earnings, the WorldCom gang turned to a much simpler, more old-fashioned ruse to inflate earnings. U.S. Securities and Exchange Commission vs. There are as many methods of categorizing financial reporting violations as there are studies of financial reporting enforcement actions. Gadel announced his resignation
from Buca in December 2004, and left the company in February 2005. In certain instances, Beazer also began purposefully not recognizing certain current period expenses. (AAER 1393, 2001) On May 11, 1998, Sunbeam issued its first-quarter 1998 earnings release. 200). RELATED-PARTY TRANSACTIONS Management Agreement—In 2000, we
entered into a management agreement with a member of our Board of Directors to provide for certain management and administrative services. In his later article in Forbes Magazine, Daniel Fisher (2002) explained to readers how Enron's revenue and
about $67 million to its profit. (This is footnote #19 in original speech.) 059402 01 ch8 p292-324.indd 310 7/7/14 9:10 AM Chapter 8 • Tall Tales 311 Assignments True/False Questions with T for true or F for false for more practice with key terms and concepts from this chapter. For Enron, "[t]he easy money was just
too tempting to pass up" (Eichenwald, 2005, p. LR 17829. (b) Auditors of nonpublic broker-dealers will be subject to oversight by the PCAOB. The problem became worse in 1998 when WorldCom acquired MCI and increased the number of departments selling the same products (Krim, 2002). These derivatives were known as credit-default swaps
(CDSs). Exploring Ethical Lapses During the Rite Aid Crisis7 By Anne Federwisch Timothy J. In all cases, however, the main objective was either to boost the appearance of corporate profits or to enhance the seeming strength of the balance sheets. Bethany McLean and Peter Elkind, in their book The Smartest Guys in the Room: The Amazing Rise
and Scandalous Fall of Enron (2004), pointed out, "This line of thinking suggests that General Motors should book all the future profits of a new model automobile at the moment the car is designed, long before a single vehicle rolls off the assembly line" (pp. 059402_01_ch9_p325-360.indd 353 7/7/14 9:11 AM 354 Chapter 9 • Mortgage Mayhem
Allowance for loan losses at end of year What is the amount of the loss that Sloppy Mortgage must recognize in its income statement in 2007 if it has no allowance for loan losses in respect of this loan? James Sterba has identified four kinds of rights: 1. "Uncooking the Books," Wall Street Journal. Power does not consolidate P2 into its consolidated
financial statements. • Identify and explain Krispy Kreme's inappropriate accounting for round-trip transactions. At these meetings, they "agreed on the approximate nature and quantity of adjustments to be made . . . in order to achieve a predetermined false financial picture" (AAER 1095, 1999). June 9, 2003. Signals of WorldCom's Fictitious
Reporting Scheme #2—Understating Expenses via Improper Capitalization of Expenses This fraud overstates earnings reported on the income statement and inflates assets on the balance sheet. "Former Cendant Controller Gets Probation." CFO. These two schemes were perpetrated in an unscrupulous and brazen manner with a total disregard for
veracity and accurate reporting. After deregulation, selling prices shot up during times of higher demand but plunged at other times, making it difficult for users to predict future purchase prices and estimate whether or not an industrial gas plant or a gas utility would be profitable. • Identify the signals in financial statements that could alert one to
the possibility that a company may be misusing restructuring reserves in order to overstate earnings. The nondisclosure of these sales had the dual effects of making the cash-flow situation look stronger: "This added $182 million in pre-tax profits to Xerox's 1999
results" (AAER 1542, 2002). His departure represented the loss of "information sharing," of which Cameron spoke (qtd. They came up with Andrew Fastow. Employee Loan—In March 2001, the Company entered into a $150,000 unsecured loan with one of its officers. Enron wrote back to the SEC and said that it planned to go
ahead and use mark-to-market accounting a year earlier than the date approved by the SEC. 059402 01 ch4 p117-143.indd 137 7/7/14 9:02 AM 138 Chapter 4 • Hocus Pocus Large aged accounts receivable were not being paid, an indication that Peregrine's financial health was deteriorating. When all or most of the houses in a development were
eventually sold, these over-allocations resulted in the affected land inventory accounts having negative (or credit) balances. **All of the illustrating companies except Lockheed were the subject of SEC enforcement actions. For example, in 1996 and 1997, approximately $12 million relating to seven different shows and twenty-seven different locations.
was transferred to the accounts of approximately thirty-one different future locations and ten other shows then in process. Current GAAP has many industry-specific and transaction-specific rules for revenue recognition. The SEC's Litigation Release No. 17692 (2002) alleged that Kopper "shared the $1.5 million management fee with Enron's CFO"—
none other than Andrew Fastow. (d) Decreasing expenses on the income statement for year 1 in accordance with EITF 01-14? (Interestingly, Bobbit did not mention the issue at a board of directors meeting the next day.) When KPMG asked Cooper to recheck her facts,
she questioned Betty Vinson (the director of management reporting) and Buford Yates about the capital expenditure entries. • The PCAOB developed an extensive inspection program. In addition, this fraud overstates the cash flow from operations (CFFO) and inflates the amount reported as "cash used in investing activities" in the statement of cash
flows. In an apparent attempt to increase confidence in its liquidity, Lehman increased its reliance on what has come to be known as the Repo 105 Transactions. Why did none of the executives inform the board of directors of the unfolding chaos? www.sec.gov 059402 01 ch5 p144-190.indd 182 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry:
From WorldCom to WorldCon 183 SEPTEMBER 30, 1999 COMMITMENTS AND CONTINGENCIES (NOTE 17) SHAREHOLDERS' EQUITY: Preference shares, $1.25,000,000,000 authorized; 1,690,175,338 shares outstanding in 1999 and 1,620,463,428 shares
outstanding in 1998, net of 11,432,678 shares owned by subsidiaries in 1998 and $67.3 in 1998 Accumulated earnings Accumulated other comprehensive loss TOTAL SHAREHOLDERS' EQUITY
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY 1998 — 338.0 324.1 4,881.5 3,607.6 4,035.0 2,584.0 3,955.6 3,162.6 (450.1) 12,332.6 $32,361.6 (203.9) 9,901.8 $23,440.7 Tyco International Consolidated Statements of Operations 1998–19993 (in millions, except share data) YEAR ENDED YEAR ENDED SEPTEMBER 30, SEPTEMBER
1999 1998 NET SALES Cost of sales Selling, general and administrative expenses Merger, restructuring and other non-recurring charges Charge for the impairment of long-lived assets Write-off of purchased in-process research and development OPERATING INCOME Interest income (loss) before income taxes, extraordinary
items and cumulative effect of accounting changes Income taxes Income (loss) before extraordinary items, net of taxes NET INCOME $22,496.5 14,433.1 4,436.3 928.8 507.5 $19,061.7 12,694.8 4,161.9 256.9 — -2,190.8 61.5
(547.1) 1,705.2 — 1,948.1 62.6 (307.9) 1,702.8 (637.5) 1,067.7 (534.2) 1,168.6 (45.7) — 1,166.2 3 Extracted from 10-K filings for Tyco International LTD. More troubling still, a company's high debt can cause analysts to lower their "buy" ratings on the company's stock. Securities and Exchange Commission. 263). www.huffingtonpost
059402_01_REF_p365-382.indd 379 O'Sullivan, Kate. This book provides an informative and invaluable analysis of the Top 20 Methods of overstating earnings and assets and understating debt in financial statements. Analysts' reports on the results of their research into
companies became one more gatekeeping function that could not be relied upon. The surrendered assets include, among other things, several homes, a Ferrari, and more than $10 million in cash and securities Docket. Overall
the release of reserves accounted for the overstatement of profit before tax of approximately $3.3 billion through the understatement of line costs. 21 059402 01 FM p001-024.indd 22 7/7/14 8:57 AM Detecting Accounting Fraud 059402 01 FM p001-024.indd 23 7/7/14 8:57 AM
059402 01 FM p001-024.indd 24 7/7/14 8:57 AM Chapter 1 Introduction to the Problem of Accounting Fraud Learning Objectives After studying this chapter, you should be able to: • Identify the elements of accounting Fraud Learning Objectives After studying this chapter, you should be able to: • Identify the elements of accounting Fraud Learning Objectives After studying this chapter a huge red flag that false reserves are being created to boost later profits.
May 16, 2002. Xerox had sold approximately $400 million of its accounts receivable in order to reduce the reported CFFO. Which of the following is not one of the categories of rights articulated by James Sterba? Also, pursuant to product lines that were to be closed as part of the restructuring in 1996, Sunbeam overstated the amount by which the
inventory had to be written down for all the segments that were going to be closed. The responsibility for the repugnant financial reporting failure does not rest solely with the WorldCom management and staff who perpetrated the frauds or with Arthur Andersen, whose audits failed to detect the irregularities. Specifically, beginning near the end of
fiscal 2005, Beazer, acting through certain of its officers and employees, engaged in negotiations with the third party entity representing the Investor Pools concerning possible sale-leaseback transactions for Beazer's model homes. 31-1999 June 30-1999 Sept. Gadel also reviewed drafts of Buca's quarterly and annual reports, financial statements and
proxy statements before they were filed with the Commission. It can then conveniently discover that the reserve wasn't required and release this surplus reserve back into the earnings in the income statement for the new period. Initially, no problems were obvious to outsiders. Such 059402_01_ch9_p325-360.indd 330 7/7/14 9:11 AM Chapter 9 •
Mortgage Mayhem 331 weekends were allegedly often marked by rowdy festivities, skimpily-clad models, and excessive alcohol. In the case of a financial institution, I would think that this response would include a consideration of any 059402 01 ch8 p292-324.indd 309 7/7/14 9:10 AM 310 Chapter 8 • Tall Tales conflicts of interest that may have
incentivized or otherwise facilitated the bad conduct, and consideration of how any such conflicts can more effectively be barred or remediated. However, Sunbeam failed to divulge this information (AAER 1393, 2001). Gadel and Skrypek each played a significant role in preparing and ensuring the accuracy of Buca's annual and quarterly reports,
financial statements and proxy statements filed with the Commission. This turned out to be a poor choice because Allegheny's CEO, Robert Buckley, was a man somewhat ahead of his time in that he was a forerunner of the high-living CEOs we are all too familiar with today. "Judge Cuts a Year from Rite Aid Chief Grass' 059402_01_REF_p365-
382.indd 374 Sentence," San Diego Union Tribune. www.oversight.house.gov. The more Sunbeam accelerated future periods' sales estimates. "Restatements Resurrected?: Accounting Fraud by the Numbers," Forbes. The fact that an Enron employee ran Chewco was not
revealed to the board of directors and was a contravention of Enron's own policies and procedures guidelines. "Krispy Kreme Ousts CEO in Turnaround Bid," Washington Post. Andrew Fastow, Former Enron CFO, Talks Ethics With Students* By Kirk Kardashian Fastow is proof that the road to ignominy is most often not well marked. This was followed
by a suspicious improvement in 1997 (after the so-called "turnaround") to 27 percent in the first quarter of 1998 and to negative 9 percent in the second quarter of 1998. By that stage, the investigators were already suspicious about almost $2$ billion of
unauthorized capital expenditure. In 2006, "Dabhol reopened as Ratnagiri Gas and Power . . . He named it Chewco, apparently after the Star Wars character, Chewbacca. In 2009, after receiving one year off his sentence for good behavior, Sullivan was released from prison and moved back to Boca Raton, Florida. The business is the first line of
defense responsible for taking, managing and supervising conflicts of interest, like other risks, effectively and in accordance with laws, regulations and the risk appetite set by the board and senior management of the whole organization. SOX Report. This was intended to keep consumers' deposits safe from being used in riskier investment banking
activities and to create a firewall to prevent a financial statements and included municipal securities disclosure reports, in this case, went beyond annual financial statements and included municipal securities disclosure reports, in this case, went beyond annual financial statements and included municipal securities disclosure reports, in this case, went beyond annual financial statements and included municipal securities disclosure reports.
development expenditure is deeply cut and maintenance on property, plant, and equipment is deferred, it is usually a fairly good guess that management is focused on short-term growth and profit. In a civil trial in 2012, Brown was sued by Timothy 059402_01_ch8_p292-324.indd 299 7/7/14 9:10 AM 300 Chapter 8 •
Tall Tales and Michael Rigas who claimed that Brown had never repaid a $400,000 loan. Post Enron, accounting for SPEs was updated by FASB No. 167 (2009). SUNBEAM The following schemes involve improper accounting in connection with business combinations
14. "State Dominates Subprime Mortgage Lending in U.S.," Los Angeles Times. www.cornerstone.com. However, to justify the acquisitions in Internet capacity, WorldCom had to insist that the demand for it was growing at an incredible speed. By the end of that year, LDDS had gone into debt to the tune of over $1.5 million. 059402 01 ch1 p025-
046.indd 28 7/7/14 8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud 29 financial condition of a corporation or business entity. This meant that the more Enron's share price fell, the more shares it would have to issue if Whitewing made losses on the assets it had purchased from Enron. Moreover, Chewco's debt was guaranteed
by Enron, and as soon as it became likely that any debt guaranteed by Enron would have to be paid by Enron, such debt should have been accounted for on Enron's balance Sheet Arrangements. In 2005 and 2006, Countrywide's Pay-Option ARMs ranged between 17% and 21% of its total loan originations. If the
next period's sales have been accelerated into the current period or if the sales are completely fictitious, the company will debit accounts receivable and Grubman acquired another associate who seemed very different from them. Beginning in the first quarter of 1997, Sunbeam
offered deep discounts and extended payment terms to get customers to place the next period's orders early. A year later Ebbers went to work for a clothing manufacturer, where he remained for five years, before buying a cheap, run-down hotel and restaurant in Columbia, Mississippi. Cosmo Corigliano and others "consented to the entry of the Final
Judgment without admitting or denying the allegations of the complaint." As set out in LR 18711, 2004. July 14, 2012. Polverari's supervisors would devise instructions describing adjustments for her to make: "Typically the instructions describing adjustments for her to make: "Typically the instructions describing adjustments for her to make: "Typically the instructions describing adjustments for her to make: "Typically the instructions describing adjustments for her to make: "Typically the instructions describing adjustments for her to make: "Typically the instructions describing adjustments for her to make: "Typically the instructions describing adjustments for her to make: "Typically the instructions describing adjustments for her to make: "Typically the instructions described adjustments for her to make: "Typically the instructions described adjustments for her to make: "Typically the instructions described adjustments for her to make: "Typically the instructions described adjustments for her to make: "Typically the instructions described adjustments for her to make: "Typically the instructions described adjustments for her to make adjustments for her to ma
certain amounts" (AAER 1275, 2000). Gadel and Skrypek found a number of different ways to inflate Buca's income by decreasing expenses through 34 below. 365 059402 01 REF p365-382.indd 365 7/7/14 9:15 AM 366 References Eaglesham, Jean. TierOne Corporation is
059402 01 ch9 p325-360.indd 354 Prime conforming loans $30 billion Pay-option ARM loans with accumulated negative amortization $10 billion Subprime 80/20 loans $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option ARM loans with accumulated negative amortization $10 billion Pay-option Pay-o
following: 0.1 percent of prime conforming loans 6.0 percent of pay-option ARM loans with accumulated negative amortization Compute the required balance for the allowance for loan losses at December 31, 2013. Instead, the Company
relied on the existence of standard provisions in supply agreements or the Illinois Commercial Code to support the contemplated vendor reimbursements. Its policy is to add this development cost to the cost of goods sold as each airplane is sold. Valukas, Examiner. Chicago Sun Times, Available online via ProQuest database. Although the lobbyist
[and] deleting the authorization file delayed acceptance of some quantity of pending returns long enough so that they did not count against net sales for the first quarter" (AAER 1393, 2001). In order to complement this oversight, some firms establish standing committees, composed of senior executives and senior 18 NASD Rules 3010 and 3012,
which are incorporated into FINRA's rulebook, contain comparable requirements. 67) As Enron's share price began its inevitable downward spiral, the Whitewing structure—like an albatross—circled back to accelerate Enron's demise. "SEC Staff Ends Probe of Lehman Without Finding Fraud," Bloomberg. (2) The ratio of the lower of the amount of the amount of the accelerate Enron's demise."
all loans secured by the property to the original appraised value or purchase price of the property. This led to the possibility that Enron would have to devalue the Raptors by $500 million at the end of the first quarter of 2000 and recognize this enormous loss in its financial statements because the Raptors could not meet their obligations. 69
059402 01 ch3 p069-116.indd 69 7/7/14 9:01 AM 70 Chapter 3 • The Sizzling Saga of Sunbeam Chapter OUTLINE • The History of Sunbeam Schemes • The History of Sunbeam Schemes • The Sunbeam Inferno • Signals of Sunbeam's Schemes • Key Terms
CEO learns that the embezzler is most likely one of three employees. (d) Zee Company had not paid for the goods by December 31. Apart from favoring Ebbers with IPO shares, SSB also gave him another brand of preferential financial assistance when he could not buy any more shares because of the margin calls with respect to his personal bank
loans. In addition, power producers were hesitant to explore and producer second not raise financing because the banks required more reliable estimates of future prices in order to assess whether the producers would be profitable enough to repay their bank loans. Although Enron began its SPE activity as a
and second quarters of 1996. Investors should be warned to use all the signals in this chapter to test whether an expense has been misclassified as an asset. Sooner is better than later." Assignments True/False Questions with T for true or F for false for more practice with key terms and concepts from this chapter. A
Buca assistant controller discussed with Skrypek that these payments appeared to represent related party transactions requiring disclosure. Like the child who does not understand the essence of ethics or morality will
be tempted to cheat at the game when no one is looking. There were several problems with this. April 22, 2013. Understatement of expenses via "lack of accrual." 15. The Allegheny Health Education & Research Foundation (aka AHERF) was described by the SEC Enforcement Files as a collection of nonprofit, acute-care hospitals, with a medical
university, physicians groups, and other affiliated entities. This means that the percentage of loans delinquent for 60 days or more were 2.75 times the percentage of such loans in 2004. Schapiro's testimony pointed out that in June 2008, Lehman posted a $2.8 billion loss, which it attributed "primarily to write-downs on residential and commercial
mortgage securities and hedges related to these securities" (p. Ovide, Shira. In January 2000, at a meeting of financial analysts in Houston, Enron and Sun Microsystems announced that they were going public, LDDS swapped some of its new
publicly traded stock for stock in Advanced Telecommunications Corp. Which of the following correctly describes the SEC's finding against Edison? From 1997 until February 2005, Gadel was the CFO and an executive vice president of Buca. The History of Sunbeam The Sunbeam story is ultimately the tale of a company that was gutted by
management in a scorching turnaround attempt made at the same time that Sunbeam's executives falsely overstated profits in the vain effort to find a buyer for the charred company and cut themselves loose from the havoc they had wreaked. The fourth factor is that the organization take reasonable steps to periodically train and otherwise
communicate with its leadership, employees and agents about its compliance and ethics program, including its standards and procedures for implementing the program. However, in its press release on April 3, Sunbeam made no mention of the fact that the shortfall in sales for the quarter was after adding two days' sales to the quarter. In some
cases, Enron had guaranteed to compensate the SPEs for any losses they may incur on the resale of Enron's assets by issuing additional Enron stock to the entities. Salomon is engaged for the first time by WorldCom on the Company's acquisition of MFS, receiving fees of $7,500,000. Chapter Outline • What Is Accounting Fraud? Loans to executives
were prohibited by the Sarbanes-Oxley Act of 2002 because: (a) The board of directors granted huge loans to company's bankruptcy in due course. Jeffrey Skilling The man that Kenneth Lay turned to was a Harvard MBA—and intermittent risk
taker— named Jeffrey Skilling, who worked at the prominent consulting firm of McKinsey & Company. May 14, 2002. Through its officers and employees, Peregrine knew that (a) a substantial portion of these receivables should not have been recorded as revenue in the first place, (b) the receivables were not impaired by acquisitions, and (c) it was
inappropriate to make it appear to the investing public that the write-offs related to non-recurring events. To Ebbers, there was no doubt—LDDS had to go public. 87) LJM1 and the Cuiába Power Plant Fastow amused himself with SPEs for several years before his maneuvers caught up with him. It also guaranteed the principal and interest
repayments. There was little 059402 01 ch5 p144-190.indd 176 20. Finally, the complaint alleges that Tyco violated the antibribery provisions of the Foreign Corrupt Practices Act when employees or agents of its Earth Tech Brasil Ltda. In fact, if the terms of the contract were fully realized, Enron would receive over $25 billion from India (Bryce
2002, p. After this, Merrill concentrated on pooling its mortgage investments into CDOs and reselling them. Lehman add not disclose the known obligation to repay
the debt. Drabinsky was sentenced to seven years in prison and Gottlieb to six years. Finally, senior management and the board of directors need to be engaged. Grant, Peter. "SEC Complaint Reveals What Caused It to Sue KPMG." February 23, 2003. October 31, 2011. Sensormatic instructed employees to withhold certain bills of lading from the
auditors because of: (a) Indication of a practice of unrealized revenue recognition. (c) Reconciliation is needed to compare the amount accrued with the vendor's statement of amount accrued with the vendor's statement account accoun
                                                                                                                                                                                                                                                                without being reported on the balance sheet. www.ocregister.com. Enron would construct SPEs such as Chewco, LJM, and the Raptors that would
use mark-to-market accounting and related-party transactions to overstate earnings and hide the debt related to all the cash that had been recklessly lost. As noted in The Financial Crisis Inquiry Report (2011): Unfortunately ... we witnessed an erosion of standards of responsibility and ethics that exacerbated the financial Crisis. As a result, inventory
at the end of 1996 was understated by $2.1 million. The common short-run focus on gain or loss needs to be measured against long-run considerations. Because LJM1 had received 3.4 million. The common short-run focus on gain or loss needs to be measured against long-run considerations. Because LJM1 had received 3.4 million. The common short-run focus on gain or loss needs to be measured against long-run considerations. Because LJM1 had received 3.4 million. The common short-run focus on gain or loss needs to be measured against long-run considerations.
value. Through it all, he managed to find time and energy to acquire ANS Communications from America Online. 121) For Kant, the moral law admitted no exception. As it transpired, the price of electricity increased dramatically toward the end of 2000 and EES lost a fortune. On April 9, 2002, Ebbers resigned as CEO of WorldCom and John Sidgmore
was appointed in his place. PARAGRAPHS 1-13 FROM COMPLAINT: Plaintiff, United States Securities and Exchange Commission") alleges as follows: NATURE OF THE ACTION 1. Although Buca's assistant controller raised with Skrypek concerns about the vague change orders used by vendors making sham donations, Skrypek
continued authorizing payment of such orders. The inclusion of these anticipated vendor reimbursements and engineering fixes was not in compliance with GAAP. In addition, there was little chance that Ebbers could repay them. CONSOLIDATED BALANCE SHEETS (IN THOUSANDS, EXCEPT PER SHARE AMOUNTS) ASSETS Current Assets: Cash
and cash equivalents Accounts receivable, net of allowance for doubtful accounts of $11,511 and $2,179, respectively Other current assets MARCH 31, 2000 $286,658 $33,511 180,372 62,811 529,841 69,940 22,826 126,277 (continued) 11 Extracted from 10-K filings for Peregrine Systems, Inc. Ethical decision-
making models for accountants, 58-60 in business world, 53-58 consequentialist/utilitarian, 54-55 justice approach, 57-58 rights-and-duties ap
50-51 federal securities laws and, 350 metaethics, 48 normative, 48, 49-53 059402 01 GLINDEX_p383-401.indd 389 risk management and, 349-350 theories of, 48-53 virtue, 49, 51-53 Executive compensation SOX and, 35 stock options, 31, 76-77 Executives, loans to, 36, 71, 162-164 Executive Summary of the SarbanesOxley Act, 36 Existing store
sales, 304-305 Expenses decrease in, as percentage of sales, 196, 197 failure to record, 194 fixed costs, 76, 128, 147, 172-173 improper capitalization of, 161-162, 170-174, 195, 198 improper capitalization of, 161-162, 170-174, 195, 198 improper capitalization of, 191-212
Extended payment terms, 93-94 External auditors, 37 F Factoring, 125 Fannie Mae (Federal National Mortgage Association), 38, 327-328, 334 FASB (Financial Accounting Standards Board), 35, 81, 249, 265-266 Fastow, Andrew, 234, 243, 250, 252, 254-263, 277, 279-280 Fastow, Lea, 277 Federal Bureau of Investigation (FBI) criminal fraud and,
28-29 fraud definition of, 26 7/7/14 9:17 AM 390 Glindex Federal Home Mortgage Corporation (Freddie Mac), 38, 327-328 Federal National Mortgage Association (Fannie Mae), 38, 327-328, 334 Feinberg, Joel, 57 Fictitious financial reporting schemes abuse of special purpose entities, 248-263 estimates of discount rates and residual values, 123-1241
failing to account for asset impairments, 206-209 false recognition of early shipments, 120 FOB destination of expenses, 161-162, 170-174 improper disclosure of sales of leases, 124 improper timing of revenue recognition, 80-84, 90-
94 improper use of bundled contracts, 123 improper use of non-GAAP financial measures, 298 improper use of non-GAAP financial measures,
accounting, 247-248 misleading of auditors, 120-121 prepay transactions, 263-264 related-party transactions, 263-264 related-party transactions, 263-264 Financial Accounting Standards Board (FASB), 35, 81, 249, 265-266
Financial analysts, independence of, 37 Financial Crisis Inquiry Report (2011), 39, 41, 332 Financial Crisis of 2008 accounting fraud Enforcement Task Force, 39-40
Financial information, high-quality, 26, 42 Financial reporting, fictitious methods of. (b) Misuse of multiple element contracts. Further, even if we could predict all the consequences, consequentialists are criticized on the basis that the different goods are not homogeneous and there is no common denominator by which to measure and aggregate the
benefits or harmful effects of actions to determine which actions to follow or which to avoid. Signal #2: CFFO Lagging Operating Income until the "sale" is paid for from the ensuing complementary round-trip transaction payment. For example, the Forms ADV stated that there were
only 23 IA accounts under management at BLMIS when, in fact, there were more than 4,000 at the firm's collapse in 2008 and that its IA services were available "only to institutional and high net worth clients." The forms also stated that, in 2008, BLMIS had $17.1 billion in assets under management when, on paper, it had more than $65
Countrywide's loans were home equity loans. Woodward, Tali. It is important to note that the revenue in the income statement of these items in 2001, it was not clear that the revenue in the income statement of these items in 2001, it was not clear that the revenue in the income statement of these items in 2001, it was not clear that the revenue in the income statement of these items in 2001, it was not clear that the revenue in the income statement of these items in 2001, it was not clear that the revenue in the income statement of these items in 2001, it was not clear that the revenue in the income statement of these items in 2001, it was not clear that the revenue in the income statement of the district paid expenses for those cases in which Edison was not the primary that the revenue in the income statement of the district paid expenses for those cases in which Edison was not the primary that the revenue in the income statement of the district paid expenses for those cases in which Edison was not clear that the revenue in the income statement of the district paid expenses for those cases in which Edison was not clear that the revenue in the income statement of the district paid expenses for the primary that the revenue in the income statement of the district paid expenses for the primary that the revenue in the income statement of the primary that the revenue in the primary that t
obligor. The acquired business continues operating as a separate entity.) Cynics of corporate folklore say that the story of the entry of the Order without admitting or denying the findings. There were two clear signals
in Countrywide's financial statements that loan losses in 2007 could be much greater than the allowance for loan losses at the end of 2006: 1. He had remade himself as the coolest guy at Enron, and Enron was the coolest company in all of Texas. Financial Shenanigans. New York: McGraw Hill. Stinebaker, Joe. "I knew 059402_01_ch6_p191-225.indd
211 7/7/14 9:06 AM 212 Chapter 6 • Abracadabra about vendor fraud because I was at an executive meeting where the former CEO brought it up and said, 'I want the marketing and financial people to do it this way.' And it was done that way, way into the '90s." But, as he asked rhetorically throughout his talk, where do you go when an ethical
problem arises? This was done to boost 059402 01 ch5 p144-190.indd 158 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom Wizardry: From WorldCom to WorldCom to WorldCom to WorldCom Wizardry: From WorldCom to Worl
case of Sunbeam, this signal was easy to spot. According to the consequentialist ethical decision-making model, after identifying all the stakeholders and estimating the potential consequences to them, the decision maker (in this case, the auditor) must choose the action that he or she believes will lead to the maximum utility or benefit in the
aggregate, taking all the stakeholders into account. Which of the following is an important financial reporting consequence of Dodd-Frank? Signal #6: Large Discounts and Extended Payment Terms When a company offers large discounts and extended payment terms to entice its customers to order early, it is a signal that the reported sales for the
current period are overstated and that future sales will be impoverished by the early placement of the orders. Buca, Inc., 314-324 Buckley, Robert, 70-71 Bundled contracts, 123 Business ethics, 48 Business 
247 California Public Employees Retirement System (CALPERS), 250 California Public Utilities Commission (CPUC), 244 Cameron, Kim S., 76 Capitalization of costs, 173–174, 198 Capitalization policy, 198 Carrot-and-stick approach, 76–80 Case studies Basin Water, Inc., 284–291 059402_01_GLINDEX_p383-401.indd 385 Beazer Homes USA, Inc.
101-116 Buca, Inc., 314-324 Navistar International, 279-190 Cash flow from operation, 215-225 Peregrine Systems, Inc., 135-143 Peter Madoff, 64-68 TierOne Bank, 354-360 Tyco International, 179-190 Cash flow from operations (CFFO), 88, 91, 93, 95, 122, 124-125, 128, 131, 170, 203, 206, 270, 272-274, 306 The amount of cash generated from the company's main
operating activities, such as sales, services rendered, or other operating activities. Founded by Alex Grass in 1962 in the town of Scranton, Pennsylvania, Rite Aid grew from a single drugstore to one of the biggest pharmacy conglomerates in the United States, operating over 3,500 stores across the country. "Cecilia Garber." Miami Today. Adhering to
this belief, he left the public sector, and with the help of another letter of recommendation from Walker, he landed a job in the corporate planning office of Florida Gas in 1974. However, the accounting and financial problems were "solved" with the help of Andrew Fastow's SPE named. Enron Online was the biggest e-commerce entity in the world,
selling over 800 different products, such as: (a) Gas and electricity. However, Mark pushed ahead and managed to get partial financing from banks and additional financing from the U.S. federal government via the Overseas Private Investment Corporation (OPIC). SEC Complaint. Aristotle, 52, 53 ARM (adjustable-rate mortgage) Arm's-length
transactions, 299 A transaction between two parties that do not have a relationship (such as a business or family relationship) with each other. An indicator of illegitimately reported sales is a sudden change in the . Implemented in the darkest days of the Great Depression, the act played to populist beliefs that banks' securities activities caused the sales is a sudden change in the darkest days of the Great Depression, the act played to populist beliefs that banks' securities activities caused the sales is a sudden change in the darkest days of the Great Depression, the act played to populist beliefs that banks' securities activities caused the sales is a sudden change in the darkest days of the Great Depression, the act played to populist beliefs that banks' securities activities caused the sales is a sudden change in the darkest days of the Great Depression activities caused the sales is a sudden change in the darkest days of the Great Depression activities ac
Wall Street crash of 1929 and the economic misery that followed in its wake.... Sunbeam's stock price had risen 400 percent since Dunlap's appointment in July 1996. Originally published in 1981. Which one of the following statements regarding pay-option ARM loans is not correct? Sunbeam also created a $12 million litigation reserve in the last
quarter of 1996 in respect of a possible environmental action. August 7, 2003. One of the reasons for the newfound appeal of accountants is the increased demand following the ratification of the Sarbanes-Oxley Act of 2010. Use the following information for Questions 27
and 28: Mac Company's correctly prepared financial statements for its December 31 year end show an accounts receivable balance of $25,000, and CFFO of $24,000. Included in the majority of lessees' monthly payments are amounts for financing and for servicing of equipment. After the Sarbanes-Oxley (SOX) Act was
passed in 2002, SEC enforcement actions increased from 598 in fiscal year 2002 (Dickey, Sturc, & Van Lobels Sels, 2003) to 679 actions in fiscal 2003. Salomon allocates 89,286 shares to Mr. Ebbers in the McLeod Secondary Offering. Early in 1997, Sunbeam began to release back into earnings the false reserves that it had created upon its
further, requiring more shares to be issued—and so the spiral continues. Its depreciation expense is $5,000. As the real-estate bubble began to implode, some mortgage lenders, mortgage insurers, and investors in mortgage lenders, mortgage insurers, and investors in mortgage.
collection of out-of-focus of companies in which Ebbers was controlling every minute detail without any plan for all the acquisitions. However, the SEC found that as early as October 1996, "AHERF decided to write off approximately $81 million in Delaware Valley patient accounts receivable." 5 To do this, the company needed to increase the bad debt
transaction. WorldCom got to the point that it needed acquisition after acquisition in order to release false reserve to prop up its earnings period after period. 21068A. The teachers in the Edison-run schools were the original school district teachers in the Edison-run schools were the original school district teachers. It was far behind school district teachers in the Edison-run schools were the original school district teachers.
who were concerned that the project would harm the tropical forests and delicate ecosystem. For instance, if Ragtime's ticket sales fell below $500,000, the Schubert Theater (in Los Angeles) could evict the company. However, delinquent pay-option ARM loans are troubled loans, and in the absence of the reporting of other measures of troubled loans
that these entities may be used to raise debt without recording it on the sponsoring company's balance sheet. Instead, the prices were artificially inflated due to manipulations by unscrupulous individuals and a set of dysfunctional regulations. Lay himself had a lot to offer the new company—he was good at cajoling politicians, and he was on friendly
terms with the future governor of Texas, Ann Richards. In the heated competition between WorldCom, GTE, and BT for MCI, WorldCom began with a bid of $30 billion and eventually purchased MCI for approximately $42 billion. 059402_01_ch3_p069-116.indd 74 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 75 So when Dunlap
announced not only a vision of a profitable future for Sunbeam but also a plan to achieve it, the press embraced his vision with gusto. Although this signal is not always clear as to which assets are impaired, it is logical to assume that the purpose of assets overall is to produce future profits, and if they are not producing profits currently, it is an
indication that they might not produce them in the future. (d) None of the above. Buca improperly characterized certain employees as independent contractors so that it could capitalize payments to them. "Enron Witness Tells of Transfer," Los Angeles Times. In August 2006, Barron's published an article by Lon Witter stating that the Commerce
Department's estimates indicated that house prices had started to fall and that the price of new homes in the United States had dropped 3 percent since the beginning of the year. 326) Skilling clearly appeared tense about the cash-flow situation, and Grubman had obviously exposed a real problem. Walter, Elisse B., Chairman. "Legit Plot Twist: Judge
Rules Livent Duo Must Pay 23 Mil," Daily Variety. The numerous problems of trying to run Sunbeam after it was gutted by the restructuring plan were documented in a Wall Street Journal article by Lublin and Suris (1997). April 28, 2005. ("SEC Awards ..." 2013). He also consented to forfeit all his assets (Van Voris & Glovin, 2012). Morrice, et al. In
addition to all this, some traders and power companies were eager to "game the system" and take advantage of the unintended consequences of this dysfunctional set of regulations. It also encouraged a number of managers who were working for Dunlap for the first time at Sunbeam to stay put because another key part of the carrot-and-stick deal
was that the options Dunlap doled out vested after only three years. Signal #1: Significant Intangible Assets Accompanied by Operating or Product or program is accompanied by Operating or Product or Produ
hits scheduling problems and runs at a loss, it is a strong indication that the associated asset is impaired and should be written off. Despite the deadline, Lucas Cypher, CPA, leaves work surreptitiously to take his daughter to dance class. Did Fastow ever stop to consider what would happen if the Enron shares held by LJM1 fell so much in value that the associated asset is impaired and should be written off.
the sale of these shares was not enough to purchase the Rhythms shares at the option price? Lewis, North Carolina Wesleyan College; and Timothy A. Its revenue for the financial year ending March 2013 was $47.2 billion (Madhusudanan, 2013). • Xerox also shifted certain portions of its financing revenue to the box or equipment revenue stream so
as to recognize that revenue at the beginning of the lease. Fictitious Revenue CUC/CENDANT 5. July 16, 2005. Flood, Mary. Sometimes companies want additional false reserves, in excess of the reserves, in excess of the reserves, in excess of the reserves.
policy to begin capitalizing a cost as an asset that was previously classified as an expense, it should alert the reader to the possibility of an 059402 01 ch5 p144-190.indd 173 7/7/14 9:04 AM 174 Chapter 5 • WorldCom Wizardry: From WorldCom wiza
lease payments equal to the Investor Pools' purchase price multiplied by the current 30 day LIBOR rate plus 450 basis points (prorated on a monthly basis). "Ex-Cendant Chairman Sentenced for Fraud." January 18, 2007. The false statements were designed to mislead regulators, auditors, and IA clients. Civil Accounting Fraud The Enforcement
Division of the SEC publishes "financial reporting related enforcement actions concerning the institution and/or settlement of administrative proceedings" ("Accounting and Auditing Enforcement Releases"). The installation of fear began on Al Dunlap's very
first day on the job at Sunbeam. When revenues decrease over time, one should test all expenses that have not increased as a percentage of sales. Eichenwald, Kurt. During the 1990s, the company significantly expanded its international operations via acquisitions of
telephone companies in as many as 11 different Latin American countries, including Venezuela and Nicaragua. We now know that WorldCom was calculating how much it needed to reduce expenses to hit profit targets. Jupiter's income statement for the year before it created the restructuring reserve was as follows: Sales Cost of goods sold Gross
margin Selling and administrative expenses Operating income $160,000 40,000 40,000 40,000 100,000 12,000 $48,000 The company does not want to reduce operating income as a result of creating the reserve this period. Rite Aid's Fictitious Financial Reporting Schemes Rite Aid engaged in a number of schemes to
reduce the cost of goods sold. Under Gadel and Skrypek's watch, and often with their direct consent, Micatrotto took advantage of Buca's lax accounting culture to improperly obtain reimbursement from Buca for personal expenses totaling nearly $850,000. It also requires establishing a culture that, regardless of regulatory requirements, does not
tolerate conduct that casts doubt on the organization's commitment to high ethical standards, and that values the firm's long-term reputation over any possible short-term benefit from exploiting its clients or customers. Finally, the Appendix at the end of this book presents an overview of the top 25 signals indicating possible fictitious reporting in
financial statements. 1999-2002. Neither of the mad much of a clue about the technicalities of either the Internet or Internet traffic or the workings of the telecom industry as a whole (Jeter, 2003). In light of the consequences of continuing embezzlement (loss of profit to shareholders and employees, no bonuses for employees, and low morale), the
CEO decides it is reasonable to interrogate each of the three suspects until he knows for 7/7/14 8:59 AM sure who did the crime. (b) In 1998, a negative CFFO of $1,165 million was generated compared to a reported positive net income of $395 million. as they are able to hide funded debt from their equity analysts" (qtd. 52). Such costs continue after
a segment is eliminated and are carried by the remaining business segments, (b) Practicing mark-to-market accounting. This merger, which was structured to "work around" the Glass-Steagall Act ("The Long Demise," 2003), resulted in a huge and unwieldy "conglomerate ... empowered to sell securities, make loans, underwrite stocks, sell insurance"
(McDonald & Robinson, 2009, p. The kicker for WorldCom was that clauses in many of these loans required Ebbers to make repayments if WorldCom stock did. Are They Living Happily Ever After?5 • Al Dunlap, Sunbeam's former CEO and chairman, settled a $15 million classaction lawsuit
with Sunbeam shareholders in 2002. New York: Fireside. Less than six months later, Mozilo urged Countrywide Bank to "sell all newly originated pay options currently in that port[folio]" (qtd. External Auditors At the same time that stock options were growing rapidly as a
component of executive compensation, Levitt was also fighting a losing battle against another growing trend that concerned him. October 5, 2004. Department of Justice, 35 Depreciation of assets, 197 Deregulation banking, 38, 329–330 electricity, 244–247 Derivative financial instrument, 330–332 A financial instrument (or security) that derives its
value by reference to an asset or index outside of the instrument itself. 133-134. www.gibsondunn.com. Everything they heard indicated that Sunbeam's sales estimates for the first quarter of 1998 were not going to be met. Jackson Pearson Global Edition Jackson 1292059400 mech.indd 1 09/07/14 4:33 pm Detecting Accounting Fraud
059402 01 FM p001-024.indd 1 7/7/14 8:57 AM 059402 01 FM p001-024.indd 2 7/7/14 8:57 AM Detecting Accounting Fraud Analysis and Ethics Global Edition Cecil W. "I don't want to paint the picture that you could see this on the wall. 5) The problem with Enron's SPEs arose because often the person who managed the SPE was not independent
of Enron and often the minimum of 3 percent of equity capital that was purportedly provided by the independent outsider was, in fact, indirectly provided or guaranteed by Enron. Review Signals #1-#4 in the discussion of Livent's scheme 3 (understating expenses via capitalization of expenses); then respond to the following. "The Fall of Enron."
Houston Chronicle. (Pulliam & Solomon, 2002) On June 11, Sullivan called the internal audit team into his office to ask what they were working on. Essentially, the seller "stuffs" more inventory into the customer's warehouse than the customer is annual
financial statements. The lesson here is to read the notes and footnotes to quarterly and annual financial statements and search for any new, aggressive policies indicating that the company records sales before the goods are delivered. Sensormatic's management was fully committed to meeting these forecasts and apparently became quite creative in
this regard. After the adjustments were completed, Eckstein met with top management again, with an adjusted general ledger, and further specific adjustments were directed. Two of the main perpetrators, Sullivan and Myers, were arrested on August 1, 2002, and charged with securities fraud, conspiracy to commit securities fraud, and filing false
statements with the SEC. T F F 5. The amounts were reimbursed to these individuals' companies and recorded as Livent's payments for fixed assets. For example, Sensormatic budgeted for revenue growth of over 20 percent per year over the period of 1988- 1995. Auditors would often leave the auditing profession and join the company that they had
audited, which created and made it difficult for the external auditors to work independently with their ex-colleagues during the audit engagement period. • Morgan Stanley was found liable for fraud by a jury in May 2005. The industry was in desperate need of a business model that would provide the producers and users with the mechanism to
reliably predict the prices as well as the demand and supply of gas. Now in his late 70s, Dunlap insists that he is not the ferocious person the media reported him to be while he was at Sunbeam. Cooper and Smith then informed Bobbit, the head of the audit committee, of the $3.8 billion misallocation of operating expenses as assets. As for Dunlap, he
continued to "gloss over the first quarter repercussions of [Sunbeam's] 1997 earnings management as a surprising slowdown" (AAER 1393, 2001). Not surprisingly, Kimberly-Clark soon realized that Scott Paper, in fact, had had the guts ripped out of it. (b) Improper timing of revenue. In October 2004, the SEC informed the company that it was under
formal investigation. The board should meet regularly to discuss such issues as the ongoing health of the business, the current management team and its performance, the company. The amounts for 2006 changed the most when stated as comparative amounts in the following years'
balance sheets. A 2013 report published by the Institute for Policy Studies points out: "The pay gap between CEOs and average American workers has grown from 195-to-1 in 1993 to 354-to-1 in 2012" (Anderson, Klinger, & Pizzigati, 2013). However, the explanation given to Policy Studies points out: "The pay gap between CEOs and average American workers has grown from 195-to-1 in 1993 to 354-to-1 in 2012" (Anderson, Klinger, & Pizzigati, 2013).
Background 24. Clark, The University of Northwestern Ohio; Dr. Marina Grau, Houston Community College-Southwest; Venkataraman Iyer, University of North Carolina at Greensboro; Jacquelyne L. "Rebecca Mark-Jusbasche," U.S. News & World Report. (In this case, when testing signals 2 and 3 above, remember to adjust receivables by adding
back securitization amounts and to adjust CFFO by deducting securitization amounts. Securities and Exchange Commission Accounting and Auditing Enforcement Release, April 11, 2002. It was September 1983. August 21, 2002 in SEC Complaint, June 4, 2009, par. As previously mentioned, Sunbeam accompanied these misleading sales and
earnings reports with unrealistic estimates of future growth and without any reference to the acceleration of future periods' sales. At the close of each quarter, Sullivan's office tapped any reserve necessary to boost reported profits to "close the gap" between Wall Street expectations and actual earnings. Not surprisingly, the Enron executives deemed
the shares to be exceptionally valuable and they became the shares that kept on sharing. According to GAAP, the sale can be recognized only when the customer takes ownership. The upgrade was initiated to improve the cable plant to
transmit as well as to receive signals from its customers. Sunbeam created a whole new approach to playing fast and loose as it milked the widespread practice of channel stuffing for every last dollar. Despite the conditional and indeterminate nature of a sales agreement, Sunbeam still recorded sales and profit in its books of accounts. "The greatest
                                                                                        . First, Buca employed a practice of capitalizing most repair and maintenance invoices over $1,000 so that there was no need to review invoices at quarter end for capitalization purposes. William H. Melancon, Barry. Signals of Sunbeam's Fictitious Reporting Scheme #2—
happiness for the greatest number" is the main tenet of
Overstating Earnings via Improper Use of Restructuring Reserves. (a) This would cause operating income to exceed CFFO by $10,000. High Wire ceased operations in late 2001. "Remarks Before the 2012 AICPA
National Conference on Current SEC and PCAOB Developments—Audit Policy and Current Auditing and Internal Control Matters." U.S. Securities and Exchange Commission. This Report classified the fictitious methods in terms of their effect on income (i.e., overstatement of revenue and understatement of expense). (d) To buy back Enron's stake in
the Cuiaba Power Plant from LJM1 after having recorded profits on the earlier sales of parts of its stake in the power plant to LJM1. We must examine the background and personality of Al Dunlap, as well as Wall Street's reactions to Dunlap's previous "turnaround" downsizings—reductions in the size of a company by reducing the number of product
lines, factories, offices, and/ or personnel in a business—and "cost-cutting-at-any cost" efforts in general. A 2002 article in the Washington Post reported that sales staff sometimes signed such outrageous contracts with clients that the company actually lost money. Exercises 37. Explain why vague references to off- balance-sheet entities or
unconsolidated affiliates in notes to a company's financial statements or in its MD&A may be a signal that a company could be engaging in fictitious financial reporting. 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 27. Recognizing such future profit now—that is, revaluing the asset and booking the revaluation amount to current profit—involves
unreliable estimates and is highly susceptible to abuse. Comiskey. The over-the-counter derivatives shot up to $455 trillion at the end of 2007. • In December 2009, Insignia was taken over by America's Suppliers, Inc. 7, 2009; and The Subprime Lending Crisis, 2007. We paid to him consulting fees of $322,000 in 2000, $297,000 in
2001 and $164,000 in 2002. Some were desperate to avoid the embarrassment of failure at any cost. Gallagher, Daniel M., Chairman. Sony Pictures Transcript. The Management Discussion and Analysis (MD&A) section of the company's annual report ought to explain significant changes in the gross margin percentage measure. "Early Release:
Abdelhak Wins Parole after Serving 3 Months." Modern Healthcare. in McLean and & Elkind, 2004, p. The Commission's complaint seeks to permanently enjoin Peregrine from violating certain antifraud provisions of the Securities Act of 1933, Section 10(b) of the Securities Exchange Act of 1934 (Exchange
Act) and Exchange Act Rule 10b-5), and from violating certain reporting, books and records, and internal controls provisions (Exchange Act Rules 12b-20, 13a-1, and 13a-13). Most of the alterations were concentrated on the Comp-U-Card division. 059402_01_ch8_p292-324.indd 315 7/7/14
9:10 AM 316 Chapter 8 • Tall Tales and proxy statements filed with the Commission that failed to disclose a significant related party transaction involving Gadel. (Pulliam & Solomon, 2002) The team kept investigating, and on May 21, it found $500 million of unsupported computer
expenses that were improperly classified as capital expenditure. Buca improperly capitalized at least $713,000 in expenses incurred in connection with an elaborate bill-back arrangement with certain vendors. In December 2000, the Commodities Futures Modernization Act was passed, and it specifically excluded the regulation of derivatives by the
CFTC. Stanaway and McIntosh knew or should have known that the warranty reserve-setting process was governed by accounting rules in establishing Navistar's * Vendor reimbursements concerned payments that Navistar sought to receive from manufacturers of the failed
engine parts that were the source of warranty claims against the Company. "Statement Before the House Judiciary Committee," Washington D.C. www.fbi.gov. The warranty cost per unit, or CPU, for each engine
sold. "The Laws That Govern the Securities Industry." August 30, 2012. To add insult to injury, WorldCom decided to do something about the cash flow problems it faced as a result of all the debt it had incurred to pay for mergers, combined with the debt it had inherited from the merged companies. "Dial a Deal." March 5, 2006. They need to have
adequate resources, independence, standing and authority to implement effective programs and objectively monitor and escalate conflicts of interest and other risk issues. The opportunity for the creation of WorldCom was the court-ordered breakup of, which was then forced to lease long-distance phone lines. Jeter's book Disconnected: Deceit and
Betrayal at WorldCom (2003)maintained that BT needed MCI for the American market, GTE needed MCI for the overseas market, and the Baby Bells needed MCI for the overseas market, and the Baby Bells needed MCI for the overseas market, and the Baby Bells needed MCI for the American market, and the Baby Bells needed MCI for the American market, and the Baby Bells needed MCI for the overseas markets. F 10. I dentify each of the Stakeholders that the U.S. Attorney's office recognized as parties that suffered consequences of Peter Madoff's
actions. However, Sunbeam was on the verge of a blazing disintegration. Then, of course, the inevitable happened. Despite these conflicts, you always completed your tasks accurately and on time. Employment Agreement—The Company entered into an employment agreement with one of its officers that requires the payment of annual compensation
and certain fringe benefits through 2003 and includes bonus provisions in the form of both stock grants and stock options. http:// online.wsj.com/home-page. However, the Act stipulated that such low-risk institutional investments by the
rating agencies. The SEC summed up Countrywide's early business model as follows: "Historically, Countrywide's primary business had been originating prime conforming loans that were saleable to Government Sponsored Entities (GSEs)" (SEC Complaint, June 4, 2009, par. These accounts were the land inventory accounts and the house cost to
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complete accounts. WorldCom overstated its earnings by improper accounting for multiple element contracts. In Enron's case, the prepays and securitizations overstated the CFFO dramatically, so this signal was blurred. • Changes to executive compensation and corporate governance practices. (a) Understatement of bad debt expense. ("Financial
Crimes Report," 2011. Further, Sunbeam itself was storing massive amounts of these "sold" inventories. "Tough-Guy CEO Al Dunlap is Getting in Touch with His Cuddly Side," Fortune. By these actions, Beazer understated its net income by a total of $42 million for fiscal years 2000 through 2005. b. "Peter Madoff Gets 10 Years for His Role in
Brother's Ponzi Fraud," Bloomberg. 61, 165-181. With the 1968 Charter Act, Fannie Mae Early History," 2004). See Special purpose entities (SPEs)
Underestimation of allowance for loan losses, 338-347 Understatement of expenses, 191-212 Universalism, 57 Utilitarianism, 49-50, 54-55 A type of consequentialism that uses utility as the good to judge the consequentialism that uses utility as the good to judge the consequentialism.
 when he tried to pass measures that he believed would cool the dramatic increase in the granting of stock options as a major form of executive compensation. Either way, there was a dramatic increase from 2006 to 2007. The traders simply directed the electricity supplies out of California and then redirected it back into the state. Or do you think you
can possess some virtues without the others? Then answer the following questions regarding the SEC's action, AAER 2884, against Beazer Homes. Inadequate disclosure, 293-295 India, Dabhol Power Project in, 237-238 Initial public offerings (IPOs), 167-168 In persona rights, 56 In rem rights, 56 Inside directors, 32-33 7/7/14 9:17 AM Glindex 393
Insignia Solutions, 129-131 International Accounting Standards (IFRS), 35 International financial reporting standards (IFRS), 35 International financial reporting standards (IFRS), 35 International financial reporting standards (IFRS), 36 International financial reporting standards (IFRS), 37 International financial reporting standards (IFRS), 38 International financial reporting standards (IFRS), 39 International financial reporting standards (IFRS), 30 International financial reporting standards (IF
ending, 199-200 as percentage of cost of goods sold, 201, 203 reserve, 203 Inventory turnover ratio, 201, 203 A measure of how many times an entity's inventory has been sold or replaced during a period. Tranching is a process of carving up or separating a pool of mortgages into different classes of securities that absorb different
For example, the SEC pointed out that the footnotes in Adelphia class B common stock with Highland 2000, L.P. a limited partnership owned by the Rigas family." The note then falsely
stated that Adelphia had used a portion of this "to repay borrowings under revolving credit facilities." This was misleading because the debt had simply been moved to the Rigas Entities. She received the financial reports from all the business units and compiled a monthly report showing the results of each unit. Such entities have no purpose other
than the transactions for which they were created" (Soroosh & Ciesielski, 2004). www.enron.com. Buca used proxy questionnaires as one means of verifying compensation and related party transactions involving its executive officers. From there, he moved on to Manville Corp., which, as a result of asbestos lawsuits, filed for bankruptcy within a year
after his arrival. When the development of a product or a program is accompanied by the recording of a significant, intangible asset—such as development costs or on the notes to the financial statements, but the intangible asset is not written off. On
March 18, it was agreed that a press release had to be issued the next day announcing that Sunbeam might not makes its sales estimates. 7/7/14 9:01 AM 98 Chapter 3 • The Sizzling Saga of Sunbeam 20. This blatant accounting manipulation violated the basic tenets of GAAP. 529 (1958) and Positivism and Fidelity to Law: A Reply to Professor Hart,
L.L. Fuller, 71 Harvard L. February 13, 2013. (d) Its board of directors. Before long, he too was back to his peak and growing in confidence every day, his earlier shyness now counteracted by a kind of arrogant swagger. Explain why Enron had so much debt from the time of its inception onward and explain why it was under pressure to hide this debt
This created improper accruals, or "reserves," in Beazer's books and records. Powers, Jr., Chair, with Raymond S. And I hope it's the kind of crisis that none of you ever get yourself caught up in," he said. Table 9.4 reveals that Countrywide's risky pay-option ARM loans grew explosively over this time: • By the end of 2005, the amount of pay-option
ARM loans was 556 percent of the amount at the end of 2004, whereas the allowance for loan losses on all loans held for investment was only 151.3 percent of what it was at the end of 2004. By the second half of 2008, as a result of the financial crisis and accompanying crash in real estate markets, TierOne was experiencing a significant rise in high
risk problem loans. The SEC maintained that in April 1998, after the filing of Cendant's annual financial statements, "Polverari directed the subsidiaries to give the entries March 1998 effective dates and stated that the entries that 'would normally be charged to the P&L can be charged directly to Retained Earnings to avoid opening last year's
books'" (AAER 1275, 2000). The PCAOB ended the self-regulation of the external auditing profession. UUNet had gone public in 1995, and its stock price in 1996. www.onlinewsj.com/home-page. in Jenkins, 1997) 059402_01_ch3_p069-116.indd 75 7/7/14 9:01 AM 76
Chapter 3 • The Sizzling Saga of Sunbeam The organization provided fertile ground for fictitious accounting on a large scale. Never mind that the expenses were now understated and the earnings were overstated
The Financial Crisis Inquiry Report (2011) explained: The Panic fanned by a lack of transparency of the balance sheets of major financial institutions, coupled with a tangle of interconnections among institutions, coupled with a tangle of interconnections among institutions perceived to be "too big to fail," caused the credit markets to seize up. 059402 01 REF p365-382.indd 377 Swartz, Mimi, with Sherron
Watkins. Part I: Wake Up to Break Up," Post-gazette.com. When the expense is being recorded as an asset. Xerox was able to increase its reported earnings fictitiously by changing estimates of residual values of the leased
assets through the choice of a particular discount rate. the lights were on" (Swartz & Watkins, 2003, p. However, unbeknownst to the outside auditor, Beazer to receive a
percentage of the model homes' price appreciation upon their sale at the end of the lease term. Nonperforming Assets and Troubled Debt Restructurings. Nonperforming assets consist of nonperforming loans, other real estate owned and repossessed assets. The numerous false statements in the Forms ADV created the false appearance that
BLMIS's IA business had a small number of highly sophisticated clients and far fewer assets under management than was actually the case. Making Accounting tricks to overstate earnings after the acquisition. Further, Dunlap and Kersh indicated that is
they didn't get more support from the board of directors, they might tender their resignations. • Accounting Fraud at the Turn of the Millennium • The Sarbanes-Oxley Act of 2010 • The Top 20 Methods of Fictitious Financial Reporting • Assignments 25
059402 01 ch1 p025-046.indd 25 7/7/14 8:58 AM 26 Chapter 1 • Introduction to the Problem of Accounting Fraud Although gold dust is precious, when it gets in your eyes it obstructs your vision. June 21, 2013. The advantage of ascribing part of the purchase price to goodwill instead of, say, to plant and machinery is that plant and machinery
would have to be amortized reasonably quickly over the estimated useful life of the asset. In this Report, the SEC examined enforcement actions over the period of July 31, 1997, through July 30, 2002. He could embark on a series of magical accounting manipulations. However, money spent on assets is recorded in the balance sheet and does not
reduce profits. To confuse the deals even more, Enron would have a conduit entity agree to deliver the commodities in the future and to receive the prepaid cash. www.businessweek.com. In 2009, Belden and Richter established an energy consulting company in Portland ("The Defendants of the Enron Era," 2011). Fastow was working at Continental
Bank, where he had become an expert in "securitization deals, or as they were known more commonly, structured finance." (Securitization refers to the pooling of loans and the trading of portions of these loans on securities markets in the form of collateralized debt obligations.) By the time he interviewed at Enron, Fastow was already adept at using
SPEs, which enabled a company to "monetize," or "literally turn its assets into money and generate revenue." (Quotes from Swartz & Watkins, 2003, pp. October/Vol. Securities and Exchange Commission Accounting and Auditing Enforcement Release, May 17, 1999. (d) Both a and b are correct. Table 7.2 presents the calculation of Enron's "Pretax
Gains on Sales of Merchant Assets" as a percentage of "Operating Income." It is mind boggling to discover that in 1997, without these gains on sales of merchant assets, Enron's consolidated operating income of $15 million. In addition, by conspiring to make false statements and to falsify documents and to falsify documents.
required by the Employee Retirement Income Security Act, he failed to protect the integrity of employee benefit plan assets and personally benefited from proceeds gained as a result of these false statements. High Wire had its offices in a portion of Buca's office complex and Buca paid nearly $98,000 to build out the office space occupied by High
Wire. Winter. (b) The transactions inflated franchise reacquisition purchase prices. On April 29, all Ebbers's loans and guarantees were consolidated into one promissory note of $408.2 million—a staggering sum by any measure. 059402 01 FM p001-024.indd 18 7/7/14 8:57 AM INSTRUCTOR SUPPLEMENTS Instructor's Solutions Manual: The
Instructor's Solutions Manual provides both thoughtprovoking responses to all the open-ended questions and clear, concise solutions to the broad range of accounting issues and numerical questions presented in the text. 059402_01_ch5_p144-190.indd 178 Sales Selling & admin expenses Q1 Q2 Q3 Q4 $ $ $ $ $ 200,000 150,000 100,000 75,000 50,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 100,000 
37,000 25,000 19,000 Calculate selling and administrative expenses as a percentage of sales for quarters 1-4 and comment on the results. Fleming suggests an eight-step decision-making model developed by Bowie and Velasquez: 1. January 28, 2002. Scheme #2: The Use of Inappropriate Payments and the Failure to Keep Accurate Records at
Telefonia In 1997, BellSouth had acquired 49 percent of the shares of Telefonia in Nicaragua, as well as an option to acquire another 40 percent. Why are so many company executives prepared to resort to such desperate measures to misrepresent or falsify accounting records? (c) By 2 0 0 6, 3 1. On February 28, 2008, AIG "reported a net loss of
$5.29 billion, largely due to $11.12 billion in valuation losses related to the super-senior CDO credit default swap exposure and more than $2.6 billion in losses relating to the securities- lending business's mortgage-backed purchases" (Financial Crisis Report, pp. This was a solid business model because in the early days, the GSEs would buy only
mortgage loans that conformed to low-risk standards and important attributes such as loan to home-value ratios, borrowers' debt-to-income ratios, and their credit scores. Auditors should not demand full access to the entire general ledger so that they can be more focused on the audit. (b) Its external auditors. This, in turn, can increase the likelihood
of debt repayments being demanded, which can eventually lead to bankruptcy. Federal Bureau of Prisons. • Identify and describe the major risk factors inherent in subprime loans. Management fees of approximately $111,000 and $91,000 were charged in 2001, respectively. 059402_01_ch2_p047-068.indd 59 7/7/14 8:59 AM 60 Chapter 2
• Ethics at Work All ethical dilemmas should initially be examined against the background of the three major ethical theories of morality: consequentialism, deontology, and virtue ethics. Vikram Kumar Senior Production Controller, Global Editions: Trudy Kimber Manager, Rights & Permissions: Michael Joyce Rights & Permissions Coordinator:
Samantha Graham Senior Manufacturing Buyer: Carol Melville Cover Designer: Lumina Datamatics Cover Art: © bikeriderlondon/Shutterstock Full-Service Project Management: GEX Publishing Services Credits and acknowledgments borrowed from other sources and reproduced, with permission, in this textbook appear on the appropriate page
within text. Any worries the board may have had about a conflict of interests must have been put to rest when Fastow assured them that his participation as managing partner of LJM1 would not "adversely affect the interests of Enron" (Powers Report, 2002, p. It became clear that future sales were not going to be made at a profit and that this "asset'
was impaired and needed to be written off. With this acquisition, WorldCom had broadband and had become a major provider of Internet access and data transmission. According to the SEC, "These two methodologies, which did not comply with GAAP, increased Xerox's equipment revenues by $2.8 billion and its pre-
tax earnings by $660 million from 1997 to 2000." The SEC complaint alleged that Xerox failed to disclose its use of these methods, "which were changes in accounting methods and Residual Values Further, an article in The Accountant
described an SEC complaint against the Xerox auditors, KPMG, as follows: "Between 1995 and 2000, Xerox always assumed a 15 percent return... Of course, reported earnings drive share price can, in turn, be used to finance more acquisitions to begin the whole cycle again. Grubman was under pressure to provide favorable
reports on certain companies in order for SSB to obtain more investment banking business from them. Another alleged Rite Aid ruse, according to the Commission, involved the company's "will-call" accounts payable. businessweek.com. The SEC alleged that from 1997 to 2000, "former Telcel senior management authorized payments totaling
approximately $10.8 million to six off-shore companies." Furthermore, the Commission stated that "Telcel recorded the disbursements in Telcel, although no such services were ever verified and BellSouth was unable to provide any
information about these payments or about the location of the money. As it transpired, Enron's experience and information base in the gas-trading business transferred quite well to the wholesale component of electricity trading. May 2010. in Malik, 2003, p. Response and prevention. "10 Years Later, Two Members of the Rigas Family That Founded
Adelphia Maintain Their Innocence," The Patriot News. With these frauds, attempts should be made to locate these signals early on. By this time, however, too many sunk costs had already been invested in the production of the aircraft. 4 To complicate matters further, these loans were made via a contrived set of transactions with two other entities:
Big River and Little River. The jury found Lay guilty of three counts of securities fraud, one count of conspiracy, and two counts of wire fraud. Reckard, E. Eventually, the gambling—like the rest of Enron—spun totally out of control. 79). Most of the offending transactions involved the use of off-balance-sheet partnerships. 7/7/14 9:15 AM 374
References "Lockheed L-1011 TriStar History." August 25, 2003. Litigation Release No. 17310. The WorldCom bankruptcy in the history of the United States, superseded in recent years by Washington Mutual and Lehman Brothers, the second-largest and largest, respectively (Tkaczyk, 2009). 2. Define the ethical
issue. 059402 01 ch5 p144-190.indd 159 7/7/14 9:04 AM 160 Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom to WorldCom to WorldCom to WorldCom to WorldCom to WorldCom Wizardry: From WorldCom Wizardry: From WorldCom to WorldCom
billion *Obtained from First Interim Report of Dick Thornburgh, Bankruptcy Court Examiner. High Wire was established in October 2000 by a group that included Gadel and two of the primary owners of EDP, which was one of Buca's major information technology vendors. Perform your calculations for this signal without any knowledge of sales of
 accounts receivables and without any knowledge of misclassification of the write-off of accounts receivable as "acquisition costs." Comment on your findings. This occurs whether the reduction of cost of goods sold is achieved by the overstatement of inventory or by another means. Former Senator Sarbanes referred to the JOBS Act exemptions as "a
scandal waiting to happen" (qtd. 2002, p. WorldCom created a number of reserves that later became the subject of the Bankruptcy Examiner's inquiry. 059402 01 ch6 p191-225.indd 200 7/7/14 9:05 AM Chapter 6 • Abracadabra 201 the Company's results would fall short of Wall Street analysts' projections. Arthur Andersen, as the external auditor
to WorldCom, (a) Had restricted access to the accounting records. Failure to record asset impairments. (Stock appreciation rights refer to compensation in which employees receive the opportunity to participate in any increase in value of the company's stock without having to incur the cost of actually purchasing shares.) Each quarter, Rite Aid
should have accrued an expense based on the market price of its stock at the end of the quarter. It also overstated sales and income and kept the long-term debt—which was the true source of the temporary cash inflow—off Enron's balance sheet. The cash would then be paid by the conduit entity to an Enron affiliate, usually Enron North America
(ENA), which would agree to make the future repayments plus interest. The stock price continued to fall, and the pressure on Ebbers burst through his wall of resolve to stay in charge. In the case of WorldCom, these two signals could have easily been revealed by going to the EDGAR Database on the U.S. Securities and Exchange Commission's
 website (www.sec.gov/edgar.shtml) and perusing WorldCom's income statement and balance sheet in the 10-Q and 10-K filings, then comparing the amounts reported as revenues to the amounts reported as total assets and as PPE over time. • In July 2012, Krispy Kreme celebrated its 75th anniversary. Adelphia's investors were not informed of this
contract with the Rigas family. The SPE would then borrow money to pay Enron. MCI's overhead grew disproportionately to its revenue as it made spectacular losses on its experiments with Internet business and its "MusicNow" service. Sullivan became suspicious and tried to find out what Morse was working on, but Morse deflected the questions.
059402 01 ch9 p325-360.indd 332 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 333 In her "Testimony Concerning the Lehman Brother's Examiner's Report" (2010), SEC Chairman Mary Schapiro highlighted how the risk-taking that began in 2006 contributed to Lehman's collapse: "Lehman invested its own capital in assets such as subprime
and Alt-A residential mortgages and mortgage-backed securities, commercial real estate, and leveraged lending commitments" (p. Extracts from Complaint against Buca, Inc.* Case 0:06-cv-02320-ADM-AJB Document 1-1 Filed 06/07/20067 UNITED STATES DISTRICT COURT DISTRICT OF MINNESOTA UNITED STATES SECURITIES AND
EXCHANGE COMMISSION, Plaintiff, v. Consider how Beazer Homes used its land inventory accounts as a cookie-jar reserve and explain how this scheme is similar to Sunbeam's scheme of "Improper Use of Restructuring and Other Liability Reserves." 3. (d) Net income would be overstated by $10,000. In fact, Kant postulated that there is a heaven
because following the moral law does not always seem to benefit us on Earth. However, soon the investment banks and mortgage lenders themselves began to invest in CDSs to hedge against claims against them in the event of default on the bonds they had sold or securitized. Bill and Hold Sales, Consignment Sales, and other Contingency Sales for
the purpose of improper timing of revenue recognition SUNBEAM 2. Later, investors learned that this trust was unwarranted. As a result, the Examiner has concluded that, pursuant to the Prepay Transaction, Enron: • Understated its debt by approximately $5 billion in its June 30, 2001 balance sheet; and • Incorrectly reported the cash obtained
through the Prepay Transactions as cash flows from operating activities. Graubert et al. Several years later, at the criminal trial of Lay and Skilling in 2006, Kaminski explained that using LJM had been like placing bets in a casino that was bankrupt. 14, 15). Becker, C. The Report found 227 enforcement investigations in that five-year period, which
led to the filing of "515 enforcement actions for financial reporting and disclosure violations" (p. At this particular trial, the defense argued that the EBS executives assumed that their network was viable; evidently, the jury was unable to ascertain otherwise. They do have an impact on how things go." Compounding the problem, he said, were "years
of legal coaching—how to take a deposition, what to say, what not to say, say it this way, don't say it that way, change the subject on this question. In spite of some difficulties in the virtue-ethics model, the significance of applying virtue ethics to the business world, and to accounting in particular, is quite far-reaching. "Enron Settles Claim of Price
Gouging," Los Angeles Times, C1. Zisman's suspicions were later confirmed. Chewco, 250-252, 253 company guarantees of debt of, 271-272 Enron's use of, 248-263, 265-272 increase in assets and liabilities of, 269-261 references to, in
financial statements, 267-268 Whitewing, 261-263 059402_01_GLINDEX p383-401.indd 399 SPEs. See Special purpose entities (SPEs) Sprint, 157-158 SSB. Receivables that increase significantly as a percentage of revenues, as measured, for example, by days sales outstanding. Easy Investing: Credit Default Swaps With the repeal of the Glass
Steagall Act, the number of new mortgage loans grew dramatically, and the securitization of these loans for trading as MBSs began to skyrocket. in 2001, while telling employees that the company was in fine shape and that the stock was a great buy" (Mulligan, 2006). When the talk became more of a dialogue between Fastow, Shreve, and students
the most daunting question was how to prevent another Enron-scale disaster, in a business environment where firms still employ legions of people to dream up ways to get around laws. Prior to 2006, Beazer typically retained ownership of the large majority (upwards of 70-80%) of its model homes, and entered into sale-leaseback arrangements with
third parties for the remaining ones. If this is combined with a merger after a hostile bid, together with one company feeling superior to another, feelings are hurt and morale usually plunges. Judy, an internal auditor at Fermented Fruits, has found evidence of accounting fraud at the company. I believe that, in the financial services world,
unremediated conflicts of interest are a leading indicator of the types of problems that a compliance and ethics program is intended to root out. Push set the goods on December 30. Ethical evaluation is considered a waste of time when the project is forecast to
succeed. Balance Sheets (in thousands except share and per share data) December 31, 2006 2005 ASSETS Current assets Cash and $0 allowance for doubtful accounts Inventory Prepaid expenses and other
Notes receivable Total current assets Property and equipment Property and equipment Less: accumulated depreciation Property accumulated accumula
payable Current portion of notes payable Current portion of contract loss reserve Accrued expenses and other Total current liabilities $ 54,567 2,416 9,123 714 634 $ 2,724 3,927 3,123 347 189 — 67,454 100 10,410 13,621 1,394 12,227 10,445 962 9,483
 7,466\ 383\ 37\ 2,485\ 10,371\ \$\ 90,052\ 2,744\ 286\ 428\ 447\ 3,905\ \$\ 1,562\ 2,007\ 17\ 292\ 1,321\ 2,291\ 7,490\ 2,150\ 674\ 15\ 741\ -273\ 3,853\ (continued) & Extracted from 10-K filings for Basin Water, Inc. Signals of Xerox's Fictitious Reporting Schemes The first two signals listed next apply to all methods of overstating revenue. The rest of the
industry ignored the proverbial iceberg and chanted their mantra, "Internet traffic is doubling every 100 days," as they swarmed across the nation and under the oceans, installing ten times more fiber-optic lines than was necessary at the time. Noonan began at his career at a pharmacy that was eventually acquired by Rite Aid, moving from stock boy
to pharmacist, to COO and eventually to interim CEO of Rite Aid. T 059402 01 ch8 p292-324 indd 311 F 9. When it became clear that the company could not reach the budget targets, "Sensormatic engaged in a variety of improper revenue recognition practices... Short-Answer Questions Required 33. (d) Hedonism. These capital vendors would then
bill back the amount of the contribution by burying the contribution amount in a subsequent inflated invoice to Buca. On October 14, 2009, TierOne filed a Form 8-K reporting an additional $13.9 million in loan loss provisions for the second quarter of 2009. 059402 01 ch6 p191-225.indd 217 7/7/14 9:06 AM 218 Chapter 6 • Abracadabra year.
after the Tables. This was the year that a court order instigated the breakup of AT&T and seven local phone companies to allow more competition in the long-distance telephone industry. Additionally during fiscal 2006 and the first two quarters of fiscal 2007, Beazer, again acting through certain of its officers and employees, improperly r
Identify the major stakeholders in this case. (c) It used death-spiral financing in which it guaranteed that if Enron's stock fell below certain specific amounts, it would issue more shares or pay cash to SPEs. (d) All of the above were signals. Drabinsky, Garth, 192, 193, 195, 198 DSO (days sales outstanding), 90, 121-122, 124 Dumbsizing, 75-76
Dunlap, Al carrot-and-stick approach of, 76-80 history of, 72-74 leadership of, 90 outcomes for, 95-96 Sunbeam and, 70-80, 83-89 Duty, 51 E Earnings expectations, 31, 128 overstated, 84-85, 94-95, 124-125, 158-162, 166, 169-170, 235 Ebbers, Bernard, 33, 36, 145-150, 154-157, 162-164, 166, 168, 174 059402 01 GLINDEX p383-401.indd 388
modest manipulations with Chewco. Explains how a particular accounting scheme or fraud leads to specific signals in the company's financial statements indicating that these financial statements have been manipulated. Buenos Aires water
utility and wastewater plants. A combination of all three of the following signals is particularly alarming. From then on, Skilling allegedly wanted Enron to focus on its trading business of actually piping gas. www.bop.gov. June 8, 1998b. 059402 01 ch9 p325-360.indd 347 7/7/14 9:11 AM 348 Chapter 9.
Mortgage Mayhem An Overview of Countrywide's Notes to Its Financial Statements Although the SEC's Complaint (June 4, 2009) alleged that Countrywide did not fully disclose all the risky attributes associated with its loans, note that Countrywide did not fully disclose all the risky attributes associated with its loans, note that Countrywide's filings in the years leading up to 2007 did disclose all the risky attributes associated with its loans, note that Countrywide's filings in the years leading up to 2007 did disclose all the risky attributes associated with its loans, note that Countrywide's filings in the years leading up to 2007 did disclose all the risky attributes associated with its loans, note that Countrywide's filings in the years leading up to 2007 did disclose all the risky attributes associated with its loans, note that Countrywide's filings in the years leading up to 2007 did disclose all the risky attributes associated with its loans, note that Countrywide's filings in the years leading up to 2007 did disclose all the risky attributes associated with its loans, note that Countrywide's filings in the years leading up to 2007 did disclose all the risky attributes associated with its loans, note that Countrywide's filings in the years leading up to 2007 did disclose all the risky attributes associated with the years leading up to 2007 did disclose all the risky attributes associated with the years leading up to 2007 did disclose all the risky attributes associated with the years leading up to 2007 did disclose all the risky attributes associated with the years leading up to 2007 did disclose all the risky attributes associated with the years leading up to 2007 did disclose all the risky attributes associated with the years leading up to 2007 did disclose all the risky attributes associated with the years leading up to 2007 did disclose and years leading up to 2007 did disclose all the years leading up to 2007 did disclose all the years leading up to 2007 did disclose all the years leading up to 200
borrowers on pay-option ARM loans held for investment. (a) Understating expenses via the release of cookie-jar reserves. There were not many seasoned executives who wanted his job. "CPAs Are Sexy: Accountants in Demand as Regulatory Climate Tightens," Boston Business Journal, January 14. Barta, Patrick. Selected Financial Statements 2004-
2007. Lattman, Peter. Turning from how regulators approach conflicts to how firms can assess and mitigate conflicts, I believe that an effective conflicts risk governance framework includes three broad considerations. By May 2000, all the adverse forces had combined and California's power nightmare began in earnest. The beauty for the
unscrupulous sponsoring company is that via equity accounting, the company's share of the SPE's earnings is accounted for in the company's income statement and the company's income statement and the company's share of the SPE's earnings is accounted for in the company's share of the SPE's earnings is accounted for in the company's income statement and the company's income statement and the company's share of the SPE's earnings is accounted for in the company's income statement and the company can still record profits on its transactions with the SPE.
found that in the audited financial statements as well as in the Disclosure Report distributed by AHERF to the public, properly adjusting the bad debt reserve of Delaware Valley would have "reduced its reported net income of $27 million before extraordinary item and change in accounting principle by approximately $40 million and similarly reduced
its reported net accounts receivable figure of $253 million by approximately $40 million." Furthermore, the MD&A section of the AHERF Disclosure Report "implied that the $72.2 million increase in Delaware Valley accounts receivable during fiscal year 1996 was a temporary phenomenon that would resolve itself." (Quotes from AAER 1283, 2000)
AHERF's Other Fabrications The SEC also found that AHERF inappropriately transferred $99.6 million of reserves from the various hospitals to Delaware Valley in 1997 to avoid recognizing the expense in its income statement when it had to write off accounts receivable and did not have a sufficient bad debt reserve. Signal #2: Increase in Accounts
Receivable as a Percentage of Sales The leading sign of an overstatement of sales is when accounts receivable increase as a percentage of sales, which is often measured as days sales outstanding (DSO). Such was the financial reporting environment at the turn of the 21st century as the management of so many companies, blinded by the lure of
stock option riches, recklessly pushed and pressurized everyone in the system to go along with the fabricated financial statements. Even his eightyear old son knew the right term for him now. 059402_01_ch7_p226-291.indd 244 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 245 the $750 per megawatt cap on purchases of
power from within California. Some firms go further, not only analyzing their weaknesses, but also issues identified at other firms so that the same problems do not happen at their establishment. The principal repayments during business
 203) After the Cuiába deal, Enron began a series of transactions using LJM1 (and later LJM2) to purportedly sell poorly performing assets or a share thereof to various SPEs, thereby recording profits or avoiding losses on the sales. The number of shares issued depends on the market value of the stock on the repayment date. By this time, UUNet had
over 4 million dial-up ports for users to log on to the Internet. Between approximately 2000 and 2007, Beazer, acting through certain of its quarterly and annual 1 The findings herein are made pursuant to Respondent's Offer of Settlement and are not binding on any other person or entity in
this or any other proceeding. Enron Broadband Services In 1997, when Enron acquired the Portland General utility business, an unintended consequence was that it also acquired FirstPoint, a small telecommunications Internet start-up company that was a tiny division of Portland General. ww.nbcnews.com. The
statement of cash flows is separated into three segments: the cash flows from operating activities, the cash flows from investing activities, and the cash flows from investing activities activities.
increases in discounts as a percentage of sales). CASE STUDY Beazer Homes USA, Inc. His first acquisition was The Phone Company in Jackson, Tennessee, where Waldron had once worked briefly to get experience in the telephone business. An Overview of Sunbeam's Fictitious Financial Reporting Schemes Sunbeam engaged in two major schemes
to make its financial statements appear much healthier than they recorded) and improper use of restructuring reserves. Examine Peregrine's
financial statements for the following yearends: March 31, 1999; March 31, 2000; and March 31, 2001. They were also aware of the considerable growth in the amount of these accounts receivable and attempted to solve the problem with changes in management. He was sentenced to one year plus one day in prison, with his sentence commencing in
October 2005. It then appears as though the "restructuring" worked and higher profits will recur, and the stock price often increases in response. Amazingly, no one seemed inclined to ask why in the world any financial institution would lend money to a newly formed trust with no track record. They presented him with a generous severance package
that included $1.5 million per year for life and use of the WorldCom jet for 30 hours per year. Specifically, the Buca vendors involved in the scheme would pay contributions to Buca to help fund the Paisano Partners Conferences. In addition, in June 2010, the SEC barred Shelton from ever serving as an officer or a director of a public company
(LR 21548, 2010). For criminal fraud cases, the burden of proof (or level of proof) required is generally higher than for civil fraud cases; "For civil cases that burden is a 'preponderance of evidence.' In criminal fraud the standard is 'beyond a reasonable doubt'" (Lawrence & Wells, 2004). Enron wanted to decrease its ownership of this problematic
investment. http:// journalofaccountancy.com. A highly unusual clause in the contract stated that the timber rights would "revert back to the owner of the underlying land at either the earlier of twenty years or if the percentage of Adelphia stock held by John Rigas fell below 50% of all the outstanding company stock" (BR-6413, 2002). Grubman
steadfastly refused to give the stock a "sell" rating. December 14, 2011. July 30, 2010. In this case, justice will be determined with reference to community values. (a) Act only according to that maxim by which you can at the same time will that it should become a universal law. would act as hubs. The Company accounted for the December 2007
transaction under the equity method. What is the amount of Rhodes Co.'s net income for year 1? Amato, Neil. Enron recognized no gains or losses in connection with these transactions with itself and moving assets to this structure. Initially, some
ardent supporters of the legislation regarded it as a type of magic potion, a cure-all for the problems plaguing the corporate world. Jeffrey Skilling—an ardent supporter of mark-to-market accounting—apparently supported Fastow's misguided thinking. interest remained too high as a percentage of income for the debt to be maintained and repaid
Nonetheless, neither Gadel nor Skrypek ensured disclosure of these related party transactions in Buca's financial statements or proxy statements or proxy statements for the years 2000 and 2001. The folksy part of his personality became more pronounced; he dressed and swaggered more and more like John Wayne. SSB also guaranteed Ebbers's loan to Citibank. My
fault. Applied ethics investigates how a normative system plays out in a practical situation and/or within a specific field. The following chart shows the interrelationship between Ebbers's IPO allocations and SSB's investment-banking work for WorldCom. T F T F 5. Xerox Corporation Litigation Release, April 11, 2002. Both law and morality require
that factors such as race, religion, gender, sexual orientation, or national origin should not affect the distribution of benefits or burdens to citizens. Wells. With this goal, the company that later became Countrywide Financial Corporation began in Calabasas, California, as Countrywide Credit Industries. This signal is, of course, based on the same logic
and dynamics as Signal #1, but it is a more pronounced signal and very easy to spot. xvii-xxv) There are many familiar themes in the above findings, as many of the characteristics found in the corporate failures at the turn of the 21st century were also features of the financial crisis of 2008, such as the following: • Failure of existing regulations and
supervisory bodies. (b) The SPE had to be controlled by someone independent of Enron to avoid consolidation. Investment banks and mortgage lenders began to invest in CDSs to hedge against claims against them in the event of default on the bonds they had sold or securitized. These investments did fairly well for Enron and CALPERS. Peregrine,
without admitting or denying the allegations of the Commission's complaint, has agreed (1) to be enjoined from violating the antifraud, reporting, books and records, and internal controls provisions of the federal securities laws, (2) to disclose the current condition of its internal controls and financial reporting procedure, when a reorganization plan
under Chapter 11 of the Bankruptcy Code becomes effective, (3) to comply, on an accelerated basis, with the rules regarding management's report on internal Auditor to ensure that Peregrine's financial results are accurately reported in Peregrine's public
financial statements, (5) to appoint a Corporate Compliance Officer to perform an ongoing review of Peregrine's corporate governance policies and employees, 059402 01 ch4 p117-143.indd 138 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 139 to prevent violations of
the federal securities laws. When a company solicits bill and hold orders from its customers and recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognition. After the merger of CUC with HFS, Inc., the newly established Cendant discovered the CUC fraud. July 14, 2008. Additionally, Gadelevery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, this represents improper timing of revenue recognizes the sales in its income before delivery of the goods, the goods are sales in the goods and the goods are sales in the goods.
and Skrypek signed Buca's management representation letters to Buca's independent auditors in connection with their annual audits of Buca's financial statements. After all, he dwelled in the elevated world of finance, not "in pipelines—expensive, dirty pipelines" (Eichenwald, 2005, p. Unusually long periods for depreciation of assets is a sign of
fictitious reporting in Livent's case. Although it was becoming obvious that Dunlap's cost-cutting turnarounds were not turning out to be such positive transformations after all, the business press generally ignored the short-lived nature of the profits that followed his ruthless downsizings. In early 2007, Mr. Forbes was finally sentenced to 12 years
and 7 months in federal prison. Describes the fraud or scheme in detail, referencing the company's financial statements as well as primary documents such as Accounting and Auditing Releases, Litigation Releases, Litigation Releases, Litigation Releases, Litigation Releases, SEC Complaints, and Bankruptcy Reports. • No new long-term contracts were allowed. • In March 2008, Xerox agreed to pay $670
million and KPMG LLP agreed to pay $80 million to settle a "lawsuit filed on behalf of Xerox investors who claimed Xerox committed accounting fraud to meet Wall Street earnings expectations" (Taub, 2008). The SEC's complaint alleged that the transaction was deceptive mainly for the following reasons: • The $423,375,076 in debt was not paid
down, but instead was shifted to Highland Video. December 2004. Signal #3: Sudden Change in Gross Margin Percentage—sales less the cost of goods sold expressed as a percentage of sales. (Schapiro, 2012) Some of the
important financial reporting consequences of Dodd-Frank are as follows8: • Smaller public companies will be exempt from Section 404(b) of the SOX Act of 2002. Gadel focused the bill-back scheme on vendors, such as construction and information technology vendors, that provided goods and services that, under more appropriate circumstances,
could be capitalized. In the 2000 Annual Report, the "Related-Party" that "acquired approximately $371 million of merchant assets and investments and other assets from Enron" in 2000. • Recognize the pervasiveness of accounting fraud. The loan accrued interest at a rate of 8% per annum with a terminately $371 million of merchant assets from Enron" in 2000.
of two years. Enron then went ahead in 1999 and "recognized after-tax income of $95 million from the Rhythms transaction" (Powers Report, 2002, p. As a result, Raptor I should have been consolidated into Enron's financial statements. In a decision about the size of the bonuses, the justice approach requires that all employees of the same category.
(or rank) must be equally eligible for the bonus and all employees achieving the same target of performance must receive the same size of bonus. What are the alternatives? Via a series of dizzyingly contrived and interlocking partnerships, LJM2 basically borrowed money—and used Enron's own stock—to purchase poorly performing assets from
Enron in order to inflate Enron's earnings, hide its debt, and provide cash to keep Enron going. Chapter 11, Case No. 08-13555. The owner of the interest at that price on the future date. "Predatory Lending: The Hidden Scourge of the Housing Market." Wyoming Lawyer. (This task force replaced
the Corporate Fraud Task Force that was created in 2002 in response to SOX.) Just as the response to the earlier crisis had been additional regulation in the form of SOX), the 2008 crisis resulted in more regulation in the form of SOX).
Under the guidance of EITF 01-142, which became effective in 2002, the Commissioner stated: Under this recent accounting guidance, Edison must report revenue on a gross basis to include those District-Paid Expenses for which it is the "primary obligor" for the expense. The power to direct the activities of a variable interest entity that most
significantly impact the entity's economic performance. In fact, he appeared to favor this kind of circular logic to rationalize his actions. www.bizjournals. Aerial, Inc., an airplane manufacturing company, incurred $1 million in development costs during the design and manufacture of a new airplane. Weinstein, Stephen. 059402 01 ch9 p325-360.indd
342 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 343 Exhibit 9.2 Extracts from Consolidated Balance Sheets Countrywide Financial Corporation 10-K 20066 December 31 2006 2005 (in thousands, except share data) ASSETS Cash Mortgage loans held for sale Trading securities owned, at fair value Trading securities pledged as collateral, at
fair value Securities purchased under agreements to resell, securities borrowed and federal funds sold Loans held for investment, net of allowance for loan losses of $261,054 and $189,201, respectively Investments in other financial instruments, at fair value Mortgage servicing rights, at fair value Mortgage servicing rights, net Premises and
equipment, net Other assets Total assets $ 1,407,000 31,272,630 20,036,668 1,465,517 $ 1,031,108 36,808,185 10,314,384 668,189 27,269,897 23,317,361 78,085,757 12,769,451 16,172,064 — 1,625,456 9,841,790 $199,946,230 69,865,447 11,260,725 — 12,610,839 1,279,659 7,929,473 $175,085,370 Exhibit 9.3 Extracts from Consolidated
Balance Sheets Countrywide Financial Corporation 10-K 2007 December 31 2007 2006 (in thousands, except share data) ASSETS Cash Mortgage loans held for sale Trading securities purchased under agreements to resell, securities borrowed and federal funds sold
Loans held for investment, net of allowance for loan losses of $2,399,491 and $326,817, respectively Investments in other financial instruments, at fair value Premises and equipment, net Other assets Total assets 6 7 $ 8,810,399 11,681,274 14,988,780 6,838,044 $ 1,407,000 31,272,630 20,036,668
 1,465,517 9,640,879 27,269,897 98,000,713 28,173,281 18,958,180 1,564,438 13,074,073 $ 211,730,061 78,019,994 12,769,451 16,172,064 1,625,456 9,907,553 $ 199,946,230 Obtained from U.S. Securities and Exchange Commission. (Hiltzik, 2012) The enormous profit that Enron made on wholesale electricity futures, as well as its lucrative
trading in natural gas, merely delayed its inevitable downfall from the huge losses it was incurring in the retail electricity business and on projects such as Dabhol, Cuiába, Azurix, and EBS. Then, on an invoice-by-invoice basis, they were allocated
large numbers of stock options that would make them multimillionaires if the Sunbeam stock price went up dramatically. On the other hand, the CFO thinks the greatest good for the greatest number will be best served if the money is sent to starving children in a poor country. During year 11, Greasy Patties Corporation decides that it would be
March 20, 1998. The Rights-and-Duties Approach to the Decision-Making Model Under this approach, when faced with an ethical decision, the decision maker would again attempt to identify all the facts and all of the stakeholders affected by a particular decision. Navistar International Corporation. (a) Consequentialism. 10 Obtained from U.S.
Securities and Exchange Commission. (b) Management fees. The trouble was that after Kimberly-Clark acquired Scott Paper, management found it to be a mess. Peter Madoff, S7 10 Cr. 228 (LTS) 3 Peter Madoff, S7 10 Cr. 228 (LTS) 3 Peter Madoff, S7 10 Cr. 228 (LTS) 3 Peter Madoff was ultimately sentenced on December 19, 2012, to ten years in prison. Financial Statements, 1998-2002. Over time, the term became
vague and generally referred to loans with a higher default risk. www.sonyclassics.com. • The wide range of end-of-chapter assignments provides students with ample opportunity to apply what they have learned. Sidgmore, John, 151 Sidgmore, John, 1
234, 235, 238, 239, 242, 246, 256, 274, 277, 278 7/7/14 9:17 AM Glindex 399 Slow shipping, 120 Requesting the shipping company to delay the shipping company
059402_01_ch2_p047-068.indd 54 7/7/14 8:59 AM Chapter 2 • Ethics at Work 55 • The auditor's family could suffer public humiliation if the auditor were criminally prosecuted. "I wanted to be a hero by solving the problem," he said. Presto! The cash problem was "solved," or at least it appeared to be. First, because the charge is described as a
regarding unconsolidated affiliates are vaque as to the reason for using the SPE, the name of the SPE, or the nature of the transactions with the SPE. (c) A and B. What is the incentive for managers to overstating the restructuring reserve decreases
net income in the current period? No rationale was given. Others at various levels and in various departments also participated in these practices" (AAER 1017, 1998). Dobby, Christine. Lockheed had an accounting policy in which it capitalized TriStar's development costs with the intention of writing them off as the planes were
 Although Lay was master of all the pipelines and gas wells that Enron possessed, he did not become master of its debt. However, Enron would get the cash up front. www.sec.gov Notes: 1) Reported Pre-tax Income for the
2nd quarter of FY 99 is before a pre-tax charge for store closings of $289.7 million 2) This table does not purport to show a complete listing of the adjustments recorded in Rite Aid's restatements. Causey "pleaded guilty to securities fraud and agreed to cooperate with prosecutors. SEC Press Release. brokerage house, to be on the lookout for
unsustainable profits at Sunbeam. Indicate which of these signals is present in Navistar's 10-K notes. www.masslive.com/business-news. Madoff also misrepresented that he, as CCO, ensured that reviews of the IA trading were being performed. Gadel and Skrypek authorized payment of these vague invoices and approved the capitalization of the
invoice payments. (b) Its gross margin will be understated. For example, there were risks such as interest rate payment default, principal repayment default, principal repayment. PowerPoint Presentations: Complete PowerPoint presentations: Complete PowerPoint presentations are provided for each chapter. Signal #3: Unusually Long Period for Depreciation of Assets If an accounting
policy note to the financial statements indicates that an asset is being depreciated or amortized over a longer periods than in the past or over longer periods. United States of America v. Now, if the child were to leave the
room during a game, you—who enjoy the game so much— would not be inclined to cheat and move a chess piece. Many internal operating decisions of the firm are made on the basis of accounting data that is used for the financial statements. 63. The size of the number is hard to believe; however, what follows is not a typographical error. If we have a
duty, there are no exceptions. latimes.com. The latest guidance for consolidation is the ASC 810 proposed update issued in 2011. When a company appears to be in a financially stressful situation, this situation can instigate a vicious cycle by making it difficult for a company to obtain future financing as well as driving up its interest rates. "Class
Action Lawsuit against Krispy Kreme Doughnuts Inc." www.chimicles.com. Beginning in fiscal year 1999, the Engine Division assumed responsibility for accounting for its warranty reserve, which reflected the Company's estimated future warranty reserved futur
AM Chapter 6 • Abracadabra 219 manufactured trucks. The total payments under these related party rental agreements were $57, $54 and $55 for the years ended December 31, 2007, 2006, and 2005, respectively. Explain why those signals could have been indications that Basin Water may have allegedly overstated its sales and understated its
loss. Consolidated Statements of Cash Flows (in thousands) Year Ended September 30 2007 Cash flows from operating activities: Depreciation and amortization Stock-based compensation expense Inventory impairments and option
contract abandonments Goodwill impairment charge Deferred income tax (benefit) provision Tax benefit from stock transactions Equity in loss (income) of unconsolidated joint ventures Cash distributions of income from unconsolidated joint ventures Cash dis
 income tax receivable Decrease (increase) in inventory Decrease (increase) in residential mortgage loans available-for-sale Decrease (increase) in crease in other changes Net cash provided by (used in) operating activities Cash flows from investing
Capital expenditures Investments in unconsolidated joint ventures Cash flows from financing activities: Repayment of term loan Borrowings under credit facilities and warehouse line Repayment of credit facilities. Repayment of term loan Borrowings under credit facilities and warehouse line Repayment of credit facilities.
facilities and warehouse line Repayment of other secured notes Borrowings under model home financing obligations Repayment of model home financing obligations Repayment of senior notes Borrowings under senior notes B
611,864 52,755 (161,605) (2,635) 35,154 5,285 42,425 15,753 44,175 -25,963 (8,205) (1,343) 352 36,068 11,945 5,511 130,235 (51,186) 11,551 (5,021) 5,844 292,532 (63,981) 134,953 91,376 (181,639) -(486,727) (92,157) (84,637) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,521) -(593,5
059402 01 ch3 p069-116.indd 111 7/7/14 9:01 AM 112 Chapter 3 • The Sizzling Saga of Sunbeam Year Ended September 30 2007 2006 2005 As Restated (2,259) 4,422 (348) — 2,635 (15,610) (170,556) 286,767 167,570 $ 454,337 Debt issuance costs Proceeds from stock option exercises Common stock redeemed Treasury stock purchases Tax
benefit from stock transactions Dividends paid Net cash (used in) provided by financing activities Increase (decrease) in cash equivalents at end of year (7,206) 7,298 (2,624) (205,416) 8,205 (16,144) 353,232 (129,528) 297,098 $ 167,570 (4,958) 5,875 — (8,092) —
(13,884) 107,833 (23,782) 320,880 $ 297,098 Extracts from form 10-K9 For the fiscal year ended September 30, 2006 Beazer Homes USA, Inc. "SEC Awards More Than $14 Million to Whistleblower." 2013. His wife, Kristie, filed for divorce in 2008. All rights reserved. "First and foremost, I'll tell you it was my fault. An owner independent of the
company must make a substantive equity investment of at least 3 percent of the SPE's assets, and that 3 percent must remain at risk throughout the transaction; and 2. However, it is important for users of financial statements to be aware of different reporting methods and to question why one method was chosen rather than another. AAER 1599
U.S. Securities and Exchange Commission Accounting and Auditing Enforcement Release, June 27, 2002. SEC enforcement actions frequently comment on how companies in violation of reporting standards consistently met their own earnings targets. Second, at Gadel's direction and with Skrypek's knowledge, Buca used an inflated invoice from EDP
to improperly capitalize at least $130,000 of ordinary expenses, including Buca's monthly telephone bill. Construction vendors that participated in the bill-back scheme typically billed for the contribution amount in vaguely worded change orders and invoices, or inflated project bids. www.time.com. "Enron Timeline." December 13, 2005. Ebbers and
his enchanted circle believed they had a vast capacity of a commodity that was in short supply, whereas they actually had a commodity that was in oversupply. • David McConnell, former CFO of AHERF, agreed to participate in an "accelerated rehabilitative disposition program" and was fined $25,000 by the SEC (Bowling, 2013). It should be tailored
to specific conflicts in the business model and clearly set forth the governance, risk management and compliance procedures to mitigate and manage these conflicts. Therefore, users of financial statements must be on high alert for unconsolidated affiliates that are described in vague terms. With each acquisition, the new company's revenue, assets,
and profits were included with those of the original LDDS. March 15, 2013. iii. • E. After two controllers produced the general ledger each quarter, they gave the information. Her decline from glory was aided by her nemesis, Jeffrey
Skilling, who led the charge to have her removed from her position as CEO of Enron International (as the development division of Enron had been renamed). A recent article in Accounting Today agrees that the SEC's emphasis will move from fraud on "Wall Street to Main Street" (Cohn, 2013). Of course, financial institutions did not lend these huge
sums of money to Enron without receiving guarantees, and eventually, when Enron was called on to repay the debts of the SPEs, the company was bankrupted. Scheme #1: Understatement of Expenses was Livent's erasure of
expense invoices. The invoices from this independent contractor contained no itemization of her time or work. To deal with this issue, SOX added provisions mandating independence of analysts from their investment banking employers. As a result, he had his first fateful meeting with Jack Grubman, the SSB stock analyst. • Recognize WorldCom's
improper capitalization of expenses. In an AAER or LR, the SEC describes how a company has allegedly infringed securities law. This dazzling scheme, which became known as "Ricochet," allowed traders to charge higher prices for out-of-state electricity (Eichenwald & Richtel, 2002). Sullivan backed down on the issue of the reserve, but did not
forget. Christie, Les. November 14, 2012. In April 2008, The Economist reported: Bankers gathering in Vienna this week for the annual bash of the International Swaps and Derivatives Association (ISDA) had some big numbers to celebrate. The bankers requested their affiliate, Citibank, not to sell any of Ebbers's stock that Citibank held as security
for its $40 million loan to him. According to the Powers Report (2002), Enron analysts had reviewed the financial viability of the structure would default and would not be able to meet its obligations on the Rhythms put "(p. These subprime
loans were often pooled and sold to the secondary market as whole loans or as mortgage-backed securities. William C. At Xerox, CFFO went from 26% of net income for 1996, to 33% for 1997. 8. August 3, 2005. (c) The net amount for accounts receivable decreases as a percentage of total current assets. First, EDP billed Buca for salary payments -
totaling $1,394,775 made to High Wire employees, even though many of these High Wire employees spent little or no time working for Buca. • The state created two new agencies that were subject to additional rules: 1. The SEC findings described the company's actions as follows: . . . at the end of each quarter, Livent simply removed certain expenses
and the related liabilities from the general ledger, literally erasing them from the company's books. in Mulligan, 2006). Clearly, in spite of increased regulations, accounting fraud remains a serious and persistent problem. 059402 01 REF p365-382 indd 382 "Who Is Fannie Mae Today?" 2012. This falsely boosts current revenues and earnings at the
expense of future periods. The SEC also found that Rite Aid allegedly failed to properly accrue an expense each quarter with respect to the stock appreciation rights (SARS) that the company granted to certain field managers. Federal Register Vol. 059402_01_ch8 p292-324.indd 295 7/7/14 9:10 AM 296 Chapter 8 • Tall Tales In July 2002, the SEC
alleged that the Adelphia case involved "one of the most extensive frauds ever to take place at a public company." The frauds centered on related-party transactions, which refer to dealings with any party that controls or can significantly influence the operations of a company so as to prevent the company from properly pursuing its own interests. Also
be wary of percentage of completion method where unbilled sales increase as a percentage of total sales. Beazer also restated its fiscal 2005 net income from $263 million to $776 million or 5%) and increase of $13 million or 5%) to
reflect the cumulative effect of adjustments for the fiscal years 1998 through 2004. (c) Conducting artificial transactions with special purpose entities. Morgan Stanley ...," 2005). 9 In the 2007 10-K, the comparative amount for the 2006 allowance for loan
losses on loans held for investment was stated as $0.327 billion. One has to consider how the company will be able to continue showing profits in the future when it can no longer release reserves to bolster profits. This is known as the hedonist's paradox, and it is an ongoing obstacle for those who try to obtain pleasure or argue for it as a moral goal.
Lockheed: Sky High6 Lockheed is presented mainly as an example of failing to record impairments of assets. 4). (This provision could prevent the situation that arose at Enron, where Arthur Andersen's technical oversight partner, Carl Bass, objected to some of Enron's accounting treatments and was removed from involvement with the audit at
Enron's request.) • Audit Committees: Audit committees consisting of a minimum of three independent directors are required. Lockheed's problems with the TriStar originally began with its choice of the British Rolls-Royce RB-211 engine for its new plane. The firm itself could be sued for monetary damages. At their core, the federal securities laws
were intended by Congress to be an exercise in applied ethics. The talk was part of the Choices & Challenges series on business and Society. . Multiple Element Contracts when used for the purpose of improper timing of revenue recognition XEROX 4. She was sentenced to five months
in prison and five months home detention ("Ex-WorldCom Executive Sentenced ...," 2005). "Don't do it." Assignments True/False Questions with T for true or F for false for more practice with key terms and concepts from this chapter. "Morgan Stanley Told to Pay $850 Million." May 18, 2005. Countrywide's
Underestimation of Allowance for Loan Losses Although the SEC alleges that many of the risk factors were not properly disclosed, in Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Countrywide's filings, the SEC Complaint (June 4, 2009) did not specifically address Country (June 4, 2009) did not specifically addr
AM Chapter 9 • Mortgage Mayhem 339 for investment on its balance sheets in the years leading up to the enormous loan losses in 2007. Noonan, former COO and interim CEO, left Rite Aid before the fraud was discovered. December 9, 2002. Clough, Alexandra. May 15, 2001. Consolidated Balance Sheets (in thousands, except per share amounts)
September 30 2005 ASSETS Cash and cash equivalents Accounts receivable Inventory Owned inventory Consolidated inventory owned 
EQUITY Trade accounts payable Other liabilities Obligations related to consolidated inventory not owned Term Loan Senior Notes (net of discounts of $4,118 and $1,095, respectively) Other notes payable Total Liabilities $297,098 161,880 2004 $320,880 70,574 2,671,082 230,083 2,901,165 78,571 101,329 28,367 121,368 80,738 $3,770,516
2,089,330\ 254,765\ 2,344,095\ 44,748\ 47,052\ 24,671\ 251,603\ 59,407\ \$\ 3,163,030\ \$\ 141,623\ 636,106\ 166,163\ -1,275,882\ 46,054\ 2,265,828\ 123,287\ 437,608\ 219,042\ 200,000\ 928,905\ 22,067\ 1,930,909\ (continued)\ 10\ Extracted from 10-K filings for Beazer Homes, USA, Inc.. 059402\ 01\ ch5\ p144-190.indd 186\ 7/7/14\ 9:04\ AM\ 187\ Chapter 5
WorldCom Wizardry: From WorldCom to WorldC
2,500,000,000 shares authorized; 1,995,699,758 and 1,935,464,840 shares outstanding, net of 22,522,250 and 17,026,256 shares owned by subsidiaries at September 30, 2002 and 2001, respectively Capital in excess: Share premium 8,146.9 7,962.8 15,042.7 12,305.7 Accumulated other comprehensive loss
(1.592.2) Contributed surplus, net of deferred compensation of $51.2 at September 30, 2002 and $85.3 at September 30, 2001 TOTAL SHAREHOLDERS' EOUITY (1.479.5) 24,790.6 31,737.4 $66.414.4 $71.022.6 Tyco International Consolidated Statements of Cash Flows 2000-2002 (in millions,
except share data) YEARS ENDED SEPTEMBER 30, 2002 2001 2000 CASH FLOWS FROM OPERATING ACTIVITIES: (Loss) income from continuing operations to net cash provided by operations adjustments to reconcile net (loss) income from continuing operations and other unusual charges (credits), net Write-off of
purchased in-process research and development Charges for the impairment of long-lived assets Goodwill impairment Minority interest in net income of consolidated subsidiary Depreciation Goodwill and intangible assets amortization
Deferred income taxes Provision for losses on accounts receivable and inventory Debt and refinancing cost amortization Charges related to prior years (see Note 1 $ (3,070.4) $ 4,401.5 $ 4,519.9 851.5 145.2 (84.2) 17.8 3,489.5 1,343.7 1.4 (7.2) 270.8 39.6 1,465.5 567.4 (535.6) 493.9 194.0 222.0 184.3 120.1 — 47.5 (410.4) 133.8 (64.1) 1,243.1 897.5
219.0 593.5 108.4 — 99.0 — 18.7 — (1,760.0) 1,095.0 549.4 507.8 354.3 6.8 — (continued) 059402_01_ch5_p144-190.indd 187 7/7/14 9:04 AM 188 Chapter 5 • WorldCom Wizardry: From WorldCom Wizardry: From
acquisitions and divestitures: Accounts receivable (Decrease in) proceeds under sale of accounts receivable program Contracts in progress Inventories Other current liabilities Income taxes Deferred revenue Other Net cash provided by operating activities from continuing operations Net
cash provided by (used in) operating activities from discontinued operations Net cash provided by operating activities CASH FLOWS FROM INVESTING ACTIVITIES: Purchase of property, plant and equipment, net Construction in progress—Tyco Global Network Acquisition of businesses, net of cash acquired Cash paid for purchase accounting and
holdback/earn-out liabilities Net proceeds from the sale of CIT Disposal of other businesses, net of cash balance acquired Net cash provided by investing activities from discontinued operations Net cash provided by (used
in) investing activities CASH FLOWS FROM FINANCING ACTIVITIES: Net proceeds from sale of common shares by subsidiary Dividends paid Repurchase of Tyco common shares (26.0) 81.8 60.0 1,014.5 (56.4) (434.1) 490.6 (992.4) 100.0 (336.5) (47.2)
(51.9) \ (833.7) \ 272.2 \ 335.1 \ (35.5) \ 117.0 \ 5,695.5 \ (192.5) \ (678.8) \ 313.7 \ (249.1) \ (606.1) \ 370.7 \ 304.1 \ (94.2) \ 6,925.5 \ 28.9 \ (850.0) \ 100.2 \ 443.9 \ 53.1 \ 896.4 \ (0.2) \ 128.4 \ 5,275.0 \ (1,708.7) \ (10,956.6) \ (894.4) \ (1,703.8) \ (111.1) \ (4,246.5) \ (544.2) \ 4,395.4 \ 138.7 \ (16.8) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \ (196.2) \
(83.2)\ (2,325.7)\ -904.4\ (142.8)\ -(177.2)\ (15,311.8)\ -74.4\ (353.4)\ -(52.9)\ (6,937.5)\ -2,684.3\ 2,156.4\ 1,516.8\ --358.6\ (11,638.6)\ (6,937.5)\ 1,951.3\ --185.7\ -(100.3)\ (789.2)\ 8,535.6\ 2,196.6\ 545.0\ -(90.0)\ (1,326.1)\ 680.4\ --355.3\ 2,130.7\ (86.2)\ (1,885.1)\ (continued)\ 059402\ 01\ ch5\ p144-190.indd\ 188\ 7/7/14\ 9:04\ AM\ 189\ Chapter\ 5
WorldCom Wizardry: From WorldCom to WorldC
in) provided by financing activities NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS TYCO CAPITAL'S CASH AND CASH EQUIVALENTS AT ERIOD SUPPLEMENTARY
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Consolidated Balance Sheet 20007 (in millions, except share data) SEPTEMBER 30 2000 CURRENT ASSETS: Cash and cash equivalents Receivables, less allowance for doubtful accounts of $442.1 in 2000 and $329.8 in 1999 Contracts in process Inventories Deferred income taxes Prepaid expenses and other current assets Total current assets
CONSTRUCTION IN PROGRESS—TYCOM GLOBAL NETWORK PROPERTY, PLANT AND EQUIPMENT, NET GOODWILL AND OTHER INTANGIBLE ASSETS TOTAL ASSETS TOTAL ASSETS CURRENT LIABILITIES: Loans payable and current maturities of long-term debt Accounts
payable $ 1,264.8 5,630.4 357.3 3,845.1 683.3 1,034.8 12,815.7 111.1 8,218.4 16,332.6 1,653.7 532.5 740.3 $40,404.3 $ 1,537.2 3,291.9 (continued) 7 Extracted from 10-K filings for Tyco International LTD. In its complaint, the SEC maintained: • From mid-1999 to the end of 2001, Adelphia excluded "billions of dollars in liabilities from its
consolidated financial statements by hiding them in off-balance sheet affiliates." • During this time, the company "falsified operations statistics and inflated Adelphia's earnings to meet Wall Street's expectations." • During this time, the company "concealed rampant self-dealing by the family that founded and controlled Adelphia, the Rigas
family." (Quotes from BR-6413, 2002) The Rigas family allegedly used company funds to purchase costly condominiums, plush holiday accommodation, and luxury cars and even to build a golf course. Skrypek ("Skrypek"), Buca's former Controller, helped preside over a corporate culture at Buca that allowed fraud to flourish. 059402_01_ch7_p226-
291.indd 229 7/7/14 9:08 AM 230 Chapter 7 • Enron and the Tale of the Golden Goose Enron had yet another crisis early on. From the outset, her company was saddled with debt when Enron financed it via the off-balance-sheet entity known as Marlin. Established in 1952 in Coudersport, Pennsylvania, Adelphia grew into one of the largest cable
television providers in the United States, operating in 29 states and Puerto Rico. Identifies the accounting fraud or method of fictitious financial reporting utilized by a specific, real-world company. T F 10. According to the SEC's ensuing investigation, "Fastow secretly controlled Chewco and Kopper, and by virtue of that control, received a share of
Chewco's profits as kickbacks from Kopper" (LR 17762, 2002). While Fastow liked to obscure the structure of his SPEs, he liked to complicate their transactions even more. Bryce (2002) explained how the analysts went wild and Enron's stock jumped. Krispy Kreme's stock price "climbed most dramatically of all, from the IPO price of $5.25 per share
to a high of $49.37 per share on August 18, 2003" ("Summary of Independent Investigation," 2005, p. For fiscal 1996, Livent reported pretax earnings of $14.2 million. Describe the concept of egoism. Most of the FBI involves financial reporting fraud: The majority of
corporate fraud cases pursued by the FBI involve accounting schemes designed to deceive investors, and analysts about the true 2 Foreign Corrupt Practices Act. • Users of financial statements, such as stockholders, potential investors, and people making loans or extending credit to the company, have the right to truthful financial
statements. As part of these journal entries, the land inventory account was reduced and a cost of sales expense account increased to reflect the value of the land and improvements that Beazer sold with the house. The SEC's enforcement action against Livent alleged that senior company officials had a special computer program designed that would
                                                             the accounting system without leaving a paper or transaction trail. The Bankruptcy Examiner, Thornburgh, summed up the major accounting hoaxes that Sullivan directed to falsify the financial statements: It appears that once income could no longer be sufficiently enhanced by the release of reserves, Mr.
Sullivan and certain other WorldCom personnel directed a series of adjustments to its line costs in successive reporting periods beginning with the first quarter of 2001. 059402_01_ch3_p069-116.indd 103 7/7/14 9:01 AM 104 Chapter 3 • The Sizzling Saga of Sunbeam net income by intentionally managing its earnings. Sunbeam's vicious cost-
cutting plan of closing production plants and cutting products, jobs, and R&D expenditure was not likely to lead to fast sales growth as reported in record numbers in 1997. These pooling points would use sophisticated equipment [and] ... The 1968 Charter Act gave Fannie Mae the authority to do exactly that ("Fannie Mae Early History, 2004").
Nonperforming assets, 358-359, 360 Noonan, Timothy J., 204, 209-212 Normand, Troy, 166 Normative ethics, 48, 49-53 A branch of ethics that offers guidelines or norms on how to distinguish between right actions and wrong actions. According to Mulford and Comiskey (2002), a good example of possible aggressive accounting with regard to
capitalization policies is American Software, which capitalized the majority of its software costs in 1997, wrote down a large amount of capitalized again in 2000. Signal #1: Increase in Accounts Receivable as a Percentage of Sales The leading sign of an overstatement of
sales is when accounts receivable increase as a percentage of sales, which is often measured as days sales outstanding (DSO). (c) Excluded the regulation of derivative financial instruments by the Commodities Futures Trading Commission. Last year, Jade had 1,000 employees on its payroll and the bookkeeper's salary (which was paid by Jade) was
$40,000. However, things started to turn sour as Krispy Kreme was accused of having "sweetened results" in its attempts to keep Wall Street happy (Maremont & Brooks, 2005). • Lockheed: Sky High • Key Terms • Ethics at Work • Assignments • Case Study: Navistar International Corporation 191 059402 01 ch6 p191-225.indd 191 7/7/14 9:05 AM
192 Chapter 6 • Abracadabra Livent: Phantom of the Finances Livent is presented mainly as an example of improper expense recognition via f ailure to record expenses. What balance sheet item did AHERF misstate, and what effect did this have on its reported income? Levitt (2002) described some of the
responsibilities of a board of directors: One of its responsibilities is to advise the CEO and the top executive team with impartial common sense and various kinds of expertise. Look at extracts from Sunbeam's quarterly income statements in Table 3.1. Calculating gross margin as a percentage of sales, as shown in Table 3.4, reveals sudden changes in
the gross margin over the quarters, from 19 percent in the second quarter of 1996 to negative 15 percent in the fourth quarter of 1996. Therefore, this approach requires the decision maker to fulfill his or her obligation to recognize and respect the rights of others. On a napkin, the waitress wrote the letters LDDC, for "Long Distance Discount
Company." The group at the meeting made one small change to "Long Distance Discount Services." At this point, LDDS, the company that was destined to evolve—with over 70 acquisitions—into the infamous WorldCom, was born. However, because the remaining members of the board of directors "ratified compensation committee actions with
virtually no data and without inquiring about or questioning the low interest rates," the Examiner believed that claims could be pursued against all of WorldCom's former directors (Third and Final Report, 2004, p. First Interim Report of Dick Thornburgh, Bankruptcy Court Examiner. The Court has jurisdiction over this action pursuant to Section
22(a) of the Securities Act [15 U.S.C. § 77v(a)] and Sections 21(d) and 27 of the Exchange Act [15 U.S.C. §§ 78u(e), 78aa]. Indeed, SSB is jointly and severally liable along with the original CUC as far back as 1985 and was allegedly directed by CUC's chairman and CEO,
Walter Forbes, from the very beginning. 7/7/14 9:06 AM Chapter 6 • Abracadabra b. For example, at the urging of Tyco officials, Thorn-EMI, whose fire protection operations Tyco acquired, made adjustments that reduced its assets and increased its liabilities by $76.5 million, resulting in Tyco's operating income in future financial periods being
overstated by approximately $29 million. In the late 1990s, the California Public Utilities Commission (CPUC) was in charge of revamping the rules for what was then referred to as California's electricity deregulation. Signal #5: Substantial Growth of Debt When the portion of a company's finance that is provided by lenders or outsiders (as opposed
to being provided by owners) increases significantly, it is an indication that the company may be taking on too much debt. The recording of early shipments of equipment remained unused until later periods. How should the decision be implemented? Vague descriptions were given of the Whitewing structure
without a clear rationale for its existence in the first place. Gas producers, industrial gas users, and utilities would be able to estimate future prices and cash flows more reliably. In September 2008, Freddie Mac was placed under a conservatorship to be overseen by the Federal Housing Finance Agency. According to the SEC, memoranda were
prepared close to the end of each quarter, specifying sales goals that needed to be met before the close of the quarter, in order to comply with the aggressive sales budgets that had been published and distributed to senior management and to the various departments. 7/7/14 8:58 AM Chapter 2 Ethics at Work Learning Objectives After studying this end of the comply with the aggressive sales budgets that had been published and distributed to senior management and to the various departments.
 chapter, you should be able to: • Identify and describe the three major normative ethical theories or schools of thought: consequentialism, deontology, and virtue ethics. Act according to a maxim which harmonizes with a possible realm (i.e., a systematic union of different rational beings through common laws).... (qtd. Winston-Salem Journal.
www.cbsnews.com. Which of the following is not true regarding the SECs allegations against Adelphia? The combination of these signals indicated that the off-balance-sheet activity was sufficiently significant as to render the published balance sheet wholly inadequate for analysis of the company. The allowance for loan losses was not increasing
nearly as much as the highrisk pay-option section of the total loans held for investment was growing. Instead of returning the payments to the insurance companies, Rite Aid reversed the accounts payable into profit "without sufficient justification or basis in violation of GAAP. August 29, 2002. There was a great deal of double billing as well as billin
of customers for work that was not done. The second factor is that the organization's "governing authority" - typically a board of directors and senior management - is knowledgeable about the compliance and effectiveness. (a)
Receivables increased as a percentage of sales. Bolt Company is a clothing manufacturer. In fact, Sunbeam's stock price actually dropped 50 cents on the Causes of the Financial and Economic Crisis in the United States. Whatever the
reason, Wall Street did not respond to this ruthless announcement. However, to the company's surprise, it becomes clear in October 2012 that Cat Trap will run for only one year and close on December 31, 2012. • David Sambol (formerly president of Countrywide) also settled SEC charges in 2010
(Dobuzinskis & Levine, 2010). Further, Foot pointed out that what is virtue in one context may not be virtue in another context. Based on these illusory reports of earnings and sales growth, as well as unrealistic estimates of future performance, the stock price broke out of the high $20 range in March 1997 and began a steady, steep rocketlike climb
until it peaked at about $52 in March 1998. (b) Allowed institutional investors such as pension funds and insurance companies to invest in non-GSE guaranteed mortgage-backed securities on the condition that they received appropriate ratings from the ratings agencies.
never reach Edison, but are expended by districts directly and then deducted from the district's remittances to Edison. Employees had already started to mock WorldCom. 059402_01_ch3_p069-116.indd 79 7/7/14 9:01 AM 80 Chapter 3 • The Sizzling Saga of Sunbeam Many believe that Sunbeam never recovered from the blow of losing White. a
percentage of sales. In addition to the SEC's efforts to fulfill the requirements of the SOX Act, a number of other organizations set to work to clean up the corporate environment and create greater financial statement transparency. For example: • The Financial Accounting Standards Board (FASB) issued or updated several accounting standards.
AAER 3165. 24. Crafty Company manufactures and sells printers. LR 18543. Gless, Peregrine's former chief financial officer (Litigation Release No. 18093). Some schools of their benefits to oneself
only (egoism). Lockheed, therefore, had to carry a share of the climbing Rolls-Royce costs while its own development costs were growing well over budget. Overstating acquired liabilities allowed Tyco to maintain on its books and records inflated reserves, which Tyco used in future periods to improve its earnings. Is the intermingling of a company's
assets with those of a major shareholder, director, or company officer illegal? Explain why the signal identified in the previous question (b.1) should alert the reader to the possibility of aggressive recognition of reported income. Jackson: Thomson/Cengage, 2006. Lay soon began fretting that HNG did not have a large enough network of pipelines.
There was such confusion between the various merged companies that inefficiency set in and disorganization spilled over to every level. Furthermore, the SEC found that Livent's management was involved in a "kickback scheme designed to misappropriate funds for their own use" (AAER 1095, 1999). 34. • We conclude a combination of excessive
borrowing, risky investments, and lack of transparency put the financial system on a collision course with crisis. Skilling, therefore, planned to build "two dozen pooling points across the globe. Wachovia and WaMu's banking operations would be sold off. Further, the quality of its products was very high and its profit margins were much higher than
Sunbeam's margins on its blenders or blankets. According to the Grand Jury Indictment: SULLIVAN, David F. 059402_01_ch2_p047-068.indd 55 7/7/14 8:59 AM 56 Chapter 2 • Ethics at Work It is important to remember that ethical dilemmas frequently involve the ossibility of actions that violate or fail to recognize the rights of others. 70. (b)
Meeting Wall Street analysts' earnings expectations. One particularly imaginative type of derivative that Enron began trading was its "weather information for its gas trading. By the end of that summer, Bernard Ebbers joined Foster and his new wife on their
honeymoon road trip back to Mississippi College. Did Fastow know that an SPE had to be consolidated with the parent company? After the October announcements of the required restatements, Sunbeam was trading in the $7 range, a spectacular plunge from its peak of about $52 per share a
mere eight months earlier (AAER 1393, 2001). • Auditors of non-public broker-dealers will be subject to oversight by the PCAOB. Rigas and his son Timothy Rigas, prosecutors alleged that the Rigas family: (a) Siphoned $100 million from Adelphia. The magnitude of that loss of focus cannot be underestimated. I'd like to think that I would have acted
differently or escaped some of the traps Tim will talk about—I would like to think that, but I'm far from sure that would be true." Noonan outlined his purpose by saying, "I'm here today to spend a little bit of time with you to talk about the crisis at Rite Aid. Finally, MacIntyre described Benjamin Franklin's utilitarian and functional view of virtue,
where hard work and early rising are seen as virtues. As a result of the conduct described above, Beazer violated Section 17(a) of the Securities Act, which prohibits materially false or misleading statements, or material omissions in the offer or sale of any security. (d) The net income reported by Edison in its income statement was incorrect. August 1
2000. • 28,000 cable subscribers of an unconsolidated Venezuelan affiliate. By this time, he was married to Linda Pigott, and they had three children: Treasure, Joy, and Faith. If the notes to the financial statements indicate that a company is capitalizing costs that other companies in the same industry recognize as expenses, it is a signal that the
company is capitalizing questionable costs. Michael Greenberger, the former director of the CFTC, alleged that he once entered Born's office as she was putting down the phone after speaking to former Assistant Treasury Secretary Larry Summers. (b) Side agreements with customers that were not recorded. However, they may have really believed
this myth and may have had no deliberate intention to deceive. Eva decides she has a duty to tell the truth at all times. It was during this first quarter of 1997 that Sunbeam began producing financial reports that made it look as though the slashing of facilities, products, jobs, and research and development could, in fact, grow sales and earnings. As a
public company, Buca is required to file certain documents with the Commission, including annual reports on Forms 10-K, quarterly reports on Forms 10-K, quarterly reports on Forms 10-V, and proxy statements. The company is still in existence but is no longer a public company.
itself can result in an action. The ratio is distorted by an even greater amount if ending inventory is overstated. in Cohen, 2004, p. (c) Could give the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment on the default of a specified loan even if the holder of the instrument the right to payment of the holder of the instrument the right to payment of the holder of th
that occurred close to Bolt's December 31 fiscal year-end date. Certainly, basic human rights must be equally accorded to all people. It is one thing to have a market value for a futures contract to sell an asset in 059402_01_ch7_p226-291.indd 232 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 233 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the Tale of the Golden Goose 230 the not-too-distant future and the G
to recognize or record the increase in value of that contract. The Powers Report (2002) presented a diagrammatic representation of the complicated set of interlocking structures that were 059402 01 ch7 p226-291.indd 260 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 261 $41 MM Premium on Put Enron Share Settled Put
100% Ownership Derivative Transactions Harrier • LLC Interest • Promissory Note $400 MM $30 MM Talon (SPE) • Enron Stock and Stock Contracts • Promissory Note $50 MM • $1,000 Cash LJM2 LLC Interest Fair Market Value Put of LLC Interest Fair Market Value Put of
cooperated with prosecutors and was sentenced to six years in prison (Partington, 2012). Yates claimed that he did not know anything about them. According to the SEC: Livent transferred costs from one show currently running to another show that had not yet opened or that had a longer amortization period. Respondent 2. The Sunbeam Inferno On
 July 19, 1996, the day that Al Dunlap was appointed CEO of Sunbeam, the stock price jumped 56 percent, from $12.50 to $18.63. Approaching ethics from a utilitarian framework, discuss whether or not the management of Sunbeam was unethical in issuing financial statements that improperly timed Sunbeam's revenue recognition.
059402_01_ch1_p025-046.indd 30 7/7/14 8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud 31 What gatekeeping checks and balances were in place in the financial reporting environment at that time? The TriStar program lost over $900 million up to 1981, when Lockheed finally wrote off the remaining amount of this impaired
asset in one lump sum of $400 million (Mondout, "Lockheed L-1011"). How was WorldCom able to continue to acquire so many companies and overstate goodwill by so much? Thus, Lehman's Repo 105 practice consisted of a two-step process: (1) undertaking Repo 105 transactions followed by (2) the use of Repo 105 cash borrowings to pay down
liabilities, thereby reducing leverage. 059402 01 ch7 p226-291.indd 242 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 243 All four of these ideas failed—some sooner, others later. April 20, 2010. Revenue recognition refers to the process of recording a transaction in the financial statements, indicating that the conditions
have been met for the earning of revenue. LR 18277. Describe how SPE LJM1 was used to assist Enron to fictitiously recognize income on its investment in Rhythms NetConnections (RHYTHMS). The Table was originally adapted from SEC's Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002 and published in Business Fairy Tales by
Cecil W. The contracts were first "sold" to a joint venture called Thunderbird—which, in turn, was owned by the Enron entity called Whitewing. In various quarters between 2000 and 2005, Beazer over-reserved house cost to complete expenses in order to defer profit to future periods. We purchased $92,000 in bakery
products in 2000. Also, because the later return of the goods due to obsolescence was concealed from the finance department, a replacement order was recorded as a new sale. Further, while sales with rights of return were growing, at year end 1997, Sunbeam actually reduced its reserve for returns from $6.5 million to $2.5 million. The ratio is
calculated as follows: Inventory turnover ratio = COGS \div Average inventory 059402 01 ch6 p191-225.indd 201 7/7/14 9:05 AM 059402 01 ch6 p191-225.indd 202 38 Overstatement Percentage 16% 9% 71% 88.3 63.0 5533% 2.4 132.8 *Obtained from AAER 1579, 2002. In essence, under FIN 46(R), if a sponsoring company has an investment in an
entity that is not self-supportive and there is a possibility that the investor may need to provide further financial support, the investee must be defined as a variable interest entity (VIE). (Ebbers eventually signed a note in September 2001 agreeing to repay the amounts extended under the guarantees.) The Global Crossing bankruptcy filing in January
2001 hit WorldCom's stock hard, putting another nail in Ebbers's coffin. The entire venture was now in jeopardy, and for the program to continue, it took the combined efforts of the British government taking over Rolls-Royce and the U.S. government providing a federal guarantee for Lockheed to receive a $250 million line of credit. Generally
Accepted Accounting Principles, or "GAAP," provides that a loan becomes "impaired" when it is probable that the bank will be unable to collect all amounts due under the original loan agreement. (b) Initially properly debiting the line-cost expense to an expense account and later transferring the expense to PPE. 5. Compare values and alternatives
While most of Enron's wholesale traders expected that the cost of electric power would increase. Calculate the times-interest-earned ratio for years 1-3. www.economist.com. Gadel and Skrypek directed Buca employees at quarter end to review repair and maintenance account invoices over $1,000 to find invoices that could be capitalized in a
sufficient quantity to meet an earnings target. At WorldCom, these signals indicated that the line-cost expense was being misallocated as the asset PPE. As shown in Table 9.3, the percent in 2004 to 0.22 percent in 2005. Explain the alleged related-party transactions
between Buca and High Wire Networks, Inc., as 059402_01_ch8_p292-324.indd 314 described in paragraphs 21-23 of the SEC Complaint filed in 2006. Essentially, all these reasons boil down to one basic and obvious motivating force—greed. This is a financial fraud, reporting, and internal controls case against Navistar, a Fortune 200 manufacturer
of commercial trucks and engines, and certain current and former employees. The board of InterNorth/HNG had decided to change the name of the Recent Settlements Involving Allegheny Health, Education and Research Foundation." Speech before the AICPA National
Healthcare Industry Conference, Washington, D.C. Willatt, Norris. According to the SEC, Adelphia purchased land from members of the Rigas family in terms of a contract in which a clause stated that the rights to the land would revert back to the owner after 20 years. (b) Change in the estimates of discount rates. Since then, Buca's stock has been
traded on NASDAQ. • In 2011, Krispy Kreme Doughnuts Inc. He realizes profits for the first time since 2004 ("Krispy Kreme Doughnuts Inc. He realizes profits of $390,172. The issue was whether Edison could report the gross amount of the fee per student as its revenues in its income statement and then separately deduct the district-paid expenses or whether it had to
report the net payment from the district (i.e., fees minus expenses) as revenues. Item I: Merchandise costing $5,000 was shipped to a retail customer on December 27. According to the SEC, most of these loans were held for investment as opposed to being sold into the secondary market. 219). West, Lawrence A., William A. The first Azurix project
involved Wessex Water, a successful water utility company in England. Adelphia's Fictitious Financial Reporting Schemes involving a Golf Course, Personal Margin Loans, and the Use of Luxury Condominiums The SEC claimed that
Adelphia used approximately $12.8 million of its funds to construct a golf course on land owned mainly by the Rigas, son of John Rigas, was not criminally charged. Instead, these findings reflect misconduct that resulted in large part from a deficient system of internal controls,
evidenced in part by insufficient numbers of employees with accounting training, a lack of written accounting policies and procedures, and flaws in the Company's organizational structure. McDonald, Lawrence G., with Patrick Robinson. 059402 01 ch4 p117-143.indd 125 7/7/14 9:02 AM 126 Chapter 4 • Hocus Pocus CUC: PHONY FUNDS6 CUC is
 Chapter 4 AAER 1017. • The signals of the alleged frauds that were scattered throughout Enron's financial statements, while the business community did not bother 3 • The Sizzling Saga of Sunbeam 71 He regarded the company he ran as his own
U.S. Securities and Exchange Commission Accounting and Auditing Enforcement Release, November 26, 2002. This revenue is earned by making the physical asset (the copy machine itself) available to the customer, and it is legitimately recognized at the beginning of the lease in sales-type leases. It manipulated cost of goods sold through a number
of mechanisms. Ward are in charge of the prosecution. (Krim, 2002) Ignoring all of the turmoil, Ebbers turned his attention to insignificant and petty issues. www.chron.com. (b) Brace must write off the $4 million by writing off $1 million in each quarter's financial statements in the year that it discovered that the asset was impaired by $4 million. In
fact, about a year after the new regulations came into effect, Timothy Belden, former head of Enron's Western energy trading desk, did an experiment to test weaknesses in California's power system. This was done in order to recognize future service revenue at the beginning of the lease. On June 24, WorldCom stock fell to below $1 on the stock
 amounts of borrowed cash, which it often lost on ill-advised projects while continuing to report earnings up front. An Overview of Krispy Kreme's records by its independent investigation, set up by two of its directors, revealed a number of accounting errors, including the
following: 1. 059402 01 ch4 p117-143.indd 128 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 129 Are They Living Happily Ever After? Again, Enron's knowledge of gas and electricity trading provided the basics it needed for success in coal trading. March 11. Signal #6: Writing Off Previously Capitalized Costs If in the past the company had a special
amount back to accounts receivable and recalculate accounts receivable as a percentage of sales that you calculated in Case Study question a2 above. There is a moral imperative to be honest no matter what the situation. Grubman was never charged with any criminal misconduct relating to WorldCom. 27. Peregrine agreed to a partial settlement
without admitting or denying the findings. (b) The Laura Nash Model. 18). (c) Metal futures. Large increases in investment of debt via contrived transactions with special purpose entities. Micatrotto also participated in
and profits for the first quarter of 2000, the bitter truth was that the company was already in dire trouble. Bankruptcy Report #3: Third Interim Report of Neal Batson, Court-Appointed Examiner. NYSE. A former Enron trader remarked, "No one ever talked to me about cash. (AAER 1095, 1999) Signals of Understatement of Expenses Here is an
examination of some of the signals indicating that a company may have engaged in improper expenses as a Percentage of Sales As with Scheme #1 (omitting expenses), if a category of
expense decreases as a percentage of sales compared to the industry or compared to previous periods, it is an alert that part of the expense may be deferred to future periods. Refer to The Top Twenty Methods of Fictitious Financial Reporting in Table 1.1 (p. In connection with this transaction, Fastow and others told Enron that NatWest wanted $20 in the expense may be deferred to future periods.
million for its interest in the partnership assets, but paid NatWest only $1 million of that sum and pocketed the rest. What is in dispute, however, is whether or not the senior managers of EBS believed their own stories. "Dunlap gift to help students bridge college/career gap." Florida State Times. Adam Michaelson (2009) described the meeting at
which Countrywide announced the establishment of the pay-option loan, and after the announcement, he asked, "How did you reach the conclusion that home values, and therefore their ability to be refinanced, might go up forever?" (p. This reduction of approximately $1,900 has been recorded as deferred revenue—affiliate on the balance sheet of
the Company at December 31, 2007. Sunbeam again offered discounts and extended payment terms and sometimes even provided the right to return the goods to Sunbeam if they could not be sold. (a) Edison's revenue recognition practices did not contravene GAAP, but failed to present an accurate picture of the issuer's financial condition. (Quotes
from AAER 1494, 2002) The strength of the FCPA legislation lies in the requirement that companies keep accurate books and records. In May 2008, as a result of its earnings management and other errors, Beazer restated its financial statements to reflect adjustments for the fiscal years 1998 through 2006, as well as the first and second quarters of
fiscal year 2007. Calculate the amount of pretax income that Power Company recognizes in its income statement for the year ended December 31, 2012, if it accounts for the revaluation on the basis described above. LR 19657. a) List the significant stakeholders b) Define the ethical issues Make sure precisely what the ethical issue is—for example,
conflicts involving rights, questions over limits of an obligation, etc. February 24, 2012. Tyco's improper acquisition accounting rules concerning the establishment and utilization of purchase accounting reserves. Noonan himself eventually pled guilty to
misprision, defined as the failure by someone who is not an accessory to prevent or notify the authorities of a felony. Homeownership has long been a part of the American Dream, and as such, it has enjoyed a long history of strong support from the federal government. G GAAP (generally accepted accounting principles), 35, 81, 232, 293 GAAS
(generally accepted auditing standards), 123 Galbraith, John Kenneth, 326 Gas trading, by Enron, 235-236 Generally accepted auditing standards (GAAS), 123 Glass-Steagall Act, 38, 329-330 Global Crossing, 163 Gluck, Robert, 89 Goeken, 80 Goeken, 89 Goeken, 89 Goeken, 89 Goeken, 89 Goeken, 89 Goeken, 80 Goeke
 John, 155 Golden mean, 52 Goldman Sachs, 38 Goodwill, 153-154, 160t, 169-170 The excess of the cost of an acquired company over the fair value of its net assets. Scott D. Ritholtz, Barry. Past SEC Chairman Schapiro (2012) summarized the highlights of the SEC's response to Dodd-Frank, as follows: • In the area of corporate governance, we have
 finalized rules concerning shareholder approval of executive compensation and "golden parachute" arrangements. Around this time, charges of bribery and corruption at the Dabhol plant began to circulate, exacerbated by an anonymous letter sent to Enron's head office. A common hypothetical example of this proposition is a situation where you may
know the location of a person who is hiding from an ax murderer. A company cannot continue for an extended period of time by increasing its cash spent on production capacity while reducing the revenue it gets from that capacity. Sunbeam's internal auditor, Deidra DenDanto, who had been sidelined by management with her concerns about the billined by management w
and hold sales, resigned the same day. February 22, 2013. The American Accounting Association Ethical Decision-Making Model The Amer
together with a call to the decision maker's own "primary principles or values" (qtd. For example, he directed Buca's construction manager to request that Buca's construction manager to request the buca's construction manager that Buca's constru
that the increased risk of the loans was not fully described in the periodic filings, it should be noted that the filings did reveal signals that could have alerted readers to the possibility of loan losses increasing greatly in the future. AAER 1664. Cohen, Stephen. (Of course, money spent on expenses goes into the income statement and reduces profit.
Enron then agreed to buy the full $394 million of gas from another conduit, Stoneville Aegean, and pay for it in installments. Enron used a multiplicity of these kinds of off-balancesheet entities to generate false profits with contrived sales and to keep debt off its balance sheet. Insignia specialized in software that allowed "operators of mobile devices and to keep debt off its balance sheet."
[to] update and repair them remotely..." (Graebner, 2006). Conceived by Jeremy Bentham (1748-1832), utilitarianism holds that the right action ethically is the action that maximizes the good. [A Merrill Lynch analyst] in one e-mail referred to a company that he had bullishly recommended as "a piece of junk." (Levitt, 2002, p. HR 4173. "The
Unkindest Cut," Forbes. Next, Dunlap began asking the executives to present their summaries of the state of their units or departments. • Explain the justice approach to analyzing ethical dilemmas. Due to such an environment of high debt, the SEC concluded that "AHERF, through certain of its senior officers, and in violation of applicable
accounting principles, misstated its financial statements and schedules" (AAER 1283, 2000). For example, in 2002, a portion of the salary of Buca's assistant controller was capitalized. Pincus, Karen. Extract from: The Role of Compliance and Ethics in Risk Management* Carlo V. For Chainsaw Al, it looked 059402_01_ch3_p069-116.indd 73 7/7/14
9:01 AM 74 Chapter 3 • The Sizzling Saga of Sunbeam like a magnificent opportunity. (c) Creation of cookie-jar merger reserves. This method of manipulating financial statements has been added as a separate category in Table 1.1. Chapters 3–9 of this book tell the story of real-world companies that illustrate the top 20 methods of fictitious
financial reporting and also identify the signals left in financial statements that alert readers to the possibility that reported income, as well as assets and liabilities, may have been influenced by these methods. Consulting fees of $276,000, $322,000 and $297,000 were charged in 1999, 2000, and 2001, respectively. The stock price began to fall and
Sullivan reached desperation point in his attempts to portray the company as profitable in the financial statements. AAER 1966. In the period, there was a dramatic increase in the amount of Enron's capital that was financed by debt as opposed to equity, as can be seen in Table 7.7. Over that period, the debt-to-equity ratio
increased from 2.86 to 4.50. AAER 1579. Even if the information in the notes is misleading, the limited disclosure often alerts the reader to the fact that related-party transactions have occurred. 059402_01_ch8_p292-324.indd 296 7/7/14 9:10 AM Chapter 8 • Tall Tales 297 A brief examination of some of the major irregularities involving Adelphia
transactions with Rigas Entities, or with members of the Rigas family, will illustrate the need for concern wherever related-party transactions are revealed in a company's financial statements. Even more devoutly Baptist than Foster, Ebbers liked the school and the town of Clinton immensely and took to southern small-town life, finding the green
openness a refreshing change from downtown Edmonton. Discuss whether the fact that the overstated revenue will likely be earned in later periods reduces the impact of the perpetrator to report revenue accurately in the current period. Apparently, as early as September 2004, Countrywide's own
Risk Management department warned the company's senior officers that "several aggressive features of Countrywide's guidelines (e.g., high loans, interest only loans, interest only loans, reduced documentation loans, and loans with layered risk factors) significantly increased Countrywide's credit risk" (SEC Complaint, June 4, 2009, par
Eventually, Enron would have to recognize these secret debts when it was forced to pay them. Pipe Dreams: Greed, Ego, and the Death of Enron. Table 5.2 WorldCom's Adjustments* Fourth Quarter 2000 $369.9 million Third Quarter 2000 $828 million *Derived from Third and Final Report. WorldCom's stock prices
soared on the grounds of its reported profits combined with its vast Internet capacity and the world's belief in the projected astronomical growth in Internet traffic. The permitting contractor's work mainly concerned the ongoing operations of Buca's restaurants, expenses which are not appropriate for capitalization. Calculate the number of Khaan
shares that must be issued on each repayment date. Perhaps most disturbing of all is that the debt must be repaid eventually, and if it cannot be repaid eventually eve
overstatement of earnings, overstatement of CFFO, and problematic debt levels. Becker, Cinda. 059402_01_ch5_p144-190.indd 146 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom Wizardry: Fr
guarantee the honest reporting of its financial affairs—from the preparation of the gatekeeping intended to provide the checks and balances to ensure the proper accounting behind the preparation of those reports. For instance, in our exams of how firms protect material non-public information (MNPI) from inappropriate uses,
such as insider trading, we have observed instances where firm programs lagged behind new business strategies that created new sources of MNPI. Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did Countrywide, however, did not consider any FICO score to be too low to be categorized within "prime." Nor did not consider any FICO score to be too low to be categorized within the prime of t
category included so-called "Alt-A" loan products with increasing amounts of credit risk, such as (1) reduced or no documentation loans; (2) stated income loans; and (3) loans with loan to value or combined loan to value ratios of 95% and higher. By the 1994 fiscal year, all quarters received significant assistance from nifty accounting that recognized
Respondent's use of sale-leaseback accounting treatment for these transactions despite knowing that such treatment was not in accordance with GAAP. Ebbers to raid the company of huge sums of money by granting or
guaranteeing him loans that totaled over $400 million. I believe that this analysis is also very germane to whether brokerdealers and investment advisers have met their supervisory obligations under the federal securities laws. From approximately 2000 to 2005, a period of strong growth and financial performance for Beazer, Beazer decreased itself.
reported net income by improperly increasing certain reported operating expenses. He made a pretense of compliance; he was really about complicity." IRS-CI Acting Special Agent in Charge Toni Weirauch said, "This scheme relied on sophisticated teamwork to prevent its discovery by investors and law enforcement. Further, the company created
huge overstated merger reserves, which it used as cookie-jar reserves to be released into profits in later periods. 207-208) Typical of many boards in the late 1990s and into the new millennium, WorldCom. Essentially, Enron
persuaded the Canadian Imperial Bank of Commerce (CIBC) to finance a deal that appeared to be a sale of Enron's share in the 20-year Blockbuster contracts. WorldCom, of course, fraudulently reallocated billions of dollars out of its linecost expense into the asset designated as PPE. After graduating from West Point and completing his three-year
military obligation, Dunlap got a job at Kimberly-Clark's New Milford plant in Connecticut. In Sunbeam's financial statements, the effect of releasing cookie-jar reserves together with accelerating sales (as discussed in Scheme 1), combined to provide a very strong signal of its extremely aggressive earnings management. Securities and Exchange
Commission Complaint vs. Former SEC Chairman Richard Breeden said it best when he stated that "[i]t is not an adequate ethical standard to aspire to get through the day without being indicted." 19 In addition, while it is undoubtedly helpful to have certain individuals or groups who are tasked with specific roles regarding mitigating conflicts, the
responsibility of everyone in the organization to identify conflicts and see that they are managed appropriately should always be emphasized. The associated revenue from PRMA was specified in the note and included in the category "Other Revenues" in the income statement. Precisely because of that uncertainty, GAAP rules do not allow a company
to record the profit on such stock until it is marketable. 138). Furthermore, the sellers could file inflated demand schedules to make an electricity line appear to be congested when it was not, and the ISO had no way of checking this information. This strategy was one of a "variety of improper revenue recognition practices" that Sensormatic allegedly
used. Heinzl, Mark. 2004. This revenue from the operating leases would have been received over a number of years over the durations of the leases. 059402 01 ch5 p144-190.indd 174 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom To Suprementation of the leases. 059402 01 ch5 p144-190.indd 174 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom To Suprementation of the leases. 059402 01 ch5 p144-190.indd 174 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom Wizardry:
of conspiracy to commit securities fraud. The National Crisis Inquiry Report (2011) concluded that the financial crisis was unavoidable. LR 18711; AAER 2014. The company used an automated underwriting system known as "CLUES" that analyzed "several variables such as FICO scores, loan to value ratios, documentation type (e.g., full, reduced,
stated) and debt-to-income rations" (June 4, 2009, par. In 1989, LDDS purchased the publicly listed Advantage Companies, Inc., of Atlanta. This is the fourth civil fraud action the Commission has filed in this investigation. (d) The huge loan is treated as a shortterm loan due in one year within the statement of financial position. Rigas and his son
Timothy Rigas, "Prosecutors alleged that the Rigas family siphoned $100 million from Adelphia's subscriber growth and its bottom line." Prosecutors at the trial displayed "more than a dozen allegedly false SEC documents signed by various
family members and receipts for personal expenses, large and small, including those for 100 pairs of slippers ordered by Timothy Rigas." In fact, the prosecutors accused the family of using Adelphia as a "private ATM." (Quotes from Masters & White, 2004) Scheme #2: Improper Use of Non-GAAP Financial Measures Not only are investors interested
in information disclosed in the financial statements but they also like to know that a company's customer base is growing and that the technical quality of the plant and products is high. July 24, 2008. As a result of the process of tranching, a ratings agency could give a higher credit rating to a class of securities carved from a pool of loans than would
be given to other classes of securities carved from the same pool of loans. Consolidated Balance Sheets (in thousands, except share amounts) September 30 2006 ASSETS Cash and cash equivalents Restricted cash Accounts receivable Inventory Owned inventory Consolidated inventory not owned Total Inventory Residential mortgage
loans available-for-sale Investments in unconsolidated joint ventures Deferred tax assets Property, plant and equipment, net Goodwill Other assets Total Assets LIABILITIES AND STOCKHOLDERS' EQUITY Trade accounts payable Other liabilities Obligations related to consolidated inventory not owned Senior Notes (net of discounts of $3,578 and
$4,118, respectively) Junior subordinated notes Warehouse Line Other notes payable Total Liabilities Stockholders' Equity: Preferred stock (par value $0.001, 80,000,000 shares authorized, 42,318,098 and 41,844,414 issued, 38,889,554 and 41,701,955
outstanding) Paid in capital Retained earnings Treasury stock, at cost (3,428,544 and 142,459 shares) Unearned compensation Total Stockholders' Equity Total Liabilities and Stockholders' Equity Total Liabilities and Stockholders' Equity Total Liabilities and Stockholders' Equity 059402 01 ch3 p069-116.indd 113 $ 2005 162,570 9,873 333,571 $ 297,098 — 161,880 3,048,891 471,441 3,520,332 92,157 122,799 59,842 29,465
1,504,688 $ 3,770,516 7/7/14 9:01 AM 114 Chapter 3 • The Sizzling Saga of Sunbeam Beazer Homes USA, Inc. During this time, Lay wrote speeches for Walker that "shook up Washington with their fervor for deregulation." Washington was impressed, and Lay was appointed interim deputy undersecretary for energy. He had never heard of Enron,
however, and was rather skeptical when he traveled to Houston to meet Skilling. CUC's use of top-side adjustments to overstate its earnings is an example of: (a) I m p r o p e r t i m i n g o f r e v e n u e recognition. While virtue ethics is able to address the utilitarian and deontological shortcomings of not attending to ethical agents, it is liable to be
famous proponent of virtue ethics. Nevertheless, a line of clippers was moved out of McMinnville and large numbers of sales were lost because of unanticipated production shortages caused by the restructuring plan. "Financial Regulation: A Primer on the Dodd-Frank Act," May. Consolidated Balance Sheets (In thousands, except share and per share and per
data) December 31, December 31, December 31, December 31, 2007 2006 ASSETS Current assets Cash and $433 allowance for doubtful accounts Inventory Current portion of notes receivable, net of $524 and $433 allowance for doubtful accounts Inventory Current assets Property
 and equipment Property and equipment Less: accumulated depreciation Property and equipment, net $ 35,456 3,167 11,443 $ 54,567 2,416 9,123 1,055 338 714 — 1,233 52,692 634 67,454 15,945 14,300 13,621 1,394 12,227 (continued) 7 Extracted from 10-K filings for Basin Water, Inc. Predictably, with the highly discounted sales before
Scott was sold, its sales were slow in the next period. money.cnn.com. The following information relates to Murky Mortgage's portfolio of loans at year end (excluding negative amortization) $100 million Interest earned for year $5 million Negative amortization accrued during th
year $2 million For Discussion 31. Kershaw, Sarah. As a consultant to Enron, Skilling provided the answer—what he called the Gas Bank (Swartz & Watkins, 2003, p. "Verizon Business." January 23, 2006. The strategy was essentially for Enron to use interlocking SPEs as a front to borrow cash from a financial institution; then some of the money
would be passed on to Enron via the contrived sale of Enron's poorly performing assets to that SPE. Sterba has also identified "in rem" rights, which hold against the world. Brigham Young University, Spring. Tyco's Ratio of Sales to Total Assets over the period 1998-2002 and then discuss
whether investors should have been troubled by the trend in this ratio. Zalta. December 3, 2012. Not surprisingly, no buyer was foolish enough to buy into this messy situation. How could fewer people produce and sell more? Philosopher Joel Schickel (2009) explains that "because good accounting practice antecedently requires the formation of good
moral character, professional ethics in accounting presupposes that practitioners come to the profession already having been formed in certain moral virtues." Applied Ethics: Ethical Decision-Making Models in the Business World Having considered the approach of the three major normative ethical theories, we must now examine how these ethical
theories apply to decision making and ask, "How do we decide what the right action is?" In answering this question, John E. "Dangerous Games," Barron's. Interestingly, David Huddie, head of Rolls-Royce's Aero Engine Department at that time, later received a knighthood from the Queen of England for securing the contract to supply the engine for
the TriStar. However, Enron would have to agree to guarantee the repayment of all the cash received, plus interest, at some point in the future. This was such an innovative idea that MCI immediately had to raise money to fight the legal battles launched by AT&T and General Electric to shut it down. Smith, Rebecca and Arron Lucchetti. The
                                                        ng with respect to individuals. UUNet had been one of the first companies to offer e-mail and Internet access to individual users. Between the market competition and the requirements of the Public Utility Commission, the charges to customers were more or less set. She now reportedly runs an art consulting
("The Defendants of the Enron Era," 2011). Revenue recognized on Enron's own stock. 496). Buchan, Howard F. • Overstate the company's earnings. From 2000 until 2004, Micatrotto, Gadel, and others treated the company's earnings.
Highland 2000 never paid cash for the securities. How did the development costs at Livent differ from preproduction costs at Livent differ from preproductio
improperly booked millions of dollars of revenue for purported software license sales to resellers. Compared to demand at that time, there had been a massive overinvestment in fiberoptic lines and Internet backbone hardware; in fact, the investment anticipated at least ten times the actual demand. With the lure of tantalizing riches from stock
options, many top executives could not resist the temptation to present financial statements that satisfied Wall Street's earnings expectations. The letter also claimed that MSEB could not pay its bills. "Downsizing or Dumbsizing?" BYU Magazine Online. To make matters worse, the Wessex facilities had to be upgraded, and the cost for this was
astronomical. Not surprisingly, Dunlap got on well with him and perhaps even imitated him. Without the technology in place, the Blockbuster project was a disaster and never went beyond a feeble pilot program. Distributive justice is concerned with how goods are
                                                                                                                                                                                                                                                                                                                                                                                                            . The company has nothing to lose and everything to gain" (gtd. With these
schemes, it was no wonder that Enron insider jokes began to circulate referring to Enron's mark-to-market accounting (McLean & Elkind, 2004). 5 The SEC issued a cease-and-desist order against Krispy Kreme in 2009 (AAER 2941). With reference to Sunbeam's financial statements, in the period
that Sunbeam overstated its restructuring expense and restructuring ex
or course of action—an extension of the utilitarian approach. Emshwiller, John R. Either way, if one considers the overstatement of expense, the most frequently used methods of fictitious financial reporting as described in Table 1.1 continue to occur. Of all the
changes brought about by Dodd-Frank, its whistleblower program has garnered a great deal of attention from the media because the whistleblower snot only are offered more protection than under SOX but also can now receive monetary awards from the SEC, which is pursuing whistleblower tips very seriously. June 27, 2013. Signal #2: Unexpected
and Unusually Large Increases in Gross Margin as a Percentage of Sales Sudden, significant increases in gross margin as a percentage of sales are indications of possible overstatement of inventory and understatement of inv
short and long, and positive and negative consequences for the major alternatives. Though he offered insights on his behavior, he did not offer excuses or shift blame. The SEC commented: The adjustments were entirely top-side adjustments were entirely top-side adjustments.
not give the telephone to him. Krispy Kreme's growth was too rapid with the addition of many new franchised stores at the expense of existing franchises. Transparency, lack of, 39 Travelers Insurance, 329-330 TriStar, 207-208 Troubled debt restructurings, 358-359, 360 Turnover ratio or sales-to-assets ratio, 170 The ratio of a business entity's total
sales to the total amount that it has invested in all of its assets. Beazer restated its fiscal year 2006 net income from $389 million to $369 million to $360 million to $360
cash flows. Which of the following is not a signal of overstatement of earnings by improper use of merger reserves? Ultimately, however, the judge found that Dunlap had engaged in "extreme cruelty" and awarded Gwyn sole custody of their son. By this time, Fastow had realized that he had complete control of the cash borrowed by an SPE, and the
golden goose was his for the plucking. They were in a bind. They renamed the business Sunbeam-Oster. In the first guarter of 1998, in order to include the results of its newly acquired company, 28. Under the reorganization plan, most of the
bank debt would be converted to equity and shareholders would receive nothing ("Bankruptcy Judge," 2002). April 13, 2006. (c) One of the outside directors is a former CEO of a law firm. Although the amount of this reserve varied by region, it was typically $2,000 to $4,000 per house, above known outstanding invoices. CFFO refers to the amount of
cash generated from the company's main operating activities. However, the allowance for loan losses as a percentage of all loans held for investment actually decreased from 0.314 percent at the end of 2004 to 0.27 percent at the end of 2005. Signal #1: Accounts Receivable Increasing as a Percentage of Revenue When the accounts receivable
amount increases as a percentage of revenue, it is a signal that the revenue recognized may be accelerated or fictitious. It developed and supported cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to resellers, to whom it granted cross-platform compatibility software, which it generally sold to reseller to the sold to reselle
based pipeline and power generating company to a marketing and logistics company" (p. The SEC also found that Livent employees recorded revenues before they should have by recognizing revenues that were subject to side agreements. "Deloitte to Pay $167.5M in Adelphia Case." www.cfo.com. In a 1998 e-mail, a Chase banker wrote, "Enron loves
these deals ... Gadel and Skrypek approved many of Micatrotto's reimbursement requests, even though they knew, or were reckless in not knowing, that some of the requests contained personal expenses. (b) I m p r o p e r t i m i n q o f r e v e n u e recognition. (AAER 1678, 2002) This estimate of $9 billion would increase, after further investigation,
to close to $11 billion. The same much-lauded "off-balance-sheet" strategies that Fastow innovated to make Enron seem financially healthy were the ones that, upon closer review, landed him in jail. From a purely technological point of view, the system was a marvel. 1998-2002. March 4, 2009. And the financial sector would deliver the biggest
bankruptcies and bailouts in American history. Explain the similarity, if any, between this signal in Adelphia's notes to its financial statements. Use the American Accounting Association's Model to analyze this case from the point of view of a chief compliance
officer who wants to act ethically in this situation. A long, dry season reduced the supply of hydroelectricity, and the start of a long, hot summer increased the demand for electric power. (b) When unconsolidated affiliates—especially constructed entities such as 7/7/14 9:08 AM 282 Chapter 7 • Enron and the Tale of the Golden Goose partnerships—
are used to generate a significant portion of the community. Refer to Table 7.1 for Enron's pretax gains on sales of merchant assets from 1997 to 2000. Multiple-Choice Questions 21. R Raptors, 259-261 Rating agencies, 328 Ratio of
sales to assets, 170-171 Rebates, 82-83, 200-201, 217-218 Recipient rights, 56 7/7/14 9:17 AM Glindex 397 Related-party transactions, 269-270, 272, 291, 296 Dealings with any party that controls or can significantly influence the operations of a company so as to prevent the company from properly pursuing its own interests. Loans with close to 100
percent loan-to-value ratios and loans on which interest is not being fully paid depend on rising house prices to avoid loan losses when borrowers default. The report found a weakened 'tone from the top' and more pressure on financial professionals—especially in emerging economies—to act unethically" ("CGMA Report," 2012). (pp. WilTel, previously
Williams Oil and Gas, had experienced a severe drop in demand for its gas and wondered what to do about the idle capacity in its gas pipelines. Skilling's Gas Bank. The plan was for Enron itself to be the Gas Bank. So when a reserve that was created is reversed because it isn't needed, it erroneously appears to be an increase in the earnings in the
period into which it is released. Then Enron repurchased LJM1's stake of Cuiába in August 2001 for $14 million. The leading example of such an aggressive policy is the practice of recognizing sales revenue before the goods are shipped to the customer. The cash for the extra equipment and the equipment itself went on a "round-trip" to the
franchisee and back to Krispy Kreme. The independent owner must exercise control of the SPE. And the more jobs he cut, the tougher and smarter the press made him look. Consolidated Statements of Cash Flows (In thousands) Years Ended December 31, 2007 2006 2005 Cash flows from operating activities Net income (loss) Adjustments to
reconcile net loss to net cash provided by operating activities: Depreciation and amortization Stock-based compensation expense Gain on sale to affiliate Issuance of warrants for services Write off of loan acquisition costs $ (15.250) $ (11.167) 995 1.706 (2.500) — 1.024 744 — 34 401 $ 563 506 31 — 417 — (continued) 059402 01 ch7 p226-
291.indd 288 7/7/14 9:09 AM Chapter 7 • Enron and the Tale of the Golden Goose 289 Years Ended December 31, 2007 2006 2005 Changes in operating assets and other Accounts payable Deferred revenues Accrued expenses and other Contract loss reserve Net book
value of systems sold Issuance of notes receivable Other assets and other liabilities Net cash used in operating activities Cash flows from investing activities Cash flows from financing
activities Issuance of common stock Repurchase of common stock Proceeds from employee stock option exercises Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from employee stock option exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from warrant exercises Issuance of redeemable preferred stock Proceeds from the proceeds from t
(decrease) in cash and cash equivalents, beginning of period (1,817) 103 (542) 1,600 (117) (1,515) 3,550 4,091 (3,353) (207) (13,256) (4,489) (367) (45) (588) (501) 2,018 3,725 636 \\ (3,386) (12,361) (6,279) (268) (80) 1,468 (354) 397 \\ (3,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (367) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,489) (4,
(11,592)(3,942) - 100(99)(3,941)(1,913) - 325(107)(1,913) - 325(107)(1,695) - (552)5278,060 - - (2,298)5,737(19,111)54,567$ 3,584 - - 596 5,156(100)(112)9,124 1,020 1,704 2,724 From Basin's 10-K 2007 NOTES, Pages F20-F228 Note 9: OTHER ASSETS Goodwill
The table below summarizes the changes in the carrying amount of goodwill for the year ended December 31, 2007 $ -8,682 $ 8,682 Long-term Accounts Receivable and Notes Receivable The Company has four customer system sales
agreements which provide for payment terms ranging from two to five years, unless certain conditions are met, in which case the payment terms are 8 Source: U.S. Securities and Exchange Commission. • Enron, once the biggest energy trading company in the world, was worth over $68 billion before it went bankrupt in December 2001. These cases
were brought in coordination with President Barack Obama's Financial Fraud Enforcement Task Force, on which Mr. Bharara serves as a Co-Chair of the Securities and Commodities Fraud Working Group. Signal #5: Adopting a More Aggressive Revenue Recognition Policy The fifth signal that a company is overstating its sales is when it begins a
policy of more aggressively recognizing revenue. Management was also aware of Sensormatic's high price-to-earnings ratio as well as the effect that faltering growth would have on the stock price. This, however, was a misnomer, as California was really engaged in what amounted to a semi-deregulation of the prices that customers paid the utility
companies for electricity and the prices that the utilities paid the power companies. March 19, 2009. In Enron's case, unrealized revenues were split between accounts receivable and assets from price risk management activities (PRMA). Cambridge University Press. The situation worsened as more OTS-mandated appraisals came in. For example, in
the case of one district (District A) in 2001, no cash at all was paid to Edison because, according to the district, the total "Per Pupil Fees" amounted to $7.5 million and the district paid expenses were $8 million in total. Skilling appointed Lou Pai, a brilliant trader with little respect for the hard-asset pipeline business, as head of the floor and trading
operations, 059402 01 ch4 p117-143, indd 135 Required a, Based on their audit, Lucas and Eva determine that someone is embezzling money from Stylish Shoes. In this way, investment banks could provide free enterprise lenders with AA or AAA ratings from the now powerful credit-rating firms. In addition, there was some suspicion about just how
much downtime the power plants really needed for maintenance. California's energy system was a formula for disaster—even without the pervasive abuse that engulfed it on so many fronts. According to Enron's Bankruptcy Examiner, the effect of Enron's Bankruptcy Examiner, the effect of Enron's much downtime the power plants really needed for maintenance. California's energy system was a formula for disaster—even without the pervasive abuse that engulfed it on so many fronts. According to Enron's Bankruptcy Examiner, the effect of Enron's 
States District Court, Central District of California. From this point on, Enron began to focus more on recording accounting profit than on making cash—so a huge problem was born. (b) The investment banking company. "The Numbers Game." Remarks at NYU Center for Law and Business, New York. 2 059402 01 ch2 p047-068 indd 65 7/7/14 8:59
AM 66 Chapter 2 • Ethics at Work of the consequences of the concealment is that the IRS was hindered from performing its lawful duty, thus harming our nation's law abiding taxpayers, along with the defrauded victims, www.coso.org, Kirk Shelton, joined Forbes in directing the scheme from at least 1991 onward (AAER 1372, 2001; LR 16919,
2001). The party required to deliver the commodity in the future cash selling price less a discount. Top-side entries, 127-128 Entries recorded in the financial statements but not in the general ledger or other formal accounting records. "Enron
Trial to Highlight 2006 Corporate Scandal Cases." December 26, 2005. As subdivisions were built, Beazer allocated the land acquisition cost, as well as past and future common development costs, to individual home lots which were then offered for sale. Taub, Stephen. • Describe BellSouth's improper accounting for foreign payments in violation of
the Foreign Corrupt Practices Act (FCPA). That's a signal to industry producers—the black-and-white television industry, for example—to retrain, retool, and move into other areas, which may cause some downsizing." As Perry explained: "Increased resource utilization is good for both business and society. The inventory turnover ratio is a common
measure of how many times an entity's inventory has been sold or replaced during a period. Certain Peregrine senior officers, and sales and finance personnel knew, or were reckless in not knowing, that the applicable accounting rules prohibited
revenue recognition on these and other transactions for which Peregrine booked revenue. 059402 01 ch4 p117-143.indd 118 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 119 Sensormatic is presented mainly as an example of improper timing of revenue recognition via holding books open after the close of a reporting period. Over that same time,
revenues dropped from $10.2 billion to $8.9 billion to $8.1 billion. www.fanniemae.com. (c) Operating income will increase by $15,000. Such a change could, of course, be the result of an improvement in efficiency or of legitimately paying off current liabilities earlier—for example, by obtaining a long-term loan. 059402 01 ch7 p226-291.indd 276
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7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 277 However, trading profits are extremely erratic, and Jim Chanos, a broker and shortseller, called Enron a "hedge fund sitting on a pipeline." Chanos also noted that "Enron was a speculative trading shop, which meant that, at an absolute minimum, its outsize price-to-earnings
multiple made no sense." (Qtd. Enron arranged for Barclays Bank to provide $11.4 million for an Enron employee to acquire 3 percent of the equity capital of the SPE named Chewco, and Enron provided a $6.6 million collateral for its repayment. (a) Do you think her duty-based approach to ethics supports or undermines your promotion? • Ability?
Lay, Enron's Former Chairman and Chief Executive Officer, with Fraud and Insider Trading," U.S. Securities and Exchange Commission, 2004-94, July 8, 2004. May be indicative of any method of overstatement of earnings, or overstatement of earnings, or overstatement of earnings.
the SEC's final judgment "without admitting or denying the allegations." Assaf, Pardue, and Simmons were ordered to pay "civil money penalties of $50,000, respectively" (AAER 1020, 1998). Numerous executives have been exposed in cases of greed and betrayal, of blatant duplicity and moral bankruptcy. • A breakdown in
responsibility and ethical standards. In dealing with the problem of how to teach and cultivate the virtues, virtue ethics often uses narratives to illustrate how a virtuous person acts. 059402 01 ch4 p117-143.indd 139 7/7/14 9:02 AM 140 Chapter 4 • Hocus Pocus MARCH 31, 2000 82,717 29,537 1,192,855 233,504 Property and
equipment, net Goodwill, net of accumulated amortization of $334,178 and $54,406, respectively. According to the December 31, 2007, 10-K, "TierOne Corporation on erroneous financial statements could result in the audit firm being sued for
monetary damages. Production of these engines was continually delayed by the Automaker until October 2002, when it cancelled the Agreement and discontinued its V-6 engine program with Navistar. "Ex-Cendant CFO Avoids Prison." CFO.com. This acceleration of future quarters' sales into the present quarter "provided a misleading impression of
the Company's results of operations for the present periods." A worse consequence, of course, was that it "also resulted in the erosion of the company's profit margins and impoverished sales in later periods." In a nutshell, this began a death spiral because the ploy would have to be repeated in the future in order for the company to announce success
in meeting target sales. www.fbi.gov. September 1, 1998. 2). AAER 1275. The SEC found that at least $35 million of this was overstated (AAER 1393, 2001). 117 059402 01 ch4 p117-143.indd 117 7/7/14 9:02 AM 118 Chapter 4 • Hocus Pocus In a speech given several years ago, past SEC chairman Arthur Levitt (1998) spoke about the numerous
companies that "operate in the gray area between legitimacy and outright fraud." He observed, "Integrity may be losing out to illusion." In order to achieve these illusory earnings and fabricated balance sheets, many companies resort to what Levitt described as "hocus pocus." This chapter presents a brief overview of, at worst, some of the lesser-
known, intentional revenue-recognition accounting frauds or, at best, misguided attempts to "improve" a company's financial statements with aggressive accounting. However, the Commission found that at least $6 million of this reserve was overstated. "Lockheed L-1011," Super70s.com. In the early 1970s, Lay's undergraduate economics professor
Pinkney Walker, was appointed to the Federal Power Commission, and Walker selected Lay as his chief aide. Second, knowing that a new firm would be arriving the following year and reviewing the work papers and the client's financial statements would have been an added incentive for external auditors to resist management's pressure to
compromise their audits. It reported restated revenue of $13.1 million in the first quarter, compared to $14.7 million previously reported. As the Bankruptcy Report pointed out, "It is the inappropriate release of these reserves that results in one form of earnings management" (First Interim Report, 2002, p. Specifically, reflect on the Supreme Court
statement from almost 50 years ago and discuss how it applies to the crisis of 2008. In his First Interim Report (2002), Richard Thornburgh, WorldCom's Bankruptcy Examiner, presented a list of the gatekeepers who failed WorldCom's Bankruptcy Examiner, presented a list of the gatekeepers who failed WorldCom's Bankruptcy Examiner, presented a list of the gatekeepers who failed WorldCom. The majority of corporate fraud cases pursued by the FBI involve accounting schemes to deceive investors, auditors
and analysts about the true financial c ondition of an entity in the form of manipulation of: (a) Financial data in the statement of financial position and income statement. But ultimately, they were gamblers, and they "bet—on anything" (Swartz & Watkins, 2003, p. In what ways did Livent understate the expenses in the financial statements? With
LJM1, Enron had overstated its earnings via its related-party transactions, had overstated the cash flow reported in its financial statements, and had falsely driven up its stock price. Beginning in 2000, Gadel and Skrypek would preliminarily assess Buca's financials at the close of each quarter and then determine how much income they needed to
"find" in order to meet analysts' earnings estimates for Buca. Holdings of more than 50 percent of the equity of the investee, where the investee is deemed to have a controlling interest. The lease cost of lines was high, and with ATC, Ebbers got a large supply of his own fiber-optic lines. However, these risky loans were issued in addition to the risks
on other exception loans issued at standards below regular underwriting standards. They were perhaps driven by a quest for power as well as intense greed. Predictably, that is what ultimately happened. Bowie and Velasquez discussed ethical issues, which are uncertainties and the ability to execute a project during decision making. Income
Statement Operating income Year 1 $ 1,000 Year 3 $ 
that should be recognized in a later period in order to have it recognized in a current period, its revenues, operating income, and net income increase, but its cash received does not. Short-Answer Questions 33. • August 14, 1996. Because our ultimate end is to comprehend the good, Aristotle thought we are happiest when we perform right action.
Mozilo did not admit or deny any wrongdoing in respect of this case (Dobuzinskis & Levine, 2010). Considering how fast the stock market as a whole was climbing in 1996, Sunbeam's stock had moved upward relatively modestly after the initial jump on the announcement of Dunlap's appointment. III, Director, Federal Bureau of Investigation. Signal
#2: CFFO Falling Behind Operating Income OR NET INCOME When CFFO decreases relative to operating income or net income, this is the prime signal of a company recognizing any form of profit ahead of time. However, Enron's gatekeepers who reviewed the Whitewing structure and Enron's financial statements apparently did not ask that
question. For the first two quarters of fiscal 2007, Beazer understated its cumulative reported net loss of $102 million by $1 million due to the reversal of improper land inventory reserves. The SEC maintained that Rite Aid's resulting restatements in July and October 2000—in which the company restated reported cumulative pretax income by a total
of $2.3 billion and restated cumulative net income by $1.6 billion—represented what the SEC called "the largest financial restatement of income by a public company" at the date of that report (AAER 1579, 2002). 103). In 2011, their convictions were upheld by the Ontario Court of Appeal, but their sentences were reduced by two years each (Dobby,
2011). Krispy Kreme was constantly mentioned in the media, and even people who had never eaten a doughnut became familiar with the brand. At the Enron's own ethics rule—which was supposed to prevent officers of the company from doing business with the company—and
approved the formation of LJM1 to be controlled by Enron's own CFO, Andrew Fastow. Unfortunately, Enron did not plan ahead as to how they would fulfill such promises of cheap power. • The Department of Justice made corporate fraud and other corporate f
Gottlieb were convicted of fraud and forgery by the Ontario Superior Court of Justice in Canada in 2009. There are "action" rights, or the rights to do things, such as to express your opinion. Finally, Beazer also restated its net loss for the first quarter of fiscal year 2007 from $59 million to $80 million (an increased loss of $21 million or 36%), and its
net loss for the second quarter of fiscal year 2007 from $43 million to $57 million (an increased loss of $14 million or 33%). By now, Ebbers was a keen acquirer of companies and was growing into a fanatical one. . • Insignia was briefly in danger of losing its listing on the Nasdaq due to falling out of compliance with Nasdaq capitalization
requirements. Table 2.1 The American Accounting Association Ethical Decision-Making Model* 1. Determine the facts—what, who, where, when and how? Singleton invited Ebbers to a meeting about starting a company to resell long-distance phone service. 21, x, xiv) Angelo Mozilo was another Countrywide executive who tried to warn the other
executives that these pay-option ARM loans could be toxic. The Enron board's approval of an arrangement with such potential for disaster was astonishing. Besides the vendor fraud, what other signs of ethical disintegration does Noonan now believe were present at Rite Aid? FICO scores range from approximately 300 to 850, with a higher score
indicating an individual with a more favorable credit profile. In the midst of all the tricks, Stuart Zisman, an attorney in Enron's financial statements. Sunbeam changed its quarter end from March 29 to March 31. A significant
decrease in the ratio of sales-to-total sest-turnover ratio), or a decrease in the ratio of sales to any particular asset such as, for example, property, plant, and equipment (PPE). Responsibilities of Corporate Management (Section 302 requires that the chief financial officers (CFOs) of SOX) Section 302 requires that the chief financial officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (CFOs) of SOX (Section 302 requires that the chief executive officers (Se
public companies assume responsibility for certifying specific areas of "each annual or quarterly report filed or submitted" to the SEC. Key Terms Death-spiral financing 249 Futures market accounting 249 Futures market 232 059402_01_ch7_p226-291.indd 278 Mark-to-market accounting 232 Prepays 235 Put option 255 Securitization 234 Special purpose
entity 248 Times-interest-earned ratio 274 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 279 ETHICS AT WORK Questions: a. www.sec.gov 059402_01_ch5_p144-190.indd 189 7/7/14 9:08 AM Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom SEPTEMBER 30 2000 Accrued expenses and other current
liabilities Contracts in process—billings in excess of costs Deferred revenue Income taxes Deferred income taxes Total current liabilities COMMITMENTS AND CONTINGENCIES (NOTE 17) MINORITY INTEREST SHAREHOLDERS' EQUITY
Preference shares, $1 par value, 125,000,000 shares authorized; 1,684,511,070 shares owned by subsidiaries in 2000 and 1,432,678 shares owned by subsidiaries in 1999, net of 31,551,310 shares owned by subsidiaries in 2000 and 11,432,678 shares owned by subsidiaries in 1999.
This elevated investors' trust in the ability of these rating agencies to accurately grade risk. Table 9.3 Illustration of Loans and Allowance for Loan Losses Derived from Countrywide's 10-Ks (in thousands, except for percentages)* 2007 2006 2005 2004 Loans held for investment Net of allowance for loan losses $ 98,000,713 $78,085,757**
$69,865,447** $39,661,191 Allowance for loan losses $ 2,339,491 $ 261,054** $ 189,201 $ 125,046 Loans held for investment before allowance for loan losses $2,339,491 $ 261,054** $ 189,201 $ 125,046 Loans held for investment before allowance for loan losses $2,339,491 $ 261,054** $ 189,201 $ 125,046 Loans held for investment before allowance for loan losses $2,339,491 $ 261,054** $ 189,201 $ 125,046 Loans held for investment before allowance for loan losses $2,339,491 $ 261,054** $ 189,201 $ 125,046 Loans held for investment before allowance for loan losses $2,339,491 $ 261,054** $ 189,201 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for investment before allowance for loan losses $100,340,204 $ 125,046 Loans held for loan losses $100,340,204 $ 125,046 Loans held
• 90 days or more \dagger • 60 days or more 5.71% 0.65% — 0.10% 0.22% — 0.08% * Table 9.3 is derived from Exhibits 9.1, 9.2, 9.3, and 9.4 which are given after the WorldCom Bankruptcy Examiner identified as being responsible for the overall control of a company. Incomplete
Disclosure of Loans or Underestimation of Allowance for Loan or Mortgage Losses and Overstatement of Loans Held for Investment and/or Investment and/or Investment of Loans or Underestimation of Allowance for Loan or Mortgage Losses and Overstatement of Loans Held for Investment and/or Investment and
convicted" (Bray, 2006). On the day that the letter arrived from the SEC giving Skilling permission to use this new accounting policy, he bought champagne to celebrate with his division's staff (Bryce, 2002, p.68). August 10, 2005. It [cash] wasn't on our annual review or included Table 7.5 Enron's Adjusted Cash Flow from Operations Compared to
Its Operating Income: 1997-2000 1997 1998 1999 2000 CFFO $211 M $1,640 M $1,228 M Possible Securitizations ($128 M) $2,400 M Operating Income $ 15 M $1,378 M $ 802 M $1,953 M $4,779 M * M = million. In early 1988, the
company filed for bankruptcy. 7/7/14 9:10 AM Chapter 8 • Tall Tales of a suspicious payment without proving that the payment was for an illegal activity. 140). The employees were great employees were great employees were great employees. "Payments to Date." May 2, 2011. Enron traders knew that if a cold front was advancing, it would cause gas prices to increase; so the company
employed meteorologists to help them predict the weather and, in turn, to predict future gas prices. (b) Is not eligible to receive a monetary award. Improper capitalization of an expense as an asset. Beginning in the first quarter of 1997, Sunbeam recorded contingent sales or quaranteed sales as normal current-period sales. www.fasb.org "Fastow
and His Wife Plead Guilty." January 14, 2004. Management fees; 3. June 24, 2011. The SEC stated that regarding $77 million of such refunds that Rite Aid recognized for FY 1999, the sales had not yet occurred. Days sales outstanding (DSO), 90, 121-122, 124 Death-spiral financing, 262, 275-276 An arrangement in which a
059402 01 GLINDEX p383-401.indd 387 borrower agrees to repay a loan amount in the form of the borrowing company's own stock. After getting married and working briefly in a bank, Skilling was accepted at Harvard Business School, where he graduated in the top 5 percent of his MBA class and then joined McKinsey. • Students are
presented with a variety of original, primary documents (or relevant extracts from such documents), adding a high level of authenticity to the realworld cases covered in the text. Litigation Release, April 19, 2005. Both HNG and InterNorth were first-rate companies with impeccable credentials, and both were targets for hostile takeovers. The stock
price dropped a little that day but remained in the high $20 range right into March 1997. The most famous proponent of virtue ethics was
                                                                                                                                                                                           . Second, according to Aristotle, "the telos of man as a species ... determines what human qualities are virtues." Traits such as temperance and practical wisdom are considered to be virtues. In
November 1985, it appointed Kenneth Lay as the CEO of the new conglomerate. He was sentenced to 25 years in prison. November 1, 2009. It was a real crisis. Even more capital could be freed up to flow into home loans if Fannie Mae were allowed to sell to investors the loans it had purchased from lenders. Certainly, from the first four signals alone
anybody reading Sunbeam's financial statements at the end of 1997 should have been alerted to the fact that its reported sales and operating profits were unreliable. Improper deferral of expenses, 192, 193, 194-195, 197 Any technique that avoids the recording of an expense in the current period by shifting the recognition of the expense to a later
period's financial statements. Segnar was keen to shut out the chance of a hostile takeover by a corporate raider and believed that all the debt InterNorth would incur by buying HNG would make it immune to a future takeover. Yet all students taking one course can be required to write five essays in a semester, whereas all students taking a different
course could be required to write seven essays in the same semester, and so on. Byrne, John A., Louis Lavelle, Nanette Byrnes, and Marcia Vickers. While so many accepted the downsizing program as an explanation for that alltoo-quick turnaround, for others, the downsizing made a quick growth in sales seem implausible. In accounting terms, if
certain conditions are met, the SPE's debt need not be "consolidated" with the company's debt and its assets are not added into the company's consolidated balance sheet. Signal #7: Guaranteed Sales The recording of sales when the customer has a right to return the product is a signal of the overstatement of sales. When investments in
unconsolidated affiliates or related-party transactions occur with specially constructed entities such as partnerships, trusts, or joint ventures—as opposed to independently established companies—one should be on the alert that the company could be using SPEs to understate debt and boost earnings. However, at the end of the first quarter of 1996
when most of the goods were still unsold, the Commission found this resulted in the revenue being overstated by $1.1 million. Explain why. The beauty of the scheme for the current period was that Enron was able to report this loan transaction as a sale in its financial statements. The investigation that led to today's guilty plea by Madoff serves as a
stern warning to those who would knowingly undermine the financial well-being of workers. CONSOLIDATED STATEMENTS OF CASH FLOWS (IN THOUSANDS) YEAR ENDED MARCH 31, 2001 Cash flows from operating activities: Depreciation
amortization, acquisition costs and other Increase (decrease) in cash resulting from changes in: Accounts payable and other liabilities Accrued expenses Deferred revenue Net cash (losed in) provided by operating activities Cash flows from investing activities: Acquisitions and investments, net of
cash acquired Purchases of short-term investments Maturities of short-term investments Purchases of property and equipment Net cash used in investments Purchases of short-term investments Maturities of short-term investments Maturities of short-term investments Purchases of property and equipment Net cash used in investments Maturities of short-term investments Purchases of property and equipment Net cash used in investments Maturities of short-term investments Maturities of short-term investments Purchases of property and equipment Net cash used in investments Maturities of short-term investment
17,328 12,467 (18,984) (5,678) (245) 2,939 12,486 4,874 (10,171) 57,611 19,803 17,974 — (49,031) (41,249) — 2,000 (20,713) (11,128) (49,000) 54,027 (12,426) (31,057) (59,962) (18,527) (continued) 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 143 YEAR ENDED MARCH 31,2001 Cash flows from financing activities: Issuance (repayments) of long
term debt Issuance of common stock Issuance of convertible subordinated notes Net cash equivalents, beginning of period Cash and cash equivalents, end of period
Cash paid during the period for: Interest Income taxes Supplemental Disclosure of Noncash Investments 059402 01 ch4 p117-143.indd 143 1,284 42,501 (1,611) (6,415) 261,900 2000 1999 (7,832) 23,427 — (1,285) (1,174) 7,921 — (1,463) — 297,659 (3,284)
14,310 7 35 5,284 253,147 11,966 6,595 33,511 $ 286,658 21,545 $ 33,511 $ 286,658 21,545 $ 1,069 $ 1,587 $ 451 $ 3,015 $ 26 $ 155 $1,762,952 $253,209 $105,499 7/7/14 9:02 AM Chapter 5 WorldCom Wizardry: From WorldCom Vizardry: From Vi
accounting in connection with business combinations (via improper use of acquisition or merger reserves and improper asset valuation). Furthermore, in response to Title VII of Dodd-Frank, the SEC is working with the Commodity Futures Trading Commission (CFTC) to develop regulations that will stabilize and fortify our financial system in the
following ways: • Increasing centralized clearing of swaps and ensuring that capital and margin requirements reflect the true risks of these products. Buca, through Gadel and Skrypek, improperly capitalized at least $1.5 million worth of invoices submitted as part of an arrangement involving High Wire and EDP. Obviously, a fictitious asset cannot
produce revenue. This was part of its creation of cookie-jar reserves—reserves created by overstating a future period, thereby implying that the company has less expense in the future period, when the earnings fail to meet the hyped expectations, the company has less expense in the future period. As the future period, thereby implying that the company has less expense in the future period.
 "cookie jar" in the form of the reserves that it does not really need. Only the costs that are truly caused by the division is closed. The corporation was beset with problems that ranged from store closures to rumors about problematic acquisitions and inaccurate
accounting practices. Business was declining; WorldCom had run out of acquisitions to falsify profits; the stock price was falling; Ebbers's loans were eating cash; and a number of suspicious events had caught the attention of WorldCom's now famous internal auditor, Cynthia Cooper. Certainly, a company cannot continue to incur losses indefinitely
and if it goes into bankruptcy or scraps a segment, certain intangible assets—such as development costs, and goodwill—will not be saleable. Yet accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head. In 1998, using markto-market accounting fraud still continues to rear its ugly head.
million in its income statement. He appeared to have forged ahead blatantly, without consolidating LJM1 into Enron's financial statements, in direct contravention of conventional accounting practice. Explain why overstating sales by holding books open after the close of a period would cause CFFO to lag behind operating income. Instead, he's back at
the modest Woodbury neighborhood home he bought for $170,000 in 1990" (Clough, 2009). (c) No decrease in operating income and no decrease net income in the period of the acquisition. Maximum utility, 55 MBSs (mortgage-backed securities), 327, 328, 332 McConnell, David, 206 McDonnell Douglas, 206 McGowan, William, 155 MCI, 155-157,
169, 175 MD&A (Management Discussion and Analysis), 293-295 Merger, 156 One business entity acquires all of the stock in another business entity by the issue of stock or payment of cash or property. Explain how Signal #3 could have alerted users of TierOne's financial statements that its allowance for loan losses at December 2008 may allegedly
have been understated. Healy, Beth. Furthermore, cash flow from operations (CFFO) lags the falsely reported profits and it becomes difficult to make sales in the following periods. At this stage, all of its transactions have been recorded properly in terms of GAAP. AAER 1020. The reason is that in the statement of cash flows, the fraud simultaneously
overstates CFFO and the amount of cash used in investing activities. In pre-Enron accounting, because such entities operate for a specific purpose, the Emerging Issue Task Force (EITF 90-15) allowed SPEs to be excluded from consolidation with the sponsor's group financial statements "as long as the equity interest of a third party owner was at least
3% of the SPE's total capitalization; at the same time, the majority of equity voting rights cannot reside with the beneficiary" (Soroosh & Ciesielski, 2004). A significant decrease in Insignia's allowances for returns as a percentage of sales is a signal that the allowance for returns may be . Explain how Adelphia misreported nonGAAP information.
March 27, 2003. (b) Which can have serious consequences. Salomon is engaged by WorldCom on its issuance and sale of $2 billion in senior notes, receiving fees of $8,330,600. "Financial Crimes Report to the Public: Fiscal Years 2010-2011." (October 1, 2009- September 30, 2011)." Federal Bureau of Investigation. May 7, 1998b.
059402_01_REF_p365-382.indd 376 McLean, Bethany, and Peter Elkind. Thus, in total, pretax income for 1999 was allegedly overstated by $13.8 million due to overstating ending inventory by not recognizing the full amount of shrinkage. Available online via ProQuest database. Search online for articles published in late 2008 about falling house
prices. Dunlap was recommended for the job as plant manager at Sterling Pulp and Paper, also in Wisconsin. "Public Accountants' Perceptions of Ethical Work Climate: An Exploratory Study of the Difference Between Partners and Employees within the Instrumental Dimension," Open Ethics Journal, Vol. Education and Training. Balance the
consequences against your primary principles or values and select the alternative that best fits. Over a period of time, WorldCom's comparison of sales to PPE produced a strong signal of overstatement of PPE because so much of the misallocation of the line-cost expense went specifically into PPE. Boards of Directors In attempting to address yet
another corporate governance concern, Levitt (2002) focused his attention on both chummy and absentee members of companies' boards of directors. After reading the extracts from AAER 3165, answer the following: 1. In addition, Blockbuster was having enormous difficulty convincing the studios to cooperate because there was not much incentive
in it for them. One 1 Obtained from the website of the Federal Bureau of Investigation. However, the cold weather never arrived and gas prices fell, with the result that on December 12, "The traders lost $550 million according to one report and $630 million according to another report" (McLean & Elkind, 2004, p. No expense needs to be recorded.
When Enron imploded, causing $40 billion in market value to disappear along with the pensions of thousands of people, Fastow fell much further than he had ever risen, becoming the most hated person in America. 10). In 2005, he was convicted of "conspiracy, bank fraud and securities fraud" ("Status of High-Profile ...," 2005). Pridgen, Dee. This
measurements of a corporation, financial performance may remain artificially inflated based on fictitious performance may remain artificially inflated based on fiction are may remain ar
known as "total return swaps" on interests in Enron's merchant assets. Global edition Global edition Global edition Detecting Accounting Fraud Analysis and Ethics Cecil W. This caused a huge cash flow problem for Enron and the company borrowed well over $3 billion in order to keep Enron Online afloat (Bryce, 2002, pp. It was a signal that
companies was going well, in reality, the infighting festered and the unnecessary duplications were nothing short of ludicrous. Flanagan, Jack, and Kevin Clarke. As individual houses in a development were sold, the land inventory accounts were decreased by an amount representing the amounts of the land and development costs allocated to each
individual house. For example, integrity, quality, respect for persons, and profit. June 18-20, 2009. According to the SEC's Complaint, "Countrywide began originating Pay-Option ARMS.'" Although Countrywide had publicly lauded the product,
the SEC's Complaint stated that "several of Countrywide's senior executives, had concluded that the product's risks to the company were severe." (Quotes from SEC Complaint, June 4, 2009, pars. Skrypek helped implement this bill-back scheme. Buca also mischaracterized the invoices of genuine independent contractors as capital expenses. With
gutted production facilities and a demoralized workforce, Dunlap began to pressure his management team to agree to incredibly high target estimates for sales and production. The Extent of Accounting Fraud While there is some debate concerning the extent of corporate fraud, in their study "How Pervasive Is Corporate Fraud?" (2013), Dyck, Morse,
may have believed that the homes that secured the loans could be sold to recover loans of borrowers who defaulted, the size of the impending losses may unwittingly have been underestimated. Then as WorldCom increased its fraudulent transfers from line costs to PPE, revenue as a percentage of PPE dropped precipitously to only 35.6 percent in the
fourth quarter of 2001 and to just 32.2 percent in the first quarter of 2001, Enron had acquired Mariner energy for $185 million and by "the second quarter of 2001, Enron had Mariner energy for $367.4 million" (McLean & Elkind, 2004, p. The 5th U.S. Circuit ruled against the need for a new trial. 97). (Cash flow from operations
things would never get that bad. For the years ended December 31, 2004, 2005, and 2006, Countrywide's allowance for loan losses as a percentage of loans held for investment did not increase in the pay-option ARM loan portfolio segment of the loans held for investment. 6. Assess the
consequences. Tyco International, 179-190 U Unconsolidated affiliates. Gwyn soon began to see another side of Al Dunlap. Number 1470. The scheme to inflate Buca's income involved taking ordinary expenses (which should be expensed in the period in which they are incurred) and 059402 01 ch8 p292-324.indd 318 7/7/14 9:10 AM Chapter 8
Beazer's outside auditor informed certain Beazer officers and employees that any Appreciation Rights represented a "continuing interest" that, pursuant to Generally Accepted Accounting Principles ("GAAP"), required Beazer to record the transactions as financing, not as sale-leasebacks. Blake, Scott. Of course, all the previously mentioned reserves
should only be created if it is probable that the unfavorable future condition actually will come to pass. Rite Aid represents a leading example of overstating earnings via understating cost of goods sold. Jade is the "primary obligor" for the bookkeeper's salary. The bill-back scheme concerned an annual conference for Buca store managers called the
"Paisano Partners Conference." Buca ostensibly funded the Paisano Partners Conference through contributions from its vendors. • Jack Grubman, analyst and crony of Bernie Ebbers, accepted a lifetime ban from the securities industry and paid a $15 million fine" (Guyon, 2005). 059402_01_ch8_p292-324.indd 302 7/7/14 9:10 AM Chapter 8 • Tal
Tales 303 The company was sold to Beatrice Foods in the 1970s, a few years after the original owner died. "Mortgage Stress Seen for '06; 059402_01_REF_p365-382.indd 380 Delinquencies on Subprime Loans Likely to Spike, Report Says," Washington Post. Section 301 of the Sarbanes-Oxley Act 2002 had caused problems rather than providing
solutions for the spread of corporate fraud globally. 059402 01 ch7 p226-291.indd 246 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 247 After leading the charge to exploit the weaknesses in California's energy grid, Timothy Belden played the system for several years, but eventually, he became too clever for his own good
Karen Brown lost the case (Reisinger, 2012). Explain why a bill and hold sale causes cash flow from operations (CFFO) to lag behind operation of Peter Madoff in your answer. Bentham's protégé, John Stuart Mill (1806-1873), defined happiness as the
presence of pleasure and the absence of pain and believed that actions have utility when they
                                                                                                                                   happiness. 29. (Buca 10-K, 2000; pages F-13, F-14) From BUCA's 10-K 2001 NOTES: Note 9 9. 52) In addition to the feeble attempt to provide outside equity of $11.4 million to satisfy the 3 percent rule, the remainder of Chewco's financing came
from another $240 million loan (which Enron guaranteed) from Barclays Bank, as well as a $132 million advance from JEDI itself. Insignia Solutions, PLC. 8). They used the non- consolidation rule to avoid including such SPEs' debt in their balance sheets and to avoid eliminating profit on related-party transactions with these entities. The SEC will
usually accept an "Offer of Settlement," and the respondents agree to the "Order Instituting Public Administrative and Cease and Desist Proceedings." The respondents generally do not admit or deny the findings. In October 1998, Telefonia hired a lobbyist (at $6,500 per month) who was the wife of a Nicaraguan politician who happened to be the
chairman of the telecommunications legislative oversight committee. Pulliam and Solomon (2002) later reported in the Wall Street Journal that Norton's response galvanized Cooper's determination to find out what was going on, and she assembled a team consisting of herself, Gene Morse, and Glyn Smith of the Internal Audit Department. Noonan
Job, 2010, p. Arthur Andersen never did press WorldCom for an explanation of these entries. (c) Understatement of reserves for bad debts. 059402 01 ch3 p069-116.indd 98 Item II: Merchandise costing $3,000 was shipped by Bolt to a retail customer on December 26, using FOB shipping. Because PPE is one of the most common assets chosen for
fraudulent companies to misclassify expenses, a frequently used way to identify this fraud is to check the ratio of sales to PPE. "Enron Trader Admits to Fraud in California Crisis," Wall Street Journal (Eastern edition). So what did Fastow do? (b) The huge loan is treated as a related party transaction in the statement of financial position. The SEC
derived duties. The retrial ended in February 2006, with the jury unable to reach a verdict and the judge declaring another mistrial ("Another Cendant Hung Jury," 2006). CFFO that significantly lags behind operating income or net income. This solution is called . In the 2006 10-K, the allowance for loan losses was stated as $0.261 billion. (c) Enron
disclosed all the names of all of its unconsolidated affiliates as well as the total assets and total debt of each one. Nitec's chairman, George Petty, fired him, declaring that "Dunlap had so completely alienated those around him that Nitec faced the mass resignation of all the company's vice presidents if he weren't let go." At that time, it appeared that
profits had turned around positively, and so Dunlap negotiated a $1.2 million severance package. 99). Enron and WorldCom In an Amended Complaint (May 1, 2003) charging Enron executives with fraud, the Deputy Director of the Enforcement Division of the SEC, Linda Chatman Thomsen, declared: At a point when Enron's touted groundbreaking
broadband technology was little more than a concept—and its business model was not commercially viable—these defendants played important roles in perpetuating the fairy tale that Enron was capable of spinning straw—or more appropriately, fiber—into gold. For example, in absence of special needs, all the students taking a particular class must
fulfill the same requirements. It can be argued that WorldCom's external auditors should not have accepted so many limitations on their access to the complete general ledger at a given time. WorldCom's internal turmoil was so well hidden that in 1998, Sullivan made the cover of CFO Magazine when he was selected for an "Excellence Award'
(McCafferty, 1998). White. "Remarks before the Conference on Listed Companies and Legislators in Dialogue Danish Ministry of Economic and Business Affairs." Speech in Copenhagen, Denmark. 43). In consenting to settlement, Xerox neither admitted nor denied the allegations of the Commission's Complaint." As set out in AAER 2234, April 19,
2005. Hoak, Kimberley. Signal #3: Reduction IN Inventory Reserve as a Percentage of Inventory When the reserve for the obsolescence or shrinkage of inventory by understating its reserve for obsolescence or shrinkage. Before she left Enron,
Mark made a fortune by selling Enron shares. (c) Systematically deceived invest in an asset solely for the reason of selling it at a higher price, the investor would be best rewarded in a leveraged transaction if the price does indeed
                                                costs for shows, such as those for construction of the adoption of the adoption of the high-risk strategy itself also signals that the company is probably in a desperate position. Which of
the following is a signal that a company may be using SPEs to overstate its earnings or understate its debt? But before the failures came the hype, and some of the misinformation. MSNBC.com. May 9, 2012. Did it not occur to them that Fastow had a same of the misinformation.
large interest in getting Enron to guarantee numerous loans for LJM1 in order to acquire substantial amounts of cash that could be used for his own gain? Salomon allocates 100,000 shares to Mr. Ebbers in the MFN IPO. Model adapted by William W. New York: Free Press/Simon & Schuster. Same-store revenue for Krispy Kreme was growing much
more slowly than parentcompany revenue. Buca disclosed in a 2005 restatement that it had improperly capitalized nearly $12 million in expenses from 2000 until 2004, which had the effect of inflating Buca's reported pre-tax income in amounts ranging between 18.8% and 36.9% per year. He was soon dubbed "Dr. Chainsaw" (Porter & Dizik, 2007)
These investments in off-balance-sheet entities were often lost or hidden in the investor's balance sheets as though they were typical investments in unconsolidated affiliates where the investor holds between 20 percent and 50 percent and 50 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent and 50 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments in unconsolidated affiliates where the investor holds between 20 percent are typical investments.
p. For sales-type leases, GAAP requires the financing revenue to be recognized over the of the . c. www.money.cnn.com. The SEC's summary of Rite Aid's overstatement of pretax income is presented in Table 6.1. Signals of the Fictitious Reporting Schemes of Reducing Cost of Goods Sold The three methods of understating cost of goods sold all
produce similar signals. There is not much point in auditing documents if the auditors are not going to reconcile the auditors
Profits." The article questioned whether Dunlap would be able to deliver on Sunbeam's estimates of sales growth. "Lucas is in the bathroom," Eva tells the managing particular expense line items" (AAER 1275, 2000).8 An Overview of CUC's
period from the second quarter of 059402_01_ch8_p292-324.indd 304 7/7/14 9:10 AM Chapter 8 • Tall Tales 305 2003 to the second quarter of 2004, Krispy Kreme reported an increase in company revenues of almost 15 percent, while same-store sales increased by less than 1 percent. (2) The ratio of the amount of all loans secured by the property
to the lower of the original appraised value or purchase price of the property. The Adelphia Account3 Adelphia Communications Corporation is presented mainly as an example of: • Failure to Disclose Related-Party Transactions and Improper Use of Related-Party Transactions. The stock price did not rise. For this information, once again we simply
elevated capital ratios. 39. He started with the unfortunate James Clegg, the chief operating officer, who had expected to get Dunlap's job. The SOX Act also prohibits public accounting firms from performing specified non-audit services for the firms that they audit. "Broadband Trial: The Outcome," CBS News. Calculate the sales/total assets ratio for
quarters 1-4. This pressure created an environment in which reporting numbers that met these expectations, no matter how these numbers were derived, apparently became more important than accurate financial reporting (First Interim Report, 2002, p. Key Terms Bill and hold sales 81 Cash flow from operations (CFFO) 88 Channel stuffing 83
Common or allocated fixed costs 76 Cookie-jar reserves 82 Downsizing 70 FOB destination 81 Traceable fixed costs 76 Ethics at Work Questions: a. ("High Wire"), a small information technology company that
engaged in a series of transactions involving Buca between 2000 and 2001. This management agreement terminated during 1999. (c) Change in the estimates of the residual values. The number of shares issued depends on the market value of the stock at the date of the stock at the date of the share issue. WorldCom overstated its sales by holding its books open at the close of the residual values.
of a reporting period. MCI recruited William (Bill) McGowan, a Harvard law alumnus, to help raise money and fight for the fledgling company. Weiss, University of Northwestern Ohio. Buca terminated Skrypek's employment in May 2005. 19. Innovation like no other. Right actions correspond to the moral law, and according to Kant, these actions are
universally discernible and universally applicable by our ability to reason. Wall Street analysts began to search for the telltale signs of fraud: growing accounts receivable and mounting inventory. It is quite another matter if you have a contract to sell gas for the next 23 years and
there are no market prices to indicate what you will have to pay for the gas you intend to sell in 23 years' time. The trouble was that Enron had not yet worked out the technical details to solve the "last mile problem—getting the content from Enron's network into people's homes" (McLean & Elkind, 2004, p. Skilling had invented a futures market in
natural gas! (A futures market is an exchange where parties can trade future date.) Soon, companies on Wall Street followed Skilling's lead, and in 1990, the New York Mercantile Exchange began trading gas
futures. • Andrew Fastow, former CFO of Enron, "pleaded guilty in January 2004 to two counts of conspiracy, admitting to orchestrate schemes to hide the company's debt and inflate profits while pocketing millions of dollars" ("Status of High-Profiles Corporate Scandals," 2005). Michaelson (2009), a vice president at Countrywide from 2003-2006
wrote of the high standards instilled in the Countrywide workforce during his early days at the company: With a precision and a professionalism I had not seen since the Air Force, the mechanisms of Countrywide processes, procedures, checking and rechecking, and attention to perfect, verifiable detail had to be on a par with or exceeding that of
NASA. Ebbers was a walking mass of contradictions: devoutly religious and a generous donor, yet bad-tempered and penny-pinching. Al Dunlap and Judy appeared to be very well matched. An Overview of Xerox's Fictitious Financial Reporting Schemes The SEC found that Xerox accelerated recognition of its equipment revenue by more than $3 billion
over the period 1997 through 2000 and "increased pre-tax earnings by $1.5 billion." The SEC findings also alleged that "KPMG's failure to comply with 3 "Pursuant to a consent to settlement by Xerox, the company also was assessed a civil penalty of $10 million. is a mortgage lender. The Examiner, however, rejected the argument on the grounds
that Ebbers had not traded at all on his SSB account, except for his IPO shares. January 2011. The game was up for Enron once the banks refused to continue extending credit to the company either directly or indirectly through its SPEs. To understand what went wrong with this behemoth company and why it went so wrong, it is necessary to take a
closer look at the following phases in the rise and fall of Enron: • Enron's energy-trading business (ECT). Allegheny (AHERF): Trick or Treatment? In exchange, Enron received the put option (from Swap Sub) valued at approximately $104 million, in addition to a note for $64 million. (a) Bad debt reserves. The overt acts in the conspiracy count also
include, among other things, making false statements to investors about BLMIS's compliance program and the nature and scope of its Investment Advisory business. The third consideration, in my view, is that this process for addressing conflicts of interest is fully integrated in the firm's overall risk governance structure. 62. What are the ethical
issues? Troubh and Herbert S. Deloitte & Touche denied any wrongdoing. Cohn, Scott. As jet travel boomed in the 1960s, there was such a demand by the airlines for larger wide-bodied jets to carry more passengers that two large airline manufacturing companies, McDonnell Douglas and Lockheed, pursued plans to design similar aircraft with similar
common stock to third parties, and reducing the fair value by the Company's ownership interest in Empire. March 20, 2004. in "Krispy Kreme COO Tate Leaving the fair value by the Company's ownership interest in Empire. March 20, 2004. in "Krispy Kreme COO Tate Leaving the fair value by the Company's ownership interest in Empire. March 20, 2004. in "Krispy Kreme COO Tate Leaving the fair value by the Company's ownership interest in Empire. March 20, 2004. in "Krispy Kreme COO Tate Leaving the fair value by the Company's ownership interest in Empire. March 20, 2004. in "Krispy Kreme COO Tate Leaving the fair value by the Company's ownership interest in Empire. March 20, 2004. in "Krispy Kreme COO Tate Leaving the fair value by the Company is allowed to recognize a profit in its financial statements in respect of the increase in the price of its own shares. Gadel and Skrypek
helped prepare and review financial statements * "Upon the filing of the Commission's complaint, and without admitting or denying the allegations in the complaint, Micatrotto consented to the entry of a final judgment ...." (LR 19719, 2006). The failed checks and balances listed by Richard Thornburgh, WorldCom's Bankruptcy Examiner, in his First
Barney (SSB) • The chief investment banker and analyst Jack Grubman • Members of WorldCom's senior accounting manipulations of employees, customers, corporate investors, and private individuals were hoodwinked by accounting manipulations of employees, customers, corporate investors, and private individuals were hoodwinked by accounting staff For many years, thousands of employees, customers, corporate investors, and private individuals were hoodwinked by accounting manipulations of massive proportions. So he talks about his experiences as a lesson to others not to
let themselves get caught up in a cascade of events with such a high personal and professional cost. If Mac goes ahead and recognizes a sale of $15,000 in its December 31 financial statements, which of the following is correct? Clearly, many auditors could not take the increased pressure from management who stood to gain significantly from
million dream house he was building in the exclusive Le Lac enclave west of the city. Since new conflicts of interest can arise rapidly as a business grows and evolves, and may become apparent to front-line employees before they come to the attention of more senior managers or control functions, communications about these standards and
procedures are also an opportunity to emphasize to all employees the importance of their role in recognizing new conflicts to appropriate control functions. • An ongoing project was launched to integrate U.S. generally accepted accounting principles (GAAP) with international financial
reporting standards (IFRS). "Downsizing or Dumbsizing?" An article in BYU Magazine titled "Downsizing or Dumbsizing?" succinctly captured the perils of these unintended consequences. (d) The transactions overstated expenses in the income statement. The value of the house is the security for the loan if the borrower becomes unable to pay the
loan. Suddenly, in 1999, CFFO turned around dramatically, to positive $1,224 million, compared to net income of $1,424 million—a ratio of 86 percent. We can say this based on which of the following? Bankers got the blame. However, whereas legitimate sales will be paid relatively soon by the customers and will turn into cash, the next period's sales
will probably only be paid next period and will remain on the balance sheet in the current period as accounts receivable instead of turning into cash. Under GAAP, a company could recognize rebates only when they were actually earned, i.e., when the entity had substantially accomplished what was necessary to be entitled to such rebates
www.sec.gov 059402 01 ch4 p117-143.indd 136 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 137 Litigation Release for Peregrine Systems, Inc. Initially, Morse downloaded so much data that he almost shut down the entire system. It was not surprising that his business focus became a little distracted. In the course of discussing these two topics, I
would like to explore with you the following propositions: 1. The investee's financial statements are consolidated into the investor's group financial statements. in Finnis, 1983, p. April 27, 2005. Bankruptcy Report of Anton R. Ace should not recognize a sale in respect of the investor's selling price. Merrill Lynch was still independent, AIG was still independent, AIG was still independent.
 solvent, and Lehman Brothers was still trading. Improper Deferral of Expenses or Losses and Overstatement of Assets LIVENT 8. At the beginning of 2002, an article in Business Week confirmed that consulting is clear.... However, when
firm omits recording its expenses and liabilities, it often also understates expenses or movement of expenses or movement of expenses from the financial statements in the period in which they should be recorded to an earlier or later
period.) Livent is also presented as a good example of the scheme of improperly deferring expenses via transferring costs from their correct accounts to delay amortization. "Ethics without the Sermon." Harvard Business Review Classics Series. 1. "Tapes Bolster Electricity Claims," Los Angeles Times, C1. Aggressive accounting
policies in terms of capitalization of expenses compared to previous periods or compared to other companies in the same industry, for items such as capitalized interest costs, development costs, or direct response advertising costs. (c) Gain on revaluation of an asset. 7). 059402 01 REF p365-382.indd 372 Pulliam, Susan. T F 7. (c)
Understatement of its cash flow from financing activities. "David Loeb, 79; Founded Mortgage Banking Firms," Los Angeles Times. Signals of Sunbeam may have engaged in fictitious financial reporting. It also contains answers to all the True/False, Fill-in-the-Blank, and Multiple Choice
Questions in each chapter. It is also critical that users of financial statements learn to identify the major methods that company's financial statements may have been falsified. Skrypek. Furthermore, if the makeup of current liabilities is given in a note, it is
important to check whether the accruals for the individual current liabilities decrease as a percentage of sales compared to previous periods.] [Hint 2: You must isolate the Product Warranty section of the Product Warranty
public by shedding light on opaque exposures and assisting in developing more robust price discovery mechanisms. Further, Fastow decided that Enron now had a market price for the Cuiába/EPE back to Enron itself. Nevertheless, the dollar amounts that were deferred instead of being expensed are
considered material for each of the first three guarters of fiscal year 2002. The disclosure may be the tip of the iceberg because it could become very tempting for officers or shareholders to use the company as its own money machine. LR 20417. Equality,
                                                                                                                                                                                                                                                                                                                                        , merit, contribution, and effort are the principles of distributive justice, according to
philosopher Joel Feinberg. With the jobs of the two men on the line, Peter Langerman, one of the directors, read to them from a prepared statement: Here is what we propose: 1. They thought they had the golden goose, and the golden goose just stole a little money out of their petty cash" (qtd. Which of the following attributes of loans is not an
indication of an increased risk of repayment default? Smythe, Christie. Signal #4: Sales of Accounts Receivable—or any future revenue stream—should alert the reader to test for all signals of accelerating revenue recognition.
May 25, 2006. Determine if there is one principle or value, or combination, which is so compelling that the proper alternative is clear—for example, correcting a defect that is almost certain to cause loss of life. Furthermore, he could buy and sell Enron's assets via LIM1. "Ebbers' Wife Files for Divorce." April 24, 2008, www.post-gazette.com. Senior
executives became too eager in their quest to deliver earnings and revenue figures that met analysts' high growth expectations in every single quarter. 059402 01 ch8 p292-324.indd 294 7/7/14 9:10 AM Chapter 8 • Tall Tales 295 The issue was that Edison's financial statements did not accurately and completely "describe the realities of Edison's
operations" (AAER 1555, 2002). "You're going to find yourself in a position where you're incented to do things really close to the line," Shreve told students. 7/7/14 9:15 AM References 367 "The Sarbanes-Oxley Act at 10: Enhancing the Reliability of Financial Reporting and Audit Quality." 2012. The company was desperate to keep this guiet because
Uzzi had been carrying an enormous load in trying to keep Sunbeam's sales from falling apart altogether. Because of the increased risks involved, investors usually demand a higher earnings-yield percentage for a trading company than for a hard-asset operating company. Since 059402 01 ch8 p292-324.indd 320 7/7/14 9:10 AM Chapter 8 • Tall
Tales 321 Buca was in the process of acquiring another restaurant chain at this time, Buca capitalized the assistant controller's salary payments as part of the acquisition. Sullivan pleaded guilty to three fraud-related counts. Leasing companies discount future cash flows when they recognize the amounts in current income. Enron would buy and sell of the acquisition are the acquiring another restaurant chain at this time, Buca capitalized the acquisition. Sullivan pleaded guilty to three fraud-related counts.
capacity on the Internet so that corporations and other carriers could get reliable network connections." However, there was a huge problem in that the technology necessary for Skilling's plan to work did not yet exist: "No one had built equipment that could provide instant bandwidth on demand." Furthermore, while Enron was spending a fortune on
these highly dubious plans, it had yet to find any customers. Martin, Dan. (b) The reserve for bad debts decreases as a percentage of accounts receivable. Fourth, MacIntyre identified a "Jane Austen" view of the virtues, which included elements of the three approaches discussed previously and included a "real affection for people" as a virtue.
www.modernhealthcare.com. To assist the instructor in guiding student discussions on ethical issues, the manual presents a range of comprehensive responses to all the questions. Key Terms Arm's-length transaction 299 Management Discussion and Analysis (MD&A) 293 059402 01 ch8 p292-324.indd 306 Non-GAAP
financial measures 298 Primary obligor 294 Related-party transactions 304 7/7/14 9:10 AM Chapter 8 • Tall Tales 307 ETHICS AT WORK Read the extract below from the speech on "Conflicts of Interest and Risk Governance" (2012) by Carlo di Florio, the director of the SEC's Office of
Compliance Inspections and Examinations, then respond to the question. Also, even before Livent was a listed company in the United States, the SEC alleged that Drabinsky and Gottlieb engineered a kickback scheme in which the two got outside individuals to inflate invoice amounts to Livent, which Livent paid and for which approximately $7 million
was kicked back to Drabinsky and Gottlieb between 1990 and 1994 (AAER 1095, 1999). Further, according to the SEC Complaint, "Several sales did not occur in the quarter for which revenue was recognized" (par. In May, Sidgmore, the new CEO, appointed Cooper to head a complete investigation into WorldCom's books. According to McLean and
Elkind (2004), "The Fastows' total secret take, just from this one partnership, ultimately reached a staggering $25.1 million" (p. These estimates are established using historical information about the nature, frequency and average cost of warranty claims. 7/7/14 9:02 AM Chapter 4 • Hocus Pocus Exercises 38. 290). (c) Improper valuation of
revenue. • Students are given the opportunity to examine the ethical dimensions (or lack thereof) of a variety of the case studies. (b) Choose a known vendor and trace the vendor to the list of accounts payable that supports the amount listed on the balance sheet. "Accounting for Special Purpose Entities Revised: FASB Interpretation 46(R)," CPA
                                          issued the first MBSs in the United States when it sold s ecurities backed by its FHA and VA loans. The FASB is working closely with the International Accounting Standards Board (IASB) to issue a new principles-based converged revenue recognition statement. Many of these lenders followed an evolution that began
with making safe, conforming loans to GSEs and then expanding 3 General background information in this section is from The Financial Crisis Inquiry Report, 2011; Friends of Angelo, 2009; McLean & Nocera, 2010; Michaelson, 2009; SEC Complaint June 4, 2009; SEC Complaint Dec. • Lack of transparency. The FASB tentatively requires that the
new standard will be effective "for annual reporting periods beginning after December 15, 2016," for public companies (Revenue Recognition Project, 2013, p. The customers can actually smell the sweet aroma and hear the hot sizzle of doughnuts being cooked to perfection. One of the most contentious parts of the SOX legislation was Section, which
addressed internal controls. (gtd. "More Bad News for Lender," Orange County Register. Of course, if a company takes on a large debt and uses that capital to earn profit at a rate of return that is much higher than the interest rate, it will be a very profitable company. The company is known worldwide, and its name has become synonymous with "-
photocopying." In the period from 1997 to 2000, Xerox paid its auditors (KPMG) the sum of "$55.8 million for auditing [its] financial statements" (AAER 2234, 2005). 059402 01 ch7 p226-291.indd 273 7/7/14 9:08 AM 274 Chapter 7 • Enron and the Tale of the Golden Goose in our targets.... So three years from now, we expect our network to be
1,000 times the size it is today. If a senior executive of a company was previously employed by the company's audit, the audit firm is prohibited from auditing that company for a period of one year. Also read the extracts from Buca's relatedparty transactions notes to its financial statements for years 2000-2002.
Toward the end of the 1990s, some countries had begun the slow process of privatizing their water utilities and wastewater facilities. Portfolio's Worst American CEOs of All Time. Conversely, the Company was prohibited from U.S. Securities
and Exchange Commission. The next decade saw dramatic changes in the mortgage industry: "Subprime loans ... increased from $35 billion in 1994 to $160 billion in 1999, accounting for 12.5% of all residential mortgages. Signal #3: Decrease in Allowance for Returns |
significant decrease in allowances for returns as a percentage of sales is a signal that the allowance for returns may be understated. The audit committee of WorldCom's board of directors was scrutinized for its lax supervision of accounting issues. For several years, three things kept Enron going—and growing—throughout its reckless and convoluted
projects: 1. 21. 059402 01 ch4 p117-143.indd 133 133 7/7/14 9:02 AM 134 Chapter 4 • Hocus Pocus (c) In 1999, the company's CFFO dramatically changed to a positive figure of $1,224 million. Goeken had sold two-way radios for truckers to stay in touch with dispatchers and, of course, to "rap" with
each other. They formed a bond and sometimes drank beer and shot pool together. When R&Q's CPU calculation was presented to Stanaway, and then ultimately to McIntosh, both typically stated that the initial estimated reserve number was too high for the Engine Division's business plan. (c) The risks of ownership must have passed to the buyer.
With the goal of homeownership being an intrinsic part of the American mentality, government policy did not end at this level of providing capital for home 059402 01 ch9 p325-360.indd 327 7/7/14 9:11 AM 328 Chapter 9 • Mortgage Mayhem loans or of separating ownership of the loans from the origination of the loans. (b) Inadequate disclosures
in its Management Discussion and Analysis (MD&A). In addition, Empire agreed to purchase one water treatment system from the Company concurrent with the December 2007 closing for a total price of $900. (b) To overstate the property, plant, and equipment. Signal #3: Late Publication of Financial Statements When a company is late in
publishing its balance sheet and statement of cash flows, it is a signal that the company may be taking time to manipulate these statements because it has something to hide. 7/7/14 9:02 AM 136 Chapter 4 • Hocus Pocus 1. Thus, a key consideration under GAAP regarding the existence and magnitude of losses for impaired loans or OREO is the fair
value of the collateral or OREO property. Discount rates, 123-124 Discounts, 93-94 Dispositions, 49, 52 Distributive justice, 57-58 Dodd-Frank Whistleblower Program, 30, 40-41 Downs, Alan, 78 Downsizing, 70, 74-76, 78, 85-86 A reduction in the size of a company by reducing the number of product lines, factories,
offices, and/or personnel. Moreover, the Company often did not receive reimbursements from vendors for engine warranty claims. U.S. Securities and Exchange Commission Complaint against Adelphia Communications Corp., John Rigas, Timothy Rigas, Michael Rigas, James Brown, and Michael Mulcahey. 059402 01 ch9 p325-360.indd
356 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 357 61. The first was its improper use of acquisition or merger reserves, and the second was the capitalizing of its line-cost expense. • Identify the signals in financial statements that could alert you to the possibility that a company may be overstating its revenues. 107). The Securities and
Exchange Commission ("Commission") deems it appropriate that cease-and-desist proceedings be, and hereby are, instituted pursuant to Section 8A of the Securities Act of 1933 ("Securities Act") against Beazer Homes USA, Inc. Second, some of the "sold" receivables were not
valid because the customers were not obligated to pay Peregrine. Enron dominated the market and "was the dominant company when it came to setting prices as well" (Swartz & Watkins, 2003, p. The times-interest-earned ratio remained between 2.5 and 2.6 over the period. (June 4, 2009, par. However, in April 1998, Citicorp, a commercial bank,
merged with Travelers Insurance, which owned Smith 059402 01 ch9 p325-360.indd 329 7/7/14 9:11 AM 330 Chapter 9 • Mortgage Mayhem Barney, an investment bank. The Street.com. Specifically, the Company deferred $4.3 million in the fourth quarter of fiscal year 2002, and $13.3 million in the fourth quarter of fiscal year 2001, $12.8 million in the fourth quarter of fiscal year 2001, $12.8 million in the first quarter of fiscal year 2002, and $13.3 million in the fourth quarter of fiscal year 2001, $12.8 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2001, $12.8 million in the fourth quarter of fiscal year 2001, $12.8 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2001, $12.8 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2001, $12.8 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2001, $12.8 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3 million in the first quarter of fiscal year 2002, and $13.3
each of the second and third quarters of fiscal year 2002.* 43. Without such a written guarantee, the Company was not entitled to defer these costs. (Today it stands as the third-largest bankruptcy in the United States, having been overtaken by Lehman Brothers—which holds the top spot—and Washington Mutual.) The Gatekeepers Who Failed
WorldCom Over the years, the capitalization of expenses and manipulation of reserves had overstated WorldCom's profits by more than $9 billion: The Commission's Amended Complaint alleges that WorldCom misled investors from at least as early as 1999 through the first guarter of 2002, and further states that the company has acknowledged that
during that period, as a result of undisclosed and improper accounting, WorldCom materially overstated the income it reported on its financial statements by approximately $9 billion. Two ways in which Enron used SPEs to overstate earnings were the abuse of markto-market accounting and contrived related party sales. When a home sale was
recorded in Beazer's general ledger, all associated homebuilding costs, including the costs of the land inventory account, were expensed to cost of sales. The promise of lucrative investment banking work may have been the driving force behind an upgrade of a company's stock, and signals that the financial statements might be
fraudulently prepared may have been ignored ... for a fee. (a) Item I's and Item II's inventory should both be included in Bolt's December 31 inventory. 35. In 1938, toward the end of the Great Depression, the Federal National Mortgage Association—or "Fanny Mae"—was established in order to buy up mortgages that were guaranteed by the Federal
Housing Administration. "Procedures for the Handling of Retaliation Complaints Under Section 806 of the Sarbanes-Oxley Act of 2002, as Amended." November 3, 2011. (Perelman had acquired a significant amount of Sunbeam stock on the sale of his company, Coleman, to Sunbeam.) Levin agreed to the request and began by rehiring executives who
had quit under Dunlap. Fundamentals of Ethics. The Report also pointed out that in 2007, Goldman's demand for AIG executives who believed that payments would be required only in the event of actual losses. One must search the notes to the
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financial statements for indications of troubled loans. This was perhaps why he ensured that the trails to the ownership and financing of his SPEs were as complicated and convoluted as possible. These were sales to customers where 2 Sunbeam consented to the entry of the order without admitting or denying the findings or conclusions of law as set

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out in AAER 1393, May 15, 2001. This is the view that morality possesses no universal appeal and is not tethered to any truth claims; right action and the good are wholly dependent on, and relative to, the situation, actors, culture, group, or time period. Brody, University of New Mexico; Jim Cali, Southern Illinois University - Carbondale; Judith M. It
is difficult to second-guess which of these should have gone, if any. To test for an indication of a fictitious receivable, one should normally be paid to the company later—back to the receivables (accounts receivable or, in Enron's
case, "assets from price risk management activities") before calculating the retion of the receivables-to-sales. Which of the following is not true regarding disclosure by Enron in its financial statements? Stanaway, who had no direct role in acquiring the rebate, then approved an entry recording the $6.2 million as income in 2003. Signal #1: Increase in
Accounts Receivable as a Percentage of Sales Once again, accounts receivable as a percentage of sales as captured in such measures as DSO is a leading signal of this fraud. Scheme #1: Overstating Ending Inventory Values to Reduce Cost of Goods Sold One of the three most significant methods that Rite Aid used to understate its cost of goods sold
 amount was that it overstated its ending inventory by failing to write down its inventory amount for the full amount of the shrinkage that it suffered. Instead, the company's accounts receivable increase. 5-8) Over the next few days, Dunlap fired five more executives. Case Study NAVISTAR INTERNATIONAL CORPORATION • Read the extracts from
AAER 3165, August 5, 2010. Although not actively involved in the schemes, he was nevertheless accused of neglecting to report the Rite Aid fraud. According to a recent Cornerstone Research article, "In 2012, the proportion of securities class action settlements involving accounting allegations increased to almost 70 percent from less than 50
percent in 2011" (qtd. November 17, 2005. Feinberg, Joel. (c) The packing case should be included in Ace's December 31 inventory. • Sensormatic was acquired by Tyco Inc. As consequentialist philosophy has developed over the years, different philosophy has developed over the years of th
unifying thread is that all consequentialists judge actions according to the sum of the net good that they cause among all those affected by the actions. September 4, 2002. Myers pleaded guilty and agreed to assist prosecutors with the case. January 17, 2006. March 1, 2005. • Increasing investor protection by enhancing security-based swap
transaction disclosure, mitigating conflicts of interest, and improving our ability to police these markets. • Martin Grass, former CEO of Rite Aid, pleaded guilty to a conspiracy charge, and in May 2004, Judge Sylvia Rambo sentenced him to eight years of imprisonment ("8-Year Sentence," 2004), but later reduced his term to seven years. Assistant
United States Attorneys Lisa A. www.jarden.com. Lavelle, Marianne. As contingent consideration for paying these rebates, however, many suppliers required the Company either to agree to new business or to repay the amount of the rebate in the form of waived price concessions on already-agreed upon future business. These companies typically
create reserves (by initially over-accruing a liability) in one accounting period and then reduce the excess reserves in later accounting periods. For example, it had not been well maintained. It's over." In his description of the scene, Byrne wrote: "Glaring
fiercely, Dunlap kept repeating the phrase, again and again, saliva spitting from his lips. 273. However, a focus on external rules, regulations, and laws, without any authentic understanding of the essential nature of ethics and morality, could prove to be ineffective. In addition, the SEC concluded that Lehman had not contravened GAAP. Kimberly-
Clark took a $1.4 billion restructuring charge in respect of its integration of Scott Paper. In fact, by the summer of 2007 (shortly before the mortgage bubble burst), "Mozilo was the market" (Muolo & Padilla, 2010, p. 059402_01_ch7_p226-291.indd 233 7/7/14 9:08 AM 234 Chapter 7 • Enron and the Tale of the Golden Goose Around this time, Enron
Finance, Skilling's Enron division, merged with Enron Gas Marketing, and the segment was renamed Enron Capital and Trade (ECT) Resources. During the relevant time period, Gadel was a director of High Wire and had a 10% equity interest in the company. Earnings in 1997 would be overstated by this amount when inventory was sold. Take on the
Street. The Sale-Leaseback Transactions 13. "Number of Cases Filed by SEC Slows," Wall Street Journal. 77) From Nitec, Dunlap eventually found a middle-management job at American Can, where he rose to become head of the plastics division. These restatements resulted "in a cumulative adverse effect on net income in excess of $98 million
(Cdn.)" (AAER 1095, 1999). March 17, 2013. "SEC Receives More Than 3,000 Whistleblower Tips in FY2012." November 15, 2012. One day later the SEC delivered a "Request for Information" concerning its investigation into WorldCom. K. Financial service firms usually have a ready market price to refer to in order to establish the value of the
financial instruments that they own and can readily sell. Many Krispy Kreme devotees were upset by the sale, and several of the franchisees grouped together to repurchase the company in 1982. 7/7/14 9:15 AM References 381 Hurtado, Patricia. Fraud at a Wisconsin foundry and in connection with certain vendor rebates and vendor tooling
transactions accounted for approximately $58 million of that total. 7/7/14 9:15 AM References 379 Johnson, Sarah. Selling Adelphia's Excess Digital Converters to a Rigas Entity Adelphia had purchased an excess inventory of digital converters. The two signals listed below may apply to any method of overstating sales. Detecting Accounting Fraud
Analysis and Ethics For these Global Editions, the editorial team at Pearson has collaborated with educators across the world to address a wide range of subjects and requirements, equipping students with the best possible learning tools. 2005. In Business Ethics: A Philosophical Reader. Mark's Enron career was finally undone by her plan to start a
 water utilities company—a sector in which she and Enron had absolutely no experience. Par. 4) Easy Credit: Securitization The housing boom, like most booms, was fueled by easy credit. The hidden problem at the heart of this accounting fantasy was that Enron secretly had to guarantee the SPE's debt in order for the SPE to get the loans. March 3,
2006. common or allocated, 76 traceable, 76 Fleming, John E., 53 FOB destination, 81, 120 A sales agreement term specifying that ownership passes to the 7/7/14 9:17 AM Glindex 391 customer only when the purchased goods arrive at their destination. Lay moved to Houston with his secretary, Linda Phillips, whom he then married after divorcing
his first wife. In 2007, an appeals court in Florida reversed the jury verdict against Morgan Stanley (Thomas, Jr., 2007). "Manipulation of California Energy Market Gives Consumers a Jolt." Los Angeles Times. Pursuant to Public Law 111-21. To the consequentialist, the most important issue in morality is to choose the right action, and this choice is
determined by examining the consequences of that action. "Ex-Rite Aid GC Loses Yet Another Case." Corporate Council. F 9. May 2013. The SEC Complaint (June 4, 2009) described up Countrywide's reported production of conventional conforming loans dropped to 38.2%, its production of
subprime loans had risen to 11%, its production of home equity loans had risen to 38.7%. EdisonLearning, 295 Edison Schools, Inc., 293-295 80/20 subprime loans, 336-337 Einstein, Albert, 48 EITF (Emerging Issues Task Force), 265 Electricity deregulation, 244-247
Electricity trading, by Enron, 236 Emerging Issue Task Force (EITF), 265 Employees, 54 England, Azurix water project in, 238-239 Enron, 30-32, 248, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 234, 243, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 234, 243, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 234, 243, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 234, 243, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 234, 243, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 234, 243, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 234, 243, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 234, 245, 250, 252, 254-263, 265-272, 276 accounts receivable as percentage of revenue, 273t Andrew Fastow and, 275t Andrew 
electricity fiasco, 244-247 cash flow from operations, 273t debt-to-equity ratio of, 275, 276t fictitious financial reporting schemes, 247-264 Gas Bank, 231-232 Jeffrey Skilling and, 231-232 Jeffrey Skilling and, 231-232 Jeffrey Skilling and, 231-235, 238, 239, 242, 246, 256, 274, 277, 278 Kenneth Lay and, 227-231, 243, 278 losses sustained by, 236-244 mark-to-market accounting, 232-234, 235, 247-248,
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234, 235-236 Enron Development, 236-237 Enron Energy Services (EES), 239-240 Enron International, 238 Enron Online, 240-241 Equality, 57 Equity accounting method in which the investment is increased or decreased
by a corresponding amount on the balance sheet. p. The researchers found that every reference to Internet traffic doubling every 100 days led back to Sidgmore and Ebbers at WorldCom. 059402 01 ch9 p325-360.indd 343 7/7/14 9:11 AM 344 Chapter 9 • Mortgage Mayhem Signal #2: Allowance for Loan Losses Not Growing in Proportion to the
 Increase in Troubled Loans When the allowance for loan losses may be understated. Notes receivable, 289-290 NYSE (New York Stock Exchange), 35 O Obama, Barack, 39 Occupational Safety and Health Administration (OSHA), 40, 41n
Odlyzko, Andrew, 151 Off-balance-sheet entities, 249, 266, 271 See also Special purpose entities (SPEs) O'Hara, Paul, 77 One-time charges, 95, 170 Operational problems, 304-305 Osprey Trust, 259, 261-263 Outside directors, 32-33 Overseas Private Investment Corporation (OPIC)
237 Overstated earnings, 84-85, 94-95 by Enron, 235, 265-272 signals of, 265-272 by Sunbeam, 94-95 7/7/14 9:17 AM 396 Glindex by WorldCom, 158-162, 166, 169-170 by Xerox, 124-125 Ovitz, Michael, 192 Oxley, Michael, 34 P Pai, Lou, 234, 240 Pardue, Michael, 118, 119, 122 Patent costs, 290 Pay-option ARM loan, 337, 340-342, 346-347 An
 adjustable-rate mortgage loan that allowed for a variety of payment options. It generally refers to the increase or decrease in the actual amount of cash in a period as a result of sales or services rendered or the performance of some other operating activities and the related expenses. Investment bankers and AIG, as well as the monoline insurers (i.e.,
insurance companies that insure against only one type of risk), wrote CDSs that "guaranteed" to pay the holders of the swaps in the event of default. Lehman Brothers Holdings Inc. www.usnews.com/usnews/biztech/ articles/050425/25eewhere.htm. Shortly thereafter, five of the executives resigned and one retired. If necessary, the company would
understate line costs down to the constant amount of close to 41 percent of sales revenue each quarter. Neal. 059402 01 ch3 p069-116.indd 80 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 81 the sales agreements even
provided that, if returned, Sunbeam would pay for shipping and storage costs. under the tutelage of two Indian government-owned firms" (Bajaj, 2010). 254). The new appraisals revealed the actual values of TierOne's collateral for impaired loans and OREO. Sunbeam's cash flow from operations (CFFO) was negative, but at the same time the
company was operating at a great profit, which signaled of inappropriately recorded. July 9, 2004. Action Co. has agreed to pay $45,000 to acquire 100 percent of the shares of Sub Co. Action Co. believes that the fair value of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. Action Co. believes that the fair value of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acquire 100 percent of the shares of Sub Co. acqui
$ 60,000.00 Action Co. believes that based on Sub Co.'s future earnings potential, it is prepared to pay $5,000 more for Sub Co. than its net asset value. Aerial estimates that it will need to sell 100 airplanes to break even on this line of aircraft. In its haste to put the deal together, Azurix had ignored
some significant information. One can browse through a company's accounting policy note to look for such evidence. Insignia's understatement of its allowance for returns is an example of improper valuation of revenue. The complaint further alleges that, from September 1996 through early 2002, Tyco failed to disclose in its proxy statements and
annual reports certain executive compensation, executive indebtedness, and related party transactions of its former senior management. Why did these checks and balances fail? By 2003, subprime lending was at $330 billion and going strong" (Pridgen, 2005). "3 Admit Guilt in Falsifying CUC's Books." New York Times. Scott Sullivan was a brilliant
quiet, reserved, and conservative young CPA who had previously audited for one of the Big Eight audit firms. GAAP permits the impairment to be measured using the fair value of the underlying collateral dependent, which is the method that was typically utilized by TierOne. In April 1999, the company went public and the stock
 jumped to $21 per share, and by May 1999, Enron's investment was worth almost $300 million. www.ftc.gov. In year 1, Rhodes Co.'s first year of operating the school, the school earned per pupil fees of $100,000. (continued) 059402 01 APP p361-364.indd 362 7/7/14 9:13 AM Appendix 363 The Top Twenty-Five Signals The Schemes That a Company
May Be Concealing 21. In the absence of clearly understandable explanations in the Management Discussion and Analysis (MD&A) section of the company's annual report or in coherent press releases, 059402 01 ch5 p144-190.indd 171 7/7/14 9:04 AM 172 Chapter 5 • WorldCom Wizardry: From WorldCom Table 5.4 WorldCom:
292 292 292 1,063 902 1,035 1,223 1,089 419 352 403 Improperly Capitalized Line Costs Less Tax Shield 119 117 197 474 390 Total Assets 97,373 99,893 98,903 99,580 101,944 104,902 103,914 103,803 Goodwill 46,670 46,594 46,113 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 50,820 5
7,204 7,770 8,241 9,061 9,852 10,807 Accumulated Depreciation *Obtained from U.S. Securities and Exchange Commission. Case Study BUCA, Inc. T F F 7/7/14 9:02 AM Chapter 4 • Hocus Pocus Fill-in-the-Blank Questions Multiple-Choice Questions Fill in the blanks with information and concepts from this chapter. Later, this would be to the
chagrin of those debtholders. (c) Understatement of reserve for bad debts. "Cutting-Edge Company Becomes a Cautionary Tale," Orange County Register. In 2000 and 2001, Gadel was a director and 10% shareholder of a small information technology company that engaged in a series of transactions involving Buca that totaled more than $1 million
Then for 1998, the company actually generated a negative CFFO of $1,165 million compared to positive reported net income of $395 million. JEDI Limited Partnership MM LP 5K 1 $1 GP 1.4 $1 $240 MM Loan Chewco Investments L.P. Note M 3 De ra m er M $3 8 Barclays Note tee $132 MM Advance 059402 01 ch7 p226-291.indd 253 G e en Li
William Dodson (replaced Michael Kopper) Barclays Big River and Little River Reserve Accounts Michael Kopper (96.5%) William Dodson (2.5%) William (2.5%) Willi
LJM Partners, LLC Andrew Fastow General Partner LjM SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Andrew Fastow Sole Director LJM SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM1) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM2) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM2) Limited Partner Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM2) Ljm SwapCo Campsie ERNB LJM Cayman, L.P. (LJM3) Ljm SwapCo Campsie ERNB LJM Cayman, LJM Cayman
prison, with his sentence commencing in November 2005 ("Sullivan Gets Five Years ...," 2005). 059402 01 ch6 p191-225.indd 221 7/7/14 9:06 AM 222 Chapter 6 • Abracadabra Navistar International Corporation and Consolidated Subsidiaries For the Years Ended October 31 Millions of dollars, except share data 2003 2002 Income (loss) from
assets Total current assets Marketable securities Finance and other receivables, net Property and equipment, net Investments and other assets Deferred tax assets Prepaid and intangible pension assets Deferred tax assets. IABILITIES AND SHAREOWNERS' EQUITY Liabilities Current liabilities Current maturities of long-term debt
Accounts payable, principally trade Other liabilities 7 otal current liabilities $ 447 78 869 494 176 146 2,210 517 955 1,350 339 66 1,463 $ 6,900 $ $ 214 1,079 911 2,204 620 — 1,043 595 242 107 2,607 116 1,239 1,479 167 63 1,286 $ 6,957 358 1,020 1,029 2,407 (continued) 059402 01 ch6 p191-225.indd 222 7/7/14 9:06 AM Chapter 6 •
Abracadabra 223 Navistar International Corporation and Consolidated Subsidiaries As of October 31 Millions of dollars 2003 Debt: Manufacturing operations Financial services operations Financial services operations Financial services operations Postretirement benefits liabilities Commitments and contingencies Shareowners' equity Series D convertible junior preference stock
Common stock and additional paid in capital (75.3 million shares issued) Retained earnings (deficit) Accumulated other comprehensive loss Common stock held in treasury, at cost (6.5 million shares held) Total shareowners' equity 2002 863 1,533 1,435 555 6,590 747 1,651 1,354 547 6,706 4
2,118 (824) (786) 4 2,146 (721) (705) (202) 310 $ 6,900 (473) 251 $ 6,957 From NAVISTAR's 10-K 2002 NOTES, Page 539 Other Liabilities Major classifications of dollars Product liabilities at October 31 are as follows: Millions of dollars Product liabilities at October 31 are as follows: Millions of dollars Product liabilities Major classifications of other liabilities and warranty Employee incentive programs Payroll, commissions and employee-related benefits.... Pratt,
Mary K. November 4, 2007. Or that he could start buying and selling Enron's assets at prices more favorable to LJM1 than to Enron? In July 2009, the Rancho Cucamonga, Calif.-based company declared Chapter 11 bankruptcy and is now defunct. In their book examining the history of the financial crisis, McLean and Nocera report: "By June 1983, the
government agencies had issued almost $230 billion in mortgage-backed securities, while the purely private sector had issued only $10 billion" (2010, p. In determining to accept Peregrine's offer of partial settlement, the Commission considered remedial acts promptly undertaken by Peregrine and cooperation afforded the Commission staff. Despite
the conditional and indeterminate nature of this agreement, Sunbeam recorded $11 million sales and $5 million profit on the "sale" in 1997, even though, as the SEC stated, "The sale price had no practical relationship to any payment Sunbeam agreed to
create a reserve of $3 million against the profit it had raised, but left the balance of the income in the 1997 financial statements. One story is that the men at the meeting asked their waitress to suggest a name for their new company. This leads to a bubble, or an inflated price for an asset that is not justified on the grounds of its actual value—for
example, a share's price that is not supported by its earnings or a house's price that is not supported by the rents it could earn. Skilling became the CEO of this new division. During the relevant period, approximately 50 percent of the vendor recoveries deducted below the line from warranty reserve calculations were based on something other than
specific contractual language. Improper accounting of foreign payments, 300-302 Improper capitalization of expenses, 161-162, 170-174, 195, 198 The improper categorization of expenses as assets. He confronted management about a possibly illegal 50-cent surcharge on Medicare prescriptions and refused to make questionable payments. The
Emerging Issues Task Force clarified the situation regarding expenses for which a company is responsible but does not pay. Deferred Start-Up Costs. Alexander, Adair Morse, and Luigi Zingales. In fact, Wal-Mart considered ending its relationship with Sunbeam due to these glitches. MCI Falls under the WorldCom Spell MCI got its start in 1963
when ex-General Electric employee John (Jack) Goeken formed a group to pursue an investment idea. Ebbers and Grubman had no knowledge of the telecom industry, which led them to overestimate the demand for the Internet capacity. It was also suspicious that "Sunbeam's
inventories exploded by some 40% or $93 million, during 1997." In addition, there were "indications that Sunbeam jammed as many sales as it could into 1997 to pump both the top and bottom lines." The article in Barron's provided the final spark that exploded the Sunbeam façade. Company Profile. Holding Books Open after the Close of a Reporting
Period for the purpose of improper timing of revenue recognition SENSORMATIC 3. We're talking about a whole new definition of short-term." In addition, "Dunlap also cut back on memberships in industry
organizations and "eliminated all corporate gifts to charities." (Quotes from Byrne, 2003, p. This signal becomes stronger if the nature of the entities is vague or their transactions are vaguely described. It was going to cost millions of dollars to relocate the plant in an absurd attempt to save a few hundred thousand dollars of transportation costs are
year. Thompson Teaching and Learning Innovation Award by the Marshall School of Business. • Respond to the following Case Study questions. In 2000, the company and Ford finalized a contract for the supply of V-6 diesel engines commencing with model year 2002 and extending through 2012. (Parasole), to provide for 8 Extracted from 10-K filings
for Buca, Inc. Scheme #2: False Recognition of Early Shipments The next improper revenue recognition practice Sensormatic used to meet its quarterly sales budgets was the ploy of shipping goods that customers had ordered for the next period. It must be done scientifically, taking
care to cut only costs that do not support greater revenues. National Hotline Services. In other words, the integrity of an action flows from the virtuous character performing such an action, and that character embodies the virtuous character performing such an action, and that character embodies the virtuous character performing such an action, and that character embodies the virtuous character performing such an action flows from the virtuous character performing such an action, and that character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such an action flows from the virtuous character performing such action flows from the vir
15, 1998. 257). 1422 (JSR). Table 1.1 adapts the terminology of the SOX Report for each method of fictitious overstatement of assets or understatement of assets or unders
that Enron's contingent liability for Whitewing's debt would become an actual liability due to Whitewing's inability for this debt understated Enron's own debt. February 1, 2002. Akers had engaged in previous discussions with the vendor about possible future business and the payment of a
signing bonus, but the terms of the signing bonus were not finalized until after the 2003 fiscal year-end. Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties issued during the period Change in liability for preexisting warranties war
Payments made Balance, end of period 059402 01 ch6 p191-225.indd 225 $185 166 11 (189) $173 7/7/14 9:06 AM Chapter 7 Enron and the Tale of 1 the Golden Goose Learning Objectives After studying this chapter, you should be able to: • Explain Enron's abuse of mark-to-market accounting. • We conclude there was a systemic breakdown in
 accountability and ethics. February 18, 2011. He served his sentence in federal prisons in Florida. People who saw him only from afar—and he was very visible around Mississippi— couldn't get over what a down-to-earth billionaire he was, always in blue jeans and boots. Livent's preproduction costs should have been expensed through amortization
over the life of the shows (up to a period of not more than five years) once the shows began. Significant fluctuations in gross margin as a percentage of sales. Why would it do that? (c) Since the issuance of the guidance of EITF 01-14 in 2002, if a company is the primary obligor for an expense, it must report revenue net of expenses that are deducted
from those revenues before payment is made to the entity. To the strict utilitarian, it is the total of the pleasure for all parties in the aggregate that determines whether the action is right, irrespective of how that pleasure for all parties in the aggregate that determines whether the action is right, irrespective of how that pleasure for all parties in the aggregate that determines whether the action is right, irrespective of how that pleasure for all parties in the aggregate that determines whether the action is right, irrespective of how that pleasure for all parties in the aggregate that determines whether the action is right, irrespective of how that pleasure for all parties in the aggregate that determines whether the action is right, irrespective of how that pleasure for all parties in the aggregate that determines whether the action is right, irrespective of how that pleasure for all parties in the aggregate that determines whether the action is right, irrespective of how that pleasure for all parties in the aggregate that determines whether the action is right.
report the entire 23 years of profit in the current quarter. Almost 20 years later, on July 21, 2002, that same company would declare one of the most spectacular bankruptcies in corporate history. II. Most countries in Europe do not have stringent laws to protect whistleblowers. "Two Enron Traders Avoid Prison." February 15, 2007. July 12, 2007.
Kardashian, Kirk, Cameron likened it to a "grenade strategy," explaining that when you fling "a grenade into a company ... it explodes, eliminating the positions of a certain number of people. That in itself would not have produced any profit until the gas was delivered. 77-78) Mark in India.
 by unconsolidated affiliates must raise concern that the company may be liable for the debts of the affiliated entities. (d) Improper accounting for round-trip transactions. The CFO of Bronto Company for $1,000 in terms of which SPOCK1 gave
 Bronto the option to sell all 10,000 shares that Bronto owned in Saurus to SPOCK1 on June 30, 2013, for $50,000. A guarantee fee; 2. There should have been suspicion as to why Enron was investing so much in unconsolidated entities. Executives found guilty in huge financial frauds do not consider their families as stakeholders in their decision to
soared to $1.8 billion during 2000 and 2001" (Smith & Wilke, 2002). Several years earlier Martin's younger brother, Roger, had resigned from his position as a senior vice president at Rite Aid because "he recognized that the top job would go to a brother he considered incompetent." (Quotes from Berner & Maremont, 1999) Less than five years after
 insurer 332 Mortgage-backed securities (MBSs) 328 Pay-option ARM loan 337 Securitization 328 Subprime loans 329 Tranching 329 ETHICS AT WORK Read the extract below from the 2011 speech on "The Role of Compliance and Ethics in Risk Management," by Carlo di Florio, Director of the SEC's Office of Compliance Inspections and
in the case of Livent, because the SEC found that Livent contradicted its own accounting policy description when it miscapitalized costs, a note regarding a change in capitalization policy is often a blatant signal of an aggressive accounting policy to intentionally decrease recorded expenses. "Breakdown of Charges against Lay, Skilling." January 20,
2006. However, WorldCom was undeterred. This became a vicious circle because the company did not produce enough profit to repay its debt—and the debt kept growing. The 10-K filing for 2007 showed loans held for investment net of an allowance for loans losses
at December 31, 2006, was only approximately $0.33 billion. A recent appraisal performed by an independent and certified real estate appraiser is normally the best evidence of a property's fair value. Third, and most incriminating of all, soon after the first allocation of valuable IPO shares to Ebbers by Salomon, Ebbers used Salomon as WorldCom's
investment banker for the first time. Indeed, the prediction in Barron's proved to be correct. For payoption loans, or loans of close to 100 percent on which the borrowers chose to pay less than the interest amount, little or no loss would occur on default and foreclosure as long as house prices continued to rise as fast as the unpaid interest. On the
basis of this Order and Respondent's Offer, the Commission finds1 that: Summary 1. Nevertheless, certain aspects of distributive justice are clear enough to be useful. The SEC noted that enormous losses were incurred in 2007 in all of these areas.
August 2006, BLMIS registered as an investment adviser with the SEC. Gadel and Skrypek targeted repair and maintenance expenses as a way to make up the difference between analyst earnings expectations and Buca's preliminary financial results. However, unlike eBay, which offers a marketplace for other buyers and sellers, Enron Online actually
purchased everything that it resold. 059402_01_ch2 p047-068.indd 61 7/7/14 8:59 AM 62 Chapter 2 • Ethics at Work 17. A leading sign of an overstatement of sales in Sensormatic's fictitious reporting schemes is the increase of accounts receivable as a percentage of sales. 2-3) Dunlap then confronted the CFO, Paul O'Hara, and blamed him for
Sunbeam's failure to meet the previous year's financial performance estimates. The prospectus filed with the registration statement incorporates by reference Respondent's annual and quarterly reports. Consequentialism While the term consequentialism while the term consequentialism.
the consequences that they produce, it is possible to distinguish between different forms of consequentialism. However, Dunlap's rage continued unabated toward the rest of the world. Twenty-four years later, in 1925, Houston Oil entered the gas business and formed two companies: the Houston Pipeline Company (to pipe natural gas) and Houston
Natural Gas (to distribute the gas). Another important lesson was that a series of minor indiscretions can slowly accrete into a major crime. Madoff from two sham trades, and disguised the proceeds of the trades as long-term stock transactions in order to take advantage of the lower tax rate for long-term capital gains; • Madoff charged
approximately $175,000 in personal expenses to a corporate American Express card and did not report those expenses as income. "Basic Legal Concepts: Beware Insufficient Knowledge of the Law," Journal of Accountancy, October. Beazer improperly accounted for more than half of these leased model homes as sale-leasebacks in order to improve
Beazer's financial results. Over the next few years, Enron's trading operations grew in many different directions until, eventually, the trading division opened Enron Online, which bought and sold over 800 different commodities. This meant that it could not guarantee the security of the transmitted information and that it would have to invest in
connection facilities to move the data to its customers. Other large customers claimed that shipments were late and that the staff turnover made continuity difficult. Why do overstatements of restructuring reserves sometimes cause gross margin percentages to change suddenly? • Explain how restructuring reserves can be used to overstate earnings
in future periods. As the scheme went on, the improper capitalization of repair and maintenance invoices significantly expanded. According to accepted accounting practice, Enron could report only 1/23 of this revenue each year for the next 23 years. If a company is operating at a profit, why would it not be generating CFFO at a similar pace?
Hedonist's paradox, 50 Hirko, Joe, 242 Holding books open, 119-120 Keeping the current period's books and records open for a few extra days after the close of a reporting period to record additional sales. July 3, 2003. Januszewski, Esq., at Cahill Gordon & Reindel LLP, Eighty Pine Street, New York, New York 10005-1702; and ii Agrees that any
such notice or subpoena for Respondent's appearance and testimony in an action pending in a United States District Court may be served, and may require testimony, beyond the territorial limits imposed by the Federal Rules of Civil Procedure. • There was no reliable market price for the sale of the assets. Fisher, Daniel. In May 2012, he was voted
one of the best professors in the Marshall School of Business and received the Golden Apple Award. Greg A. In particular, one school recognizes a plurality of communities in which the diversity of the communities must be taken into
account. (Third and Final Report, 2004, p. However, Michael Price needed to be the new CEO of Sunbeam. From 2000 through 2004, Buca also filed with the Commission several S-8 registration statements in
Malaysia Reviewers Mohamad Hajj, Lebanese University, Malaysia 20 059402_01_FM_p001-024.indd 20 7/7/14 8:57 AM ABOUT THE AUTHOR Cecil Jackson, Professor of Clinical Accounting in the Leventhal School of Accounting at the
University of Southern California, teaches courses on detecting accounting fraud and on managerial accounting for the MBA program as well as the graduate and undergraduate accounting fraud and on managerial accounting for the MBA program as well as the graduate and undergraduate accounting for the MBA program as well as the graduate and undergraduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the MBA program as well as the graduate accounting for the graduate acc
that is, exactly what happened because the "hedge guarantee" that Enron would sell its Rhythms stock at $56 a share to LJM1 was not a guarantee at all. The sixth factor is whether the organization has appropriate incentives to support the compliance and ethics program, and appropriate disciplinary measures for failing to take reasonable steps to
prevent or detect criminal conduct. Although InterNorth was three times the size of HNG, the deal was done on terms that were unusually favorable to HNG. Accounting Fraud and the Financial Crisis of 2008 Ironically, in 1999, about two-and-a-half years before the SOX Act was signed into law, the Glass-Steagall Act was repealed and the Financial
Services Modernization Act was passed to deregulate the banking sector in the United States. The various bilking schemes became so pervasive that they had their own names. Debt company guarantees of, 271-272 growth of, 275 troubled debt restructurings, 358-359, 360 understatement of, 265-272 Debt-equity ratio, 275, 276t Decision-making
models for accountants, 58-60 American Accounting Association, 59, 59t in business world, 53-58 consequentialist/utilitarian, 54-55 ethical, 53-61 justice approach, 57-58 rights-and-duties approach, 55-57 Deferred assets to sales ratio, 197 Deferred costs, 197, 220-221 Deferred revenue, 128 Deloitte & Touche LLP, 300 DenDanto, Deidra, 87-58 rights-and-duties approach, 55-57 Deferred assets to sales ratio, 197 Deferred costs, 197, 220-221 Deferred revenue, 128 Deloitte & Touche LLP, 300 DenDanto, Deidra, 87-58 rights-and-duties approach, 55-57 Deferred assets to sales ratio, 197 Deferred revenue, 128 Deloitte & Touche LLP, 300 DenDanto, Deidra, 87-58 rights-and-duties approach, 55-57 Deferred assets to sales ratio, 197 Deferred assets to sales ratio, 197 Deferred revenue, 128 Deloitte & Touche LLP, 300 DenDanto, Deidra, 87-58 rights-and-duties approach, 55-57 Deferred assets to sales ratio, 197 Deferred revenue, 198 Deloitte & Touche LLP, 300 DenDanto, Deidra, 87-58 rights-and-duties approach, 57-58 rights-and-d
Denna, Eric L., 75 Deontological theory, 49, 50-51 A normative ethical theory that uses duty as the criterion for right action. What is meant by negative amortization? Whalen, Don, Esq., Mark Cheffers, and Olga Usvyatsky. Conflicts of interest. December 7, 2009. 28. After hearing an appeal in March 2011, the Supreme Court sent Skilling's case to
the 5th U.S. Circuit Court of Appeals in New Orleans to determine whether a new trial was necessary. The CFO of Power Company buys the remaining equity interest in P2 with cash loaned to him by Power. SEC's Enforcement Program Continues to Show Strong Results in Safeguarding Investors and Markets. According to the SEC, "Krispy Kreme
increased the price it paid for the franchise by $800,000, i.e., from $65,000,000 in return for the franchise purchasing from Krispy Kreme certain doughnut making equipment" (AAER 2941, 2009). • Scott Livengood was removed from his position as CEO in January 2005. Essentially, mark-to-market accounting allowed Enron to look at
an 059402_01_ch7_p226-291.indd 247 7/7/14 9:08 AM 248 Chapter 7 • Enron and the Tale of the Golden Goose asset—be it a merchant asset or a contract or publicly traded stocks—and revalue it to its "fair" value. Models that are useful for the evaluation of ethical issues in the business world include: (a) The American Accounting Association
percent equity requirement. It simply looks bad to have Andersen earning more on consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation for accepting increasing consulting fees from Nanette Byrnes et al., 2002) Together with condemnation fees from Nanette Byrnes et al., 2002) Together with condemnation fees from Nanette Byrnes et al., 2002 and 2002
 failures. See Accounting fraud Corporate Fraud Task Force (CFTF), 40 Corporate governance, reforms, 35-38 Cost-accounting analysis, 76 Cost of goods sold, 199 The cost of inventory sold during the period. Further, part of the securitization included a related-party transaction with an off-balance-sheet partnership entity (Whitewing). Reporting
Failures Regarding Certain Deferred Start-up Costs 38. And they didn't want to lose their stock options, which had increased in value, but for the most part had not yet vested in Pincus, 2002, p. Citing Brown's advanced age, 76 at that time, his attorneys described the sentencing as "a de facto death sentence" (Scolforo, 2004). October 22, 2002.
 "Accounting Fraud Targeted: With Crisis-Related Enforcement Ebbing, SEC Is Turning Back to Main Street," Wall Street Journal. 059402_01_ch6_p191-225.indd 209 7/7/14 9:06 AM 210 Chapter 6 • Abracadabra As Jim Balassone, executive-in-residence at the Markkula Center for Applied Ethics, noted in his introduction, "Tim and I are the same
age, with similar backgrounds and education. Enron generally issued only its income statement of tas financial statement of cash flows available much later, when it filed its financial statement with the SEC. All Sullivan and his cohorts had to do was acquire numerous companies and
pretend they were paying for large amounts of goodwill as they overstated the reserves and undervalued the assets. Because neither JEDI nor Chewco were independent entities, this amount was a related-party transaction that, in effect, amounted to Enron paying itself. By 2002, Telcel had become the largest wireless supplier in Venezuela and was
 BellSouth's largest revenue earner in Latin America. CUC International, Inc., was a company (registered in Delaware) that sold club memberships to its customers for automobile, dining, shopping, and travel services. The first loan of $50 million was made to Ebbers by the WorldCom compensation committee on September 6, 2000. "Accounting in
Crisis," Business Week, January 28. 30). In the fourth quarter of 1999, Enron booked another $31 million using mark-to-market accounting on a further revaluation of this same plant. Gadel improperly charged Buca for such things as family vacations and visits to strip clubs. Adelphia, its subsidiaries, and the Rigas Entities all deposited and withdrew
                                                                                     . Beazer recorded this purchased land as an asset on its balance sheet in accounts denoted as "land inventory accounts of the parcel, such as costs for sewer systems and streets. There was a time, about
13 years ago, when Andrew Fastow had achieved the pinnacle of success and fame that could be expected of a chief financial officer. Available online via EBSCOhost. The use of any trademarks, nor does the use of such trademarks imply any
affiliation with or endorsement of this book by such owners. The reversal led Rite Aid to find new adjustments in the fourth quarter to offset the reversal. In mid November, 2013, the company's share price was almost $26.00 per share. 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam Required a. CBSNEWS.com. 1983. It offers suggested
fictitious financial reporting. Further, if the transaction involves actual work that must be done in the future to realize a future profit, the profit can only be recognized once the work has been done. Such analysis and contemplation is highly likely to increase the decision maker's awareness of all the nuances and issues at stake. In the 2006 10-K, therefore the decision maker's awareness of all the nuances and issues at stake.
was a change to Note 8 on loans held for investment from reporting delinquencies of more than 90 days, to reporting delinquencies of more than 90 days.
11.12 percent. With these acquisitions, the company's sales grew and the volume of reswitching equipment grew as well. For financial service firms, this auditing, monitoring and testing should, in my view, encompass testing of the effectiveness of the organization's policies and procedures regarding management of conflicts of interest. The
Liquidation of LJM1 To add insult to injury, Fastow hoodwinked a whole group of individuals in the shares of this private company were worth. Today's plea represents an important step forward." DOL-OIG Special Agent in Charge Robert L. The
financing revenue for years 1, 2, and 3 were $400, $600, and $800, respectively. Beazer, a Delaware corporation headquartered in Atlanta, Georgia, is a homebuilder with operations in at least twenty-one states. In February 2001, an accountant named Wanda Curry reported to Enron's chief accounting officer that she was investigating several
discrepancies at EES. However, the conglomerate did not adjust its 1996 financial statements. (d) Improper capitalization of expenses. "FTC's Competition Bureau Closes Investigation into Comcast, Time Warner Cable and Adelphia Communications," January 31, 2006. The Gas Bank was a brilliant concept. Similarly, if management
announced that it was going to increase sales by cutting products and increase production by closing plants and firing employees, that would sound counterintuitive; the logic might be questioned, and the predictions of increased earnings might not sound credible. The Powers Report (2002) summarized these pre-Enron requirements3 as follows: A
company that does business with an SPE may treat that SPE as if it were an independent outside entity for accounting purposes if two conditions are met: 1. These companies had price-earnings ratios far higher than Enron's. www.dw.de. The stock continued to rise after Dunlap said, in July, that he had begun a study for a downsizing plan that would
produce a turnaround. Calculate Brite's days' sales in inventory for Q2, Q3, and Q4. The revenue must be earned. 059402_01_ch9_p325-360.indd 337 7/7/14 9:11 AM 338 Chapter 9 • Mortgage Mayhem Countrywide's loans in its 10-Ks
was misleading "because its description of 'prime non-conforming' and 'nonprime' loans in its periodic filings were insufficient to inform investors what type of loans were included in these categories" (June 4, 2009, par. The charming pictures of the campus and town looked enticing, and Foster decided that this was the fresh start that he needed.
Statement of cash flows, 91 Steinhardt, Michael, 71 Steinhardt Partners Fund, 71 Steinhardt Partners Fund, 71 Steinhardt Partners Fund, 71 Steinhardt Partners Fund, 71 Steinhardt, Michael, 71 Steinhardt Partners Fund, 71 Steinhardt, Michael, Michael
us consider the convoluted transactions of Raptor I, which was started with the formation of an SPE officially called Talon LLC. The adjustments always increased earnings, and they never had supporting documentation. As such, utilitarianism is capable of being either overly permissive or overly stringent. The SPE known as LJM SwapCo was made
general partner of LIM Swap Sub. • Our stock markets require valid information in order to operate efficiently. Securitization refers to the pooling of loans and the trading of portions of these loans on securitizes markets in the form of collateralized debt obligations.
2000, 2001, and 2002. The auditors either passed or missed the adjustments listed in Table 5.2. Thornburgh stated that for the $239,000,000.'" At certain times, the reserves were released even though personnel had determined "that such reserves"
were needed to ensure that the company had accrued the appropriate level of reserves in relation to its liabilities." At other times, the releases were cookie-jar reserves that had been kept for when costs needed to be reduced. (c) Improper deferral of expenses. Using Marianne Jennings' seven signs of ethical collapse as a guide, he noted that he could
probably give a concrete example of each one. They did not want to lose the value of all the shares they mere reporting in their financial statements. Gross
profit, 200 Grubman, Jack, 148-149, 156, 169, 174 Grubman, Richard, 274 GSE (government-sponsored enterprise/entity), 328, 334, 335 GSE conforming loans, 328-329, 335 Guaranteed liabilities, 271-272 Guaranteed sales, 80-81, 94 H Hannon, Kevin, 242 Happiness, 49 Harlow, Phillip, 89 Hedonism, 50 A type of classic utilitarianism that uses
 pleasure (and/or pain) to judge the consequences of an action. Fastow's story is a perfect case study for business school students on the blurry line between genius problem solving and fraud. Homes are the foundation upon which many of our social, personal, governmental, and economic structures rest. Lehman's efforts throughout the summer of
mortgages that were guaranteed by the Veterans Administration. "Scott Livengood, CEO, Krispy Kreme." June 22, 2004. What are the facts? LR 17001. In 2006, the FTC agreed to the acquisition of Adelphia by Time Warner Cable and Comcast ("FTC's Competition Bureau...," 2006). The decline of a company's asset-turnover ratio is an indication that
assets are impaired. Although members of WorldCom's internal audit department were finally instrumental in uncovering the financial reporting frauds and reporting frauds and the understaffing of its internal audit department. "Europe
US Take Different Approaches to Whistleblowing," Deutche Welle. In fact, whenever any expense fluctuates too wildly as a percentage of sales or stays at a constant percentage of sales or stays at a constant percentage of sales or stays at a constant percentage of sales quarter after quarter of 1997, $29 million was later
reversed and restated as future periods' sales. Bryce, Robert. It was also its most brazen scheme. Explain why Rite Aid's failure to write down its ending inventory amount—to agree with values determined by physical inventory counts—caused it to overstate its income. Fastow went astray not with one shocking act of fraud, but by degrees. In the
fourth quarter of 1997, Sunbeam entered into a thoroughly inconclusive "sales" agreement with a fulfillment house to sell an indeterminate amount of spare parts to the Sunbeam trajectory had been approaching in the form of Morgan Stanley's
 "due diligence" test for the debt offering that it was underwriting to raise the cash for Sunbeam's acquisitions of Coleman, First Alert, and Signature Brands. 7 Originally published in 2007 by the Markkula Center for Applied Ethics, at Santa Clara University, California: www.scu.edu/ethics. 2004, p. Krispy Kreme also failed to accrue the full amount
of incentive compensation expense in accordance with the PCAOB, and it requires the board to establish or modify, as required, standards for auditing, reporting, ethics, and quality control. (AAER 1585, 2002) The obvious question in the face of
such a brazen and crude fraud is, where were the auditors? www.forbes.com. May 30, 2013. Section 404(a) "requires management to report on the effectiveness of the company's internal controls over financial reporting, and Section 404(b) requires the auditor's attestation regarding their effectiveness" ("The Sarbanes-Oxley Act at 10," 2012). He
was going to close production plants, drop product lines, and slash workers' jobs. Overstatement of ending inventory or of revenues; understatement of purchases or cost of goods manufactured. In this instance, as is often the case, Livent achieved the deferral of expenses by moving the cost from one asset account to another, where the amortization
could be delayed. First, he noted that during the time of Homer, bodily strength and physical courage were considered major virtues on the grounds that Cosmo Corigliano, who served as controller of CUC from 1983 to 1995 and as CFO from 1995 to 1997, "assisted
                                                                        inancial reporting fraud and later, as CUC's Chief Financial Officer, proceeded to orchestrate and refine the fraud" (AAER 2014, 2004).7 Referring to the CUC case, Richard Walker, SEC Director of Enforcement, noted that "large, complex, and long-
originate at the highest levels of a company" (AAER 1372, 2001; LR 16919, 2001). But what bothers me about Al Dunlap is his lack of precision. RELATED-PARTY TRANSACTIONS Management Agreement with its former parent company, Parasole Restaurant Holding, Inc. (a) Conforming to GSE
underwriting standards. Bank of America paid $45 million of this amount. The brochure was, oddly, an advertisement for Mississippi College in the town of Clinton. Born in Pittsburgh in 1953, Skilling was the son of an engineer-turned- traveling salesman who lost his job, forcing the family to move to Chicago, where Skilling, with very little effort, did
exceptionally well in high school. for the 11. Future amortization of patent costs at December 31, 2007 is approximately $107 per year for each year thereafter through 2024. Lay put one of his traders, Mike Muckleroy, in charge of the salvage effort. Securities and Exchange
Commission News Release. T F 6. The $18.5 million total represented 5.9 percent of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (d) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] . . . . sec.gov. (e) Revenue recognized over the life of the lease. [and] 
Fees—The Company utilizes the son of one of the board of directors to perform architectural and design related services. As the mortgage loans being securitized grew increasingly weighted toward loans on the same houses, the banks grew wary of issuing letters of credit
guaranteeing the securitized loans against default. He believed that he just needed to appoint the right kind of CEO—a leader who could do another turnaround of Sunbeam. Describe the role of tranching in the granting of easy credit that fueled the housing bubble. To his credit, he first rejected the job, but Skilling talked him into accepting the
position. www3.cfo.com. 059402 01 ch5 p144-190.indd 147 7/7/14 9:04 AM 148 Chapter 5 • WorldCom Wizardry: From WorldCom to Wor
ended the Azurix hemorrhage when it paid over $300 million to buy back the shares—held by the public—at just over $8 a share, when the shares were trading at around $3.50 per share. According to Mill, actions are right in proportion to the happiness they tend to promote and the morally best action of those open to us is the action that maximizes
happiness— or (in his sense) has utility. In June 2009, Bernard Madoff was sentenced to 150 years in prison (Henriques, 2009). An MBS is a financial
                                                                                                                                                                                                                           that gives the owner a partial interest in a pool of mortgage loans. When Xerox factored or sold its accounts receivable to avoid reclassifying them as operating leases instead of sales-type
leases, this had the effect of: (a) Decreasing the amount of revenue it reported. In the latter case, the investment in PPE assets is not producing the revenue for which the investment was made in the first place. 22. So less than a week after Dunlap announced his plan, White left Sunbeam. In May 1991, when Skilling cracked open the champagne to
celebrate his right to use mark-to-market accounting, he was focused on the ability to report massive amounts of expected future earnings as current-period profits and the boost this would give to Enron's stock price as well as to his compensation, definition of, 119 fictitious revenue, 126-129 improper timing, 122-125 premature revenue recognition
121 at Sensormatic, 119-122 Improper timing of revenue recognition, 80-84, 90-94, 119-120, 122-125 The process of formally recording a revenue item in the financial statements in an earlier or later period than the period by leasing
companies" ("SEC Complaint...," 2003). Mill, who became the leading utilitarian scholar, specified that the net pleasure to be maximized when performing the right action referred to the pleasure of all who would be affected by the action, and not just one's own pleasure. Both sales and franchise acquisition rights (an intangible asset) were
overstated in the process. As a result of this civil litigation, KPMG agreed to pay a total of $22.475 million in penalties. Not only had operations become chaotic and confused with all the uncoordinated and incongruent companies, but the telecom industry itself was feeling the effects of having built capacity for an overestimated future growth
projection (Krim, 2002). (c) Offering deep discounts and extended payment terms. U.S. Securities and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using tranching, traders "could divide the securities and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using tranching, traders "could divide the securities and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using tranching, traders "could divide the securities and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using tranching, traders "could divide the securities and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using tranching, traders "could divide the securities and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using tranching, traders "could divide the securities and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using transition and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using transition and Exchange Commission Accounting and Auditing Enforcement Release, June 21, 2002. Using transition and Exchange Commission Accounting and Exchange Commission Accounting Enforcement Release, June 21, 2002. Using the Exchange Commission and Exchange Commission Accounting Enforcement Release, June 21, 2002. Using the Exchange Commission Accounting Enforcement Release, June 21, 2002. Using the Exchange Commission Accounting Enforcement Release, June 21, 2002. Using the Exchange Commission Accounting Enforcement Release, June 21, 2002. Using the Exchange Commission Accounting Enforcement Release, June 21, 2002. Using the Exchange Commission Accounting Enforcement Release, June 21, 2002. Using Exchange Commission Accounting Enforcement Release, June 21, 2002. Using Exchange Commission Accounting Enforcement Release, June 21, 2002. Using Exchange Commission Accounting Exchange Commission Accounting Enforcement 
p. Enron could move gas in its own pipelines with its own connections all the way from the power plant to the utility company. These changes seem to be effective. (Non-GAAP financial measures that are not included in accordance
with GAAP.) For example, in its 10-Ks for 2000 and 2001, the company was accused of misreporting documents or explanations" (Third and Final Report, 2004, p. Purchasing Timber Rights from the Rigas Family According to the Commission,
Adelphia purchased certain rights, including timber rights, to 3,656 acres of land owned by the Rigas family in Potter County, Pennsylvania. "Cendant Official Must Pay Back $3.27 Billion." Washingtonpost.com. accounting fraud and, 151-155, 159-160, 169-170 by WorldCom, 149-156, 159-160, 166-167 Action rights, 56 383
059402 01 GLINDEX p383-401 indd 383 7/7/14 9:17 AM 384 Glindex Adelphia Communications Corporation, 295-300 AICPA (American Institute of Certified Public Accountants), 32, 36, 48 AIG, 38, 332 Allegheny International, Inc. The banks and insurers lobbied strenuously against this to protect their new, highly lucrative profit stream. It is
concerned with the ethical categories of good and bad. Press Release. 059402 01 ch8 p292-324.indd 312 (b) The company falsified operations statistics. "BellSouth Profit Up on Wireless Growth." January 25, 2006. For MacIntyre, performing a practice in such a way as to benefit inherently from that practice is a virtue because one achieves an
intrinsic benefit that can be obtained only from performing the practice properly. However, if the CEO announced that he or she was going to perform a turnaround in a brief period by embarking on an aggressive downsizing and cost-cutting plan, Wall Street would embrace the plan and celebrate the vision of a quick turnaround with high profits and
even higher stock prices. "Insignia is now a wholly owned subsidiary of ASI" ("Insignia Solutions," 2009). LR 20312. Since 1977, the had been responsible for monitoring audit independence and quality, but it did not have the power to punish wrongdoers in the face of accounting frauds. Further, EDP billed Buca for salary payments totaling
$1,394,775 made to High Wire employees, even though many of these High Wire employees spent little or no time working for Buca. T T T 16. J. Securities and Exchange Commission Complaint for Violation of the Federal Securities and Exchange Commission Complaint for Violation of the Federal Securities and Exchange Commission Complaint for Violation of the Federal Securities and Exchange Commission Complaint for Violation of the Federal Securities and Exchange Commission Complaint for Violation of the Federal Securities and Exchange Commission Complaint for Violation of the Federal Securities and Exchange Commission Complaint for Violation of the Federal Securities Laws vs. April 26, 2005. Third, several of the "sold" invoices were fake. Without these errors, the company would no
have been able to meet its aggressive sales and earnings estimates as consistently as it did. Edison received approximately $6,500 per year for each student enrolled at each school, and the teachers usually received compensation that reflected the extra teaching hours required in the Edison schools. The complicated structure of the Rhythms
transactions can be seen in Exhibit 7.3. With these absurd procedures injected into Fastow's interlocking SPEs, it is no wonder that later, in attempting to unrayel it all. Enron's post-bankruptcy CEO. Stephen Cooper, declared, "It looks like some deranged artist went to work one night" (gtd. During fiscal year 2006, when Beazer began to reverse
some of the excess accruals, Respondent overstated its net 059402_01_ch3_p069-116.indd 105 7/7/14 9:01 AM 106 Chapter 3 • The Sizzling Saga of Sunbeam income by over $1.2 million. The Wizards of WorldCom During a CNBC television interview hosted by David Faber in September 2003, Robert Hudspeth, a former WorldCom vice president
described how there appeared to have been a discrepancy between WorldCom's internal numbers and the numbers touted on Wall Street. 276, 283) The combination of Arthur Andersen's restricted access to the accounting records together with the machinations by WorldCom to deceive the auditors led to Arthur Andersen's being oblivious of these
top-side transfers from expenses to assets. 7/7/14 9:15 AM References 369 Byrne, John A. This would require Enron to build a massive energy plant estimated to cost just under $4 billion. This gave the impression of a financially healthy company. ** Part III of Speech. Too Big to Fail. Fastow offered to invest $1 million of his own cash into LJM1, with a
further 059402 01 ch7 p226-291 indd 252 7/7/14 9:08 AM Guarantee Fee tn d Pa r ite Enron bt ran a Gulr Pa tn er GP $114 K LP Sole Member SONR #2 LLC $10 K Little River Funding LLC $314 K Big River Funding LLC SONR #1 L.P. $1 K SONR #1 LLC Sole Member Exhibit
7.1 A Diagram of the Chewco Transaction. Prepaid expenses, 197 Prepays, 235, 263-264 Transactions in terms of contracts in which one party enters into a contract with another party to deliver a commodity in the future at a specified price. They also understated Enron's contingent liabilities in the notes to Enron's financial statements. "The
Numbers Game: Remarks at NYU Center for Law and Business." www.sec.gov. They resulted not only in significant financial consequences but also in damage to the trust of investors, businesses, and the public.... The Examiner claimed that Ebbers breached his fiduciary duties and "that SSB aided . . . and abetted those breaches" (Third and Final
Report, 2004, p. This is likely to show up in ratios that measure accounts receivable as a percentage of sales (for example, an increase in DSO). 059402 01 ch1 p025-046.indd 41 7/7/14 8:58 AM 42 Chapter 1 • Introduction to the Problem of Accounting Fraud To fight accounting fraud effectively, it is essential that those who prepare and use
financial statements understand the ethical underpinnings necessary for a healthy and functional business environment and why it is imperative that investors have access to and trust in "high quality" financial information. For example, a power project in the Dominican Republic caused soot to be blown onto a neighboring hotel, resulting in an
extremely expensive lawsuit: "For Enron, the deal was a complete bust; through mid-2000 the company had collected a pathetic $3.5 million investment." Possibly the most infamous hardasset losses for Enron—and the deals that Mark pushed hardest to accomplish—were the Dabhol Power Project in India and the Azurix water
project in England. August 26, 2007. If the reciprocal payment is supposedly for an investing activity, as in Krispy Kreme's case, this signal will also be obscured. According to the Commission, Sensormatic instructed employees to withhold certain bills of lading from the auditors because they would have indicated a practice of premature revenue -
recognition, in which revenue was recorded in the financial statements in an earlier period than it should have been recorded. Morgan Stanley, 86-87, 96 Morse, Gene, 164-165 Mortgage-backed securities (MBSs), 327, 328, 332 Financial instruments that give the owners an interest in a mortgage loan or a partial interest in a pool of mortgage loans.
McLean and Elkind (2004) pointed out: ... This means that the percentage of loans delinquent for 90 days or more in 2006 was 6.5 times as high as in 2005. So in 1998, Mark began the startup water company called Azurix, which she financed with money from Enron via an Enron off-balance-sheet entity named Marlin. "Enron's Dirty Laundry,"
Newsweek. University Park, PA: Pennsylvania State University Press. Rudolph, Vernon, 302 S Sabatino, Casper, 129 Sales accounts receivable as percentage of, 203 overstatement of, 121-122 ratio of deferred assets to, 197 Sales discounts, 93-94 Sales
estimates, inability to meet, 94 Sales-to-PPE ratio, 171-172 The ratio of a business entity's sales to the amount it has invested in property, plant, and equipment. Around that time, LDDS's first two CPAs quit the company—ostensibly because of "personality clashes." Looking back, one has to wonder if there were other reasons. *Obtained from U.S
Securities and Exchange Commission. (d) Will likely be vilified by the SEC. August 4, 2005. The predicament was simply this: Enron began its life with too much debt. 059402 01 ch2 p047-068.indd 66 7/7/14 8:59 AM 67 Chapter 2 • Ethics at Work In addition, from 1998 through 2008, Madoff engaged in a tax fraud scheme involving the transfer of
wealth within the Madoff family in ways that allowed him to avoid paying millions of dollars in required taxes to the IRS. If the ratio is lower than the industry average or if it is decreasing, it is an indication that some expenses may be recorded as assets or that the investment in assets is not efficient in that it is not producing sufficient revenue.
Understating assets or overstating liabilities and reserves when acquiring a new company: When a new company: When a new company is acquired, how does understating liabilities and reserves when acquiring a new company is acquired, how does understating liabilities and reserves when acquiring a new company is acquired, how does understating liabilities and reserves when acquiring a new company is acquired, how does understating liabilities and reserves when acquiring a new company is acquired, how does understating liabilities and reserves when acquiring a new company is acquired, how does understating liabilities and reserves when acquiring a new company is acquired, how does understating liabilities and reserves increase the reported post-acquiring a new company is acquired, how does understating liabilities and reserves when acquiring a new company is acquired, how does understating liabilities and reserves increase the reported post-acquired post-acqu
143.indd 134 30. How did WorldCom spin so out of control? She may think that the virtue of courage requires her to tell the truth in an astute and effective way. In fact, huge losses became evident in 2007, when the allowance for loan losses on all loans held for
investment jumped from $0.2619 billion in 2006 to $2.34 billion in 2007. Chapter 5 AAER 1585. As early as January 2003, an article in the Wall Street Journal warned that in the subprime sector, the numbers of delinquent loans and foreclosures were much higher than expected (Barta, 2003). "Towns Dread Job Cuts But Investors Appliand the Role of
'Chainsaw,'" Schifrin, Matthew. The full extent of TierOne's loan-related losses did not become publicly known until late 2009, after OTS required TierOne to obtain new appraisals for its impaired loans. CFFO refers to the amount of cash generated after expenses from the company's main operating activities, such as sales, services rendered, or other
operating activities. • Michael Mulcahey, former vice president, was found not guilty of conspiracy and securities fraud ("Status of High-Profile ...," 2005). In spite of these amendments, the size of the financial obligation to MSEB was still outrageous and would probably have bankrupted the province. In an attempt to decrease the likelihood of
auditors being pressured by management into adopting manipulative accounting treatments, SOX requires reporting of the following to the board's audit committee for its review: • Critical accounting policies and practices used by the organization, including methods, assumptions, and judgments. In a company that sells membership subscriptions
deferred revenue as a percentage of total revenue is an indication that the company may be overstating revenues. Madoff Investment Securities, LLC 64 Chapter 3 The Sizzling Saga of Sunbeam 70 The History of Al Dunlap 72 How Wall Street Embraced Sunbeam 89 The History of Sunbeam 89 The History of Sunbeam 80 The History of Sunbeam
Dumbsizing?" 75 Dunlap's Carrot-and-Stick Approach 76 An Overview of Sunbeam's Fictitious Financial Reporting Scheme #1: Improper Timing of Revenue Recognition via Bill and Hold Sales, Consignment Sales 80 Scheme #2: Improper Use of Restructuring Reserves 84 The Sunbeam Inferno 85
Signals of Sunbeam's Schemes 90 Signals of Sunbeam's Fictitious Reporting Scheme #1—Improper Timing of Revenue Recognition via Bill and Hold Sales, Consignment Sales, and Other Contingency Sales 94 Are They
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Living Happily Ever After? 95 Key Terms 96 • Ethics at Work 96 • Assignments 97 Case Study: Beazer Homes USA, Inc. 101 Chapter 4 Hocus Pocus 117 Sensormatic: Madness at Midnight 118 An Overview of Sensormatic's Fictitious Financial Reporting Schemes 119 Scheme #1: Holding Books Open after the Close of a

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Reporting Period 119 Scheme #2: False Recognition of Early Shipments 120 Scheme #3: Slow Shipping Requests 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #3: Misleading the Auditors 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #3: Misleading the Auditors 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #3: Slow Shipping Requests 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #3: Misleading the Auditors 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment 120 Scheme #4: Recognizing Sales at the Time Sales at the Time
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Myth of Internet Growth 151 Making Accounting Magic with Acquisitions 152 MCI Falls under the WorldCom Spell 155 Problems at WorldCom 156 An Overview of WorldCom 156 An Overview of WorldCom 157 Problems 158 Scheme #1: Improper Use of Merger Reserves 159 Scheme #2: Improper Capitalization of Expenses 161 The
Collapse of Wizard World 162 Ebbers Loses Control 162 The End of the Sullivan Era 164 059402 01 FM p001-024.indd 11 7/7/14 8:57 AM 12 Contents The Gatekeepers Who Failed WorldCom Fraud 169 Signals of the WorldCom Fraud 169 Signals of WorldCom Fraud 169 Signals of the WorldCom Fraud 169 Signals of the WorldCom Fraud 169 Signals of the WorldCom Fraud 169 Signals of WorldCom Fraud 169 Signals of the WorldCom Fraud
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Reporting Scheme of Failing to Account for Asset Impairments 208 Are They Living Happily Ever After? 209 Key Terms 209 • Ethics at Work 209 • Assignments 212 Chapter 7 Enron and the Tale of the Golden Goose
226 The Start of Enron 227 Kenneth Lay 227 Jeffrey Skilling 231 Andrew Fastow 234 Enron Capital and Trade (ECT) 235 How Enron Doline 240 Enron Broadband Services 241 The Electricity Fiasco in
California 244 Enron's Fictitious Financial Reporting Scheme #1: The Abuse of Mark-to-Market Accounting via Mariner Energy 247 Scheme #2: The Abuse of SPEs 248 Scheme #3: The Prepay Transactions 263 Signals of the Enron Frauds 265 Signals of Enron's Fictitious Reporting Schemes of Using SPEs (or
Unconsolidated Affiliates) to Understate Debt and Overstate Earnings 265 059402_01_FM_p001-024.indd 13 7/7/14 8:57 AM 14 Contents General Signals of Enron's Assorted Financial Problems 272 Are They Living Happily Ever After? 277 Key Terms 278 • Ethics at Work 279 • Assignments 280 Case Study: Basin Water, Inc
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After? 302 Krispy Kreme and the Missing Dough 302 An Overview of Krispy Kreme's Operational Problems 304 An Overview of Krispy Kreme's Operational Problems 304 An Overview of Krispy Kreme's Operational Problems 304 An Overview of Krispy Kreme's Operational Problems 305 The Krispy Kreme and the Missing Dough 302 An Overview of Krispy Kreme's Operational Problems 304 An Overview of Krispy Kreme's Operational Problems 305 The Krispy Kreme's Operational Problems 306 An Overview of Krispy Kreme's Operational Problems 307 An Overview of Krispy Kreme's Operational Problems 308 An Overview of Krispy Kreme's Operation
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9 Mortgage Mayhem 325 The Housing Bubble 326 Easy Credit: Securitization 327 Easy Profit: Tranching 328 Easy Banking: Regulations Repealed 329 Easy Investing: Credit Default Swaps 330 Hard Times 332 The Countrywide Story 334 Increased Credit Risk 336 Pay-Option ARM Loans 337 Countrywide's Misleading Description
of Loans in SEC Filings 338 Countrywide's Underestimation of Allowance for Loan Losses 338 Signals of Countrywide's Underestimation of Allowance for Loan Losses 348 Are They Living Happily Ever After? 348 Key
Terms 349 • Ethics at Work 349 • Ethics at Work 349 • Assignments 350 Case Study: TierOne Bank 354 Appendix 361 References 365 Glindex 383 059402 01 FM p001-024.indd 16 7/7/14 8:57 AM Preface About the Book Accounting fraud, or the manipulation of financial statements, has become an
increasingly s erious issue over the last two decades, leading to the collapse of ostensibly solid companies, exacerbating in an acute lack of confidence in financial markets and in the accuracy of financial statements. However, post Lehman, accounting rules have been changed. Ultimately, the accrual was re-
established and the $6.6 million attributable to the will-call payable was repaid to the insurance carriers" (AAER 1579, 2002). As shown in Table 9.3, the percent in 2005 to 0.65 percent in 2006. Assignments True/False Questions Answer the following questions with T
for true or F for false for more practice with key terms and concepts from this chapter. Prepare the journal entry in Bronto Company's books, accounting for the put option and specifying whether each account in the entry is a balance sheet item or an income statement item. (d) An asset's price increases faster than its earnings. Buca
conducted an initial public offering of its stock in 1999. "'Chainsaw Al' Now Aspires to be 'Al the Builder,'" Wall Street Journal. Ebbers and Sullivan became a duo on the path to mayhem. Our reserve for unfunded loan commitments at December 31, 2008 and $2.7 million, respectively, which represents potential future losses
associated with these unfunded commitments. (b) Increasing the amount of revenue it reported. Jones, Kenneth. Over the next few years, Enron was to offer dizzying numbers of stock options to its executives. Krim, Jonathan. • Edison is no longer listed on the NASDAQ. (2006) As we proceed from the major ethical theories of morality toward a
decisionmaking model and test the different approaches for their applicability or usefulness in relation to an ethical evaluation of all the options in a specific business dilemma, the likelihood increases that we will better discern what the right action is and why it is important to do what is right. Some of these loans were unethical in that they were
made at very low interest rates. The end of the Sprint merger was, in effect, the end of WorldCom. The misallocation of expenses as assets is known as the improper of expenses. To Kelly Morrison at GEX Publishing Services, many thanks for navigating this book through production so efficiently. 2011). By now, WorldCom was an inefficient mess.
Although it did not seem so at the time, "Rebecca Mark was one of the lucky ones—she got out at the top" (McLean & Elkind, 2004, p. 7/7/14 9:15 AM GLOSSARY/SUBJECT INDEX A AAER (Accounting and Auditing Enforcement Release) Abdelhak, Sherif, 206 Accountants demand for, 48 ethical decision-making models for, 58-60 Accounting and
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impairments, 208-209 of fictitious revenue, 128-129 of improper use of merger reserves, 169-170 of improper use of merger reserves and 169-170 of improper use of 
problems, 304-305 of overstatement of earnings, 265-272 of overstatement of sales, 121-122 of reducing cost of goods sold, 201-204 of underestimation of allowance for loan losses, 339-347 of understatement of sales, 121-122 of reducing cost of goods sold, 201-204 of understatement of earnings, 265-272 of understatement of expense
196-198 Accounting policies changes in, 131, 173-174, 198 slow asset write-off, 208 Accounts payable list, 197 Accounts receivable long-term, 289-290 net, 205 as percentage of revenue, 272, 273t as percentage of sales, 90-91, 93t, 121-122, 124, 128, 131, 306 sales of, 125 Acquisitions One business entity issues
stock or pays cash or other assets for the voting stock of another business entity. 2000, 2001, 2002. Chewco and JEDI were significant in two major ways. Sunbeam's stock began to plunge, falling $4 within minutes" (Byrne, 2003, pp. Comment on Sabre Company's timesinterest-earned ratio over the threeyear period as a signal of its ability to
continue to meet its interest payments. 41. The New York Times, on May 12, noted that in the analysts' meeting, "Mr. Dunlap attributed the 'early buy' debacle to everything from a marketing executive who approved 'stupid deals' with retailers to El Nino.... Signals of Fictitious Reporting Scheme #1—Understating Expenses and the Corresponding
Liabilities via Lack of Accrual Numerous signals can alert investors to the fictitious reporting scheme of simply omitting the recording of expenses in the current period. Om Malik (2003) clarified the misconception in his book Broadbandits by saying, "Think of 'Internet traffic doubles every 100 days' as an urban legend" (p. 13). Auditors cannot allow
their relationship with the people who appoint them to interfere with the special relationship they have with users of financial statements. Philosopher Stephen Cohen (2004) succinctly described the essence of modern consequentialism: "It is the effects, or consequences, that are morally significant, not intentions or rules or commitments." Of all
forms of moral analysis, utilitarianism is probably the most widespread, and many argue that it is the most intuitive approach to judging what action is right and what action is reporting some of its cash spent on operating expenses as cash invested in PPE or it is reporting some of its cash spent on operating expenses as cash invested in PPE or it is reporting some of its cash spent on operating expenses as cash invested in PPE or it is reporting some of its cash spent on operating expenses as cash invested in PPE or it is reporting some of its cash spent on operating expenses as cash invested in PPE or it is reporting some of its cash spent on operating expenses as cash invested in PPE or it is reporting some of its cash spent on operating expenses.
serious problems. usatoday.com. Schumer, Chairman. While guidance issued by the banking regulators referenced a credit score ("FICO score") at 660 or below. An ongoing investigation would have to determine the amount of
the restatements. The final principal payment of $100 became due in 2006, and as such, the note has been classified as current. (Quotes from Laing, 1998b, pp. To remain competitive, Countrywide jumped on the subprime bandwagon. The Report shows that of this amount, $198.7 million was to satisfy loans to Ebbers for other companies controlled
by him, $36.5 million was for a letter of credit used to support Mississippi College, $165 million was a personal loan to Ebbers, and $7.6 million was for interest on these loans. The California Power Exchange (CAL PX): Power had
to be bought and sold through CAL PX, which established hourly prices. Signal #4: CFFO Significantly Less Than Operating Income   The release of cookiejar reserves boosts operating income but does not produce cash flow. Dunlap was hired to do a turnaround at Nitec, which was in a bit of a slump. 3, 1-7. (Quotes from McLean & Elkind, 2004, p.
Each company was seemingly unconcerned about the fact that what each of them was doing was being done ten times over by their competitors. Explain how Navistar's accounting for its rebates differs from Rite Aid's improper accounting for its rebates. This scheme was so elaborate that the company needed to create a set of what
were known as "off-books" records in order to keep track of the prematurely shipped goods to ensure that they were later shipped from the warehouses to the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time, as originally requested by the customers at the appropriate time.
expertise to every step of the process, and I could not have company officers and directors. In 1997, the company aggressively negotiated with suppliers to secure rebates that applied to purchase contracts covering future periods
purchases. 90) were highly unrealistic. "My one wish is I had clarity of mind" (Taub, 2007, Jan. Easy Profit: Tranching Once Fannie Mae was given permission to buy conventional mortgages and securitize them, "all kinds of new mortgage companies that competed with banks and S&Ls [Savings and Loans] for mortgage
customers" (McLean & Nocera, 2010, p. (b) The earnings related to an asset increase sharply. January 19, 2005. 59) According to the Examiner's findings, Enron's cash flow from prepays in 1999 was $1.2 billion, which was greater than Enron's reported total CFFO. The Acquisitions Spree The three men who influenced WorldCom used the company
for their own convoluted reasons. 1993. Again, these are all telltale signs of returns waiting to happen. The misspelled Acquasition fittingly described his ego as well as his only real business strategy of collecting an increasingly out-of-focus conglomeration of companies. As each aircraft was sold, this average development cost was expensed and a
corresponding amount was written off the development-cost asset. What were the factors that led to such widespread allegations of accounting fraud? According to rumor, Lay explained his decision by saying that Borget would be kept in line. Van Voris, Bob, and David Glovin. After AT&T's breakup in 1984, MCI expanded astronomically under
McGowan's leadership, developing a huge fiber-optic network that supported the long-distance phone service that we all know. All it takes is a change in attitude. Improper Use of Restructuring and Other Liability Reserves. The crucial point is that he dragged WorldCom interests into his private activities by pledging his WorldCom stock to secure historia.
personal bank loans. In another instance (District B), the SEC alleged that the district "has paid Edison only $400,000 in FY 2002, even though Edison has recorded over $17 million in revenues from District B for the first two quarters of FY 2002, along with over $18 million in expenses" (AAER 1555, 2002). Sensormatic manufactures electronic
 security systems and is probably best known for its anti-shoplifting security devices. While the practice of investment bankers allocating some IPO shares to Ebbers was strikingly unusual. New York: Macmillan. (Quotes from Byrne, 2003, pp
Toxic mortgages, 38 Traceable fixed costs, 76 Fixed costs that exist because a particular business segment exists. In August 2002, he received up to 23 months in prison (Becker, 2002). From NAVISTAR'S 10-K 2003 NOTES, Page 58 Other Liabilities Major classifications of other liabilities at October 31 are as follows: Millions of dollars 2003 2002
Product liability and warranty Employee incentive programs Payroll, commissions and employee-related benefits Postretirement Postretirement benefits Postretirement Post
273 26 79 282 21 206 41 48 10 34 296 (continued) 059402 01 ch6 p191-225.indd 224 7/7/14 9:06 AM Chapter 6 • Abracadabra Millions of dollars 2003 2002 Other 270 1,466 (911) $ 555 260 1,576* (1,029) $ 547 Total other liabilities Less current portion Other long-term liabilities 225 *Author's Note: In the 2003 notes, there was a small change to
the 2002 Total other liabilities amount, as compared to the amount for Total other liabilities stated in the 2002 note. January 24, 2005. "What the Collapse of Peregrine Financial Says about the Sarbanes-Oxley Law," Huffington Post. Fastow selected Michael Kopper, an employee at Enron, to be the person who would "independently" run Chewco and
purportedly contribute the required 3 percent of the equity capital—amounting to $11.4 million—to Chewco. 108). Consolidated Statements of Cash Flows (in thousands) Year Ended September 30 Cash flows from operating activities: Depreciation and
amortization Stock-based compensation expense Goodwill impairment and write-off of inventory-related assets Deferred income tax provision (benefit) Tax benefit from stock transactions Equity in loss (earnings) of unconsolidated joint ventures Changes in operating
assets and liabilities: Increase in accounts receivable Increase in inventory Increase in trade accounts payable (Decrease)/increase in other liabilities Other changes Net cash used in operating activities Cash flows from investing activities: Capital expenditures
Investments in unconsolidated joint ventures Cash Distributions from and proceeds from term loan Repayment of term loan Borrowings under credit facilities Repayment of term loan Borrowings u
other notes payable Borrowings under senior and junior notes payable Debt issuance costs Proceeds from stock redeemed Treasury stock purchases Tax benefit from stock purchases Tax benefit f
41,487 - 772\ 352\ 9,229\ 11,945\ 130,235\ 5,511\ (54,631)\ 11,551\ (5,021)\ 5,844\ 8,374\ 7,381 - 3,180\ (22,740)\ 8,127\ (1,561) - (171,251)\ (430,345)\ (92,157)\ (19,462)\ (492)\ (92,342)\ 680\ (304,463)\ (91,306)\ (572,114) - (16,775)\ 18,336\ 199,076\ 1,333\ (84,263)\ (4,571)\ (413,705) - (16,828)\ (2,234)\ 123,210\ 1,837\ (73,719)\ (11,542)\ (49,458)\ (9,873)\ 4,655
(13,448) (40,619) -5,597 (10,271) (25,844) -5,639 (66,218) (48,470) (30,476) ---- (30,400) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) (439,700) 
351,703 (continued) 059402 01 ch3 p069-116.indd 114 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 115 Year Ended September 30 2006 (Decrease)/increase in cash equivalents at end of year Cash and cash equivalents at end of year Supplemental cash flow information: Interest paid Income
taxes paid Supplemental disclosure of non-cash activity: Increase in consolidated inventory not owned Land acquired through issuance of notes payable (134,528) 2005 2004 (23,782) 247,508 297,098 $ 162,570 320,880 $ 297,098 $ 162,570 320,880 $ 297,098 $ 111,501 $ 228,181 $ 79,088 $ 233,965 $ 65,237 $ 170,475 $ 164,540 $ 64,144 $ — $ 40,608 $ 111,501 $ 228,181 $ 79,088 $ 233,965 $ 65,237 $ 170,475 $ 164,540 $ 64,144 $ — $ 40,608 $ 111,501 $ 228,181 $ 79,088 $ 233,965 $ 65,237 $ 170,475 $ 164,540 $ 64,144 $ — $ 40,608 $ 111,501 $ 228,181 $ 79,088 $ 111,501 $ 228,181 $ 79,088 $ 233,965 $ 65,237 $ 170,475 $ 164,540 $ 64,144 $ — $ 40,608 $ 111,501 $ 228,181 $ 79,088 $ 111,501 $ 228,181 $ 79,088 $ 111,501 $ 228,181 $ 170,475 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,540 $ 164,54
188,585 $ 21,502 Extracts from FORM 10-K10 For the fiscal year ended September 30, 2005 Beazer Homes USA, Inc. • There was no SEC enforcement action or allegation of intentional wrong doing at Lockheed. In the recording of Krispy Kreme's roundtrip transactions, equipment sales were made to a franchisee shortly before the reacquisition of
the franchise and the sales price of the equipment was deducted from the reacquisition cost of the franchise. Lay's decision would come back to haunt him. This had the effect of decreasing Insignia's allowance for product returns, thereby increasing reported revenue" (AAER 1133, 1999). AAER 1542. By recharacterizing the Repo 105 transaction as allowance for product returns, thereby increasing reported revenue" (AAER 1133, 1999).
 "sale," Lehman removed the inventory from its balance sheet. WorldCom dropped to third place, and Enron's h bankruptcy fell to sixth on the list (Ovide, 2011). The Xerox Corporation is a multibillion-dollar Connecticut-based company that specializes in the production, sale, and lease of duplicating machines and services. Electricity trading worked
well for Enron because several of the fundamentals behind the successful trading of gas futures also worked for trading electricity futures. Subprime mortgage crisis, 38, 326-334, 348 Sullivan, Scott, 149, 154, 156, 158, 164-166, 174 Summers, Larry, 331 Sunbeam, 69-96 balance sheets, 92t carrot-and-stick approach at, 76-80 disintegration of, 85-
90 downsizing at, 74-76, 78, 85-86 Dunlap and, 70-80, 83-89 fictitious financial reporting schemes, 80-85 history of, 70-71 improper timing of revenue recognition, 80-84, 90-94 improper use of restructuring reserves, 84-85 7/7/14 9:17 AM 400 Glindex income statements, 92t outcomes for, 96 plant closings, 78-79 signals of fictitious schemes at,
90-95 Sunk costs, 207 A cost that has already been incurred and the expenditure cannot be reversed by any future decision or action. 111). (d) Act according to a maxim that harmonizes with a possible realm (i.e., a systematic union of different rational beings through common laws).
targets through the improper capitalization of expenses. The stock increase was based on fiction. • September 29, 1997. Signals of Fictitious Reporting Scheme #2—Understating Expenses was based on fiction. • September 29, 1997. Signals of Fictitious Reporting Scheme #2—Understating Expenses Here is an examination of some of the signals indicating that a company may have engaged in improper deferral of expenses. This
process of granting outrageous company loans was particularly rampant in the case of WorldCom; for example, in 2001, the WorldCom Compensation Committee authorized loans or loan guarantees to Ebbers for $150 million. This expense ostensibly is to anticipate some event in the future and to provide for it in the current period—that is, to set
 aside current-period profit and create a reserve now for when the expense, or liability, materializes in the future. July 14, 2003. A group of Buca's senior accounting personnel, including the assistant controller, the tax director, and Skrypek, met with Gadel in June 2003 to confront him about some of the accounting abuses identified above. • Respond
to the following Case Study Questions. Bureau of Prisons Website. For example, when it comes to the distribution of material goods, we can all see the necessity of providing 059402 01 ch2 p047-068.indd 57 7/7/14 8:59 AM 58 Chapter 2 • Ethics at Work disaster relief to those in need after a natural catastrophe, such as those affected by tornadoes
in Oklahoma or earthquakes in Mexico. • There were policies favorable to the parent company but detrimental to its franchisees, such as expecting "franchisees, such as expecting "franchisees to buy equipment and ingredients from headquarters at marked-up prices" (O'Sullivan, 2005). 43) Chapter Outline • Livent: Phantom of the Finances • Rite Aid: "The Keys to the Kingdom" •
Allegheny (AHERF): Trick or Treatment? When fraudulent financial statements are allowed to be presented after corrupt audits, this decreases confidence in the capital markets, which, in turn, makes it harder for American firms to raise capital either locally or internationally. This improperly reduced expenses and increased Beazer's earnings. Vinson
 Fictitious Financial Reporting Schemes • The Collapse of Wizard World • The Gatekeepers Who Failed WorldCom • Signals of the WorldCom Fraud • Key Terms • Ethics at Work • Assignments • Case Study: Tyco International, Ltd. 273-274). Weissmann, Jordan. Litigation Release No. 17627. With Rice and Hannon at the helm of EBS, Skilling
 believed that Enron would transform the telecom world. Surprisingly, despite this difficulty, Sensormatic's quarterly financial reports continued to meet analysts' earnings forecasts almost to the cent. "Status of High-Profile Corporate Scandals." November 23, 2005. Some students cannot be required to write more essays than other students or taken
 more tests or attend more class sessions. • Timothy Belden (a former head of Enron's energy trading) pleaded guilty "to engaging in a conspiracy that illegally manipulated the California power market." Belden "agreed to forfeit $2.1 million he maintained in two brokerage accounts at Charles Schwab" (Eichenwald & Richtel, 2002). www.lw.com
According to doughnut lore, a fresh Krispy Kreme is the ideal melt-in-your-mouth doughnut, with just the right chewy texture of freshly fried sugary dough drizzled with the perfect glaze. 059402 01 ch8 p292-324.indd 297 7/7/14 9:10 AM 298 Chapter 8 • Tall Tales In the criminal trial of founder John J. The crisis of 2008 shifted the focus of SEC
only when the owner died. Sunbeam's income statement showed a massive restructuring charge of $154.9 million in the last quarter of 1996 that included the over-accruals for items such as the advertising reserve and the litigation reserve. In spite of the glitches encountered implementing SOX, the reform was a rational response to problems that
endangered the fundamental stability of our capital markets. For the rest of Enron's business life, there would always be a tension within the company between those who wanted Enron to expand its "asset-lite" trading arm and those who wanted to consolidate its hard-asset pipeline business. • Timothy J. 228). After all the acquisitions, most
employees did not know what inventory WorldCom carried. January 3, 2008. In fact, Kopper received $1.6 million for managing Chewco. Gadel instructed the assistant controller to pay the former vice president of real estate a $100,000 "finder's fee" for two leases she had previously negotiated. Explain whether you can identify the signal that
TierOne's allowance for loan losses may allegedly have been understated. Nobody seemed to care, however, because the executives at Enron were imbued with a form of hysteria. 33-34) More ominous than the embarrassing name, Enron had another problem right from its inception—a problem that was concealed for years until it mushroomed into
monster. Who are the stakeholders? The next piece of the puzzle was for Fastow to determine what LJM1 would use for cash to buy the Rhythms stock from Enron. Some of these include the following: • Loans to Executives: Some of the most outrageous corporate looting prior to SOX occurred via a two-step loan process. And at Carlisle Plastics,
Carlisle management made entries to its books and records, at Tyco's post-acquisition earnings. Ebbers was accused of withholding information from WorldCom's board of directors as well as misleading them. If future power prices
rose above the $750 cap for power purchased from California, would this be a disincentive for the construction of power plants in California? Sensormatic's stock was used to finance acquisitions, and the stock price was sensitive to the company's revenue growth and to analysts' revenue and earnings estimates. Hence, a reserve is created for this
probable, expected future loss. 059402 01 ch5 p144-190.indd 169 7/7/14 9:04 AM 170 Chapter 5 • WorldCom Wizardry: From WorldCo
have a supernormal return on assets, it is a signal that the goodwill may be false because, in economic terms, goodwill is an ability to earn supernormal profits. Peregrine engaged in other deceptive practices to inflate the company's revenue, including entering into reciprocal transactions in which Peregrine engaged in other deceptive practices to inflate the company's revenue, including entering into reciprocal transactions in which Peregrine engaged in other deceptive practices to inflate the company's revenue, including entering into reciprocal transactions in which Peregrine engaged in other deceptive practices to inflate the company's revenue, including entering into reciprocal transactions in which Peregrine engaged in other deceptive practices to inflate the company's revenue, including entering into reciprocal transactions in which Peregrine engaged in other deceptive practices to inflate the company's revenue, including entering into reciprocal transactions in which Peregrine engaged in other deceptive practices to inflate the company's revenue, including entering into reciprocal transactions in which peregrine engaged in other deceptive practices to inflate the company's revenue, including entering into reciprocal transactions in the peregrine e
purchases of Peregrine software. Beazer's insufficient internal controls failed to prevent the recording of the fraudulent accounting entries in its general ledger and 059402 01 ch3 p069-116.indd 107 7/7/14 9:01 AM 108 Chapter 3 • The Sizzling Saga of Sunbeam caused Respondent to file with the Commission financial statements that failed to
conform with GAAP. Explain your answer. Second, "Enron often ended up guaranteeing some or all of the debt." Third, hugely optimistic assumptions were made at the beginning of the projects, assuming that little or nothing would go wrong. (2002, p. www.chron.com FASB Summary of Statement No. 167, 2009.
 www.stthomas.edu/cathstudies/cst/conferences/ Dayton/Daytonpapers.html. In an attempt to shore up the struggling company, Livengood tried to blame Krispy Kreme's problems on the growing popularity of low-carbohydrate diets; so the company announced that it was developing a "sugar-free doughnut" (O'Sullivan, 2005). AHERF's swift growth
came at the expense of large debt, and along with the debt came the pressure to appear financially stable. 7/7/14 9:10 AM Chapter 8 • Tall Tales b. • The utilities were required to fulfill their purchasing obligations on existing longterm contracts while selling at reduced fixed rates to customers. (b) Breaking a foreign country's law that prohibited
foreign companies from holding a majority of the stock in a telecommunications company. "Ultimately, you have to correct it. THE DEFENDANTS 9. John Finnis presents Kant's three formulations of the categorical imperative: 1. After Virtue: A Study in Moral Theory. 7/7/14 9:15 AM 380 References Chapter 9 "About Freddie Mac." 2012. In 2006, the
Dunlaps gave a substantial gift to Florida State University (Murphy & Ray, 2006). In 1999, American Software had to write off previously capitalized software costs.) It is important to note that for this particular fraud of misallocating expenses as fixed assets, CFFO lagging operating income is usually not as helpful as it is in uncovering other frauds.
To him, extremes in behavior or tastes were vices, whereas moderation—the golden mean—was the primary virtue. (The net asset value of a business entity's assets less the value of its liabilities and reserves.) Of this colossal amount, $28.2 billion was related to its acquisition of MCI. The
insurance companies stepped in to offer a different kind of derivative to keep the time bomb ticking. In 2000, the Company filed an amendment to the employment agreement that extended the terms of the contract through 2004. Dickey, Jonathan C., John H. The note to the financial statements showed that although delinquencies increased for the
risky pay-option loans, the allowance for loan losses as a percentage of all loans held for investment actually decreased. (d) One of the outside directors is an actor. • Describe CUC's method of reporting fictitious revenue. 059402_01_ch3_p069-116.indd 85 7/7/14 9:01 AM 86 Chapter 3 • The Sizzling Saga of Sunbeam This time, the stunning
magnitude of the planned cuts in jobs, plant facilities, and products shocked Wall Street. Alleging Billion Dollar Accounting Fraud The U.S. Securities and Exchange Commission today filed a settled civil injunctive action in the United States District Court for the Southern District of New York against Tyco International Ltd. In such a case, the spirit of the Southern District Court for the Southern District of New York against Tyco International Ltd. In such a case, the spirit of the Southern District Court for the Southern District Co
the law must always be communicated. Whenever goodwill, as a factor of earnings, increases dramatically over time with consecutive acquisitions, it is a sign to be very skeptical about a company's financial statements. When, in addition, the assets are growing at a faster rate than sales, some expenses probably are being reported as assets.
GlobalSecurity.org. Although regulation has its place in the business world, rules and laws without a sense of why they matter will always be problematic because there will always be those who look for loopholes in order to abide by the letter of the law, rather than the spirit of the law. An Overview of Livent's Fictitious Financial Reporting Schemes
Allegedly, Livent's manipulations were carefully orchestrated by senior management. Huffington Post published an article titled
 "Mortgage Stress Seen for '06; Delinquencies on Subprime Loans Likely to Spike, Report Says" (Downey). The fear factor was firmly in place. However, the department was set up with a flawed focus and was not truly independent. The methods by which Madoff engaged in tax fraud included the following: • Madoff received approximately
$15,700,000 from Bernard L. What ethical system will Eva be using to make her decision? Lockheed's delay in writing off the impaired asset caused both assets and earnings management reaching its greatest level in the fourth quarter of that
year (AAER 1393, 2001). Florence E. September 10, 2006. The Executive Summary of the Sarbanes-Oxley Act presents guidelines for CEOs and CFOs who are required to certify the following: • The report does not contain untrue statements or material omissions. One of the loans included in Sloppy Mortgage Corporation's loans at January 1, 2006,
was a pay-option ARM loan of $900,000 taken out on January 1, 2006, when the value of the house was $900,000. January 2, 2006. 178, 187). Others started to believe that they were immune to mundane rules and regulations. Cianci.
growth" ("Summary of Independent Investigation," 2005, p. "The final judgments, entered pursuant to Gadel's and Skrypek's consents, permanently enjoin them from violating Section 17(a) of the Securities Act of 1934 (Exchange Act of 1934 (Exchange Act) and Rules 10b-5, 13b2-1
13b2-2, 14a-3, and 14a-9 thereunder and from aiding and abetting violations of Sections 13(a), 13(b)(2)(B) of the Exchange Act and Rules 12b-20, 13a-1, and 13a13 thereunder without admitting or denying the
Commissioner's findings." As set out in AAER 1495. Gadel and Micatrotto showed little regard for sound corporate governance and helped create an environment that was conducive to fraud. It may be helpful for us to consider the special rights and duties that our particular relationships with specific persons demand. Mandatory rotation of auditors
could have prevented them from losing their independence in at least two ways: First, the forced rotation would have precluded the audit firms from building too much familiarity. "The 10 Largest U.S. Bankruptcies," CNNMoney. For the preparation of Bolt's December 31 financial statements, which of the following is correct? (b) Ended the
prevention of commercial banks from trading in securities. Practical Ethics. Skrypek routinely approved Gadel's improper reimbursement requests. That same day the CFO, Scott Sullivan, and the controller, David Myers, were asked to resign. 7/7/14 9:15 AM 378 References AAER No. 2765. In Sunbeam's case, the SEC found that "in total, $24.7
million in fourth quarter [1997] sales to distributors were subject to rights of return" (AAER 1393, 2001). The statutory maximum sentences for each of the charged offenses are set forth in the attached chart. www.denverpost.com. "UC Reaches $168-Million Settlement with Enron Directors in Securities Fraud Case." January 7, 2005. The goods were subject to rights of return" (AAER 1393, 2001).
received by the retail customer on December 30 and were on the customer's shelves and available for sale on January 2. 84). June 29, 2009. At the meeting, the directors found no comfort from the answers they received about the accounting numbers or about the strength of the current quarter. In its tenth year of operating, its total sales for year 10
amounted to $100 million. While it is difficult to pinpoint exactly when Enron crossed the line from legal to fraudulent financial accounting, Fastow's next step must have been one of the first in that direction: Fastow constructed an SPE to buy CALPERS' half of JEDI. Furthermore, because the divisions were under pressure to meet sales growth
targets and the sales staff wanted commissions, sales often were made at below cost. 059402 01 ch6 p191-225.indd 223 7/7/14 9:06 AM 224 Chapter 6 • Abracadabra From NAVISTAR's 10-K 2002 Plan of Restructuring charges, the company has recorded
nonrecurring charges of $170 million primarily related to the company's V-6 diesel engine program with Ford. 059402_01_ch9_p325-360.indd 344 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 345 December 31 2005 2004 (In thousands) Original loan-to-value ratio (1) Original combined loan-to-value ratio (2) Average original FICO score
Delinquencies (3) 75% 78% 720 0.22% 73% 75% 730 0.08% (1) The ratio of the lower of the amount of the lower of the amount of the lower of the amount of the lower of the property to the amount of the lower of the amount of the lower of the property to the amount of the lower of the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the amount of the lower of the property to the property to the amount of the lower of the property to the amount of the lower of the property to th
Accounting Fraud 39 The Financial Crisis Inquiry Report (2011), published by the National Commission on the Causes of the Financial and Economic Crisis in the United States, came to the following conclusions: • We conclude this financial crisis was avoidable. The purpose of JEDI was to invest in energy projects. Ethics is fundamental to the
securities laws, and I believe ethical culture objectives should be central to an effective regulatory compliance program. (a) Krispy Kreme engaged in contrived equipment sales to franchisees. In some situations, one may see merit, contribution, or effort as paramount.
Clearly, this policy encouraged large projects that might not be prudent. (par. In the case of Edison, the SEC alleged: "In its filings with the Commission, Edison has not disclosed the existence and amounts of these District-Paid Expenses. In October 2013, the SEC awarded over $14 million to a whistleblower: The whistleblower, who does not wish to
be identified, provided original information and assistance that allowed the SEC to investigate an enforcement matter more quickly than otherwise would have been possible. Enron's SPE Whitewing was used to borrow money that was paid to Enron for Whitewing's purchase of Enron assets, and Enron recorded the cash received as cash flow from
operating activities. 167). 059402 01 ch7 p226-291.indd 226 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 227 • Related-party management fees • Contrived put options purporting to lock in profits on investments in shares • Mark-to-market revaluations of assets via references to contrived sales to these contrived entities
 Recognition of profits on its own stock that was issued to off-balance-sheet entities 3. Ford is seeking to cancel the V-6 supply contract. That was the improper use of non-GAAP measures. To fight the rampant fraud revealed by the
2008 crisis, President Obama established the Financial Fraud Enforcement Task 059402_01_ch1_p025-046.indd 39 7/7/14 8:58 AM 40 Chapter 1 • Introduction to the Problem of Accounting Fraud Force in November 2009. Investment Bankers Thornburgh, WorldCom's Bankruptcy Examiner, also criticized WorldCom's investment banker, Salomon
Smith Barney (SSB), and its star analyst, Jack Grubman. Therefore, under this approach to the decision-making model, when you are faced with an ethical dilemma in a business environment, it is vital to identify all of the stakeholders in the decision; that is, you should consider everyone who might be affected by the decision. Since 2001, goodwill
need not be amortized at all unless it becomes impaired. Act only according to that maxim by which you can at the same time will that it should become a universal law. Throughout 1997, Sunbeam overstated earnings by releasing parts of these overstated earnings by releasing parts of the parts of t
47 7/7/14 8:59 AM 48 Chapter 2 • Ethics at Work Everything that counts does not necessarily be counted does not necessarily be counted. In fairness, Ebbers tried to get the entire WorldCom hodgepodge onto a shoestring budget—except, of course, his own hundreds of millions of dollars of compensation
059402 01 ch5 p144-190.indd 156 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to the signals of those misstatements will strengthen the overall alert for this method of understatement of expenses. United States
Bankruptcy Court Southern District of New York in re: WorldCom Inc. Senator Charles E. The company had a particularly toxic mix of these loans. In other words, the accounts receivable asset will not turn into a cash asset. Bribery is difficult to identify in financial statements. (d) Operating income will increase by $5,000. "Krispy
Kreme COO Tate Leaving the Company." August 16, 2004. The house immediately went into foreclosure, and the house quickly sold for $700,000. Scheme #1: Holding Books Open after the Close of a Reporting Period The SOX Report, which examined all the SEC Enforcement Actions for July 31, 1997, through July 30, 2003, found 25 enforcement
actions in this period "involving the failure of issuers to close their books properly at the close of a reporting period" (2002, p. According to AAER 1017, at Sensormatic shortly before midnight on the last day of the quarter, the computer system that and shipments was manipulated to change the date and time on the computer clock. Of this,
$49.8 billion of goodwill was comprised of payments for acquired companies in excess of the acquired assets or by anticipating liabilities. April 26, 2002. ** sales to customers. This section serves to describe the company's financia
health and the results of its operations to help users gain a better understanding of the company's financial statements. news.com/BellSouth. For example, while factory farms are not illegal, certain beef-producing companies may believe that they have a moral right to provide more natural living conditions for their animals. T 059402_01_ch5_p144-
190 indd 175 F 3. "Utility Exposes Enron Green at Its Core," Washington Post. In the 1990s, ECT developed guickly from a small trading department into a large and highly profitable division. Report of Investigation by the Special Investigation by the Special Investigation of Directors of Enron Corp. Livent arranged for outside associates to purchase
                                                                                                                                                                                      _. With the innovation of electricity, it began producing toasters and irons and changed its name to Sunbeam Corp. Eva reflects carefully before she answers the managing partner. Signal #3: Deferred Revenue Decreases as a
Percentage of Total Revenues In a company that sells membership subscriptions, deferred revenue decreasing as a percentage of total revenue is an indication that the company may be aggressively recognizing subscription revenues that will actually be earned only in future periods. (b) Nothing in the preceding description of the transaction
indicates that Pull Company had a substantial business purpose for ordering the goods on a bill and hold basis. "Krispy Kreme Doughnuts Inc. Just Ask Him." Fortune. How could closing so many factories lead to increased production and sales? F Fill-in-the-Blank Questions Fill in the blanks with information and concepts from this chapter. in
November 2001 and was removed from the New York Stock Exchange because "fewer than 600,000 shares remain[ed] publicly held" (NYSE, 2001). If word got out that Enron was short this amount, other dealers would buy up the spot oil, driving up the price, and Enron was short this amount, other dealers would buy up the spot oil, driving up the price, and Enron was short this amount, other dealers would buy up the spot oil, driving up the price, and Enron was short this amount, other dealers would buy up the spot oil, driving up the price, and Enron was short this amount, other dealers would buy up the spot oil, driving up the price, and Enron was short this amount, other dealers would buy up the spot oil, driving up t
and McIntosh directed R&Q to include anticipated vendor reimbursements in the warranty reserve calculation despite the lack of any specific language in the vendor contracts providing for such recoveries. Scheme #1: Improper Use of Multiple-Element Contracts or Bundled Contracts The major offending accounting actions in the SEC complaint
were concerned with Xerox's treatment of its lease contracts. The second broad consideration, I believe, is to have a good compliance and ethics program tailored to address the conflicts of interest the firm has identified and *The Securities and Exchange Commission, as a matter of policy, disclaims responsibility for any private statements by its
employees. March 27, 2012. As a result, Sidgmore led UUNet to accept a buyout offer from MFS Communications on August 12, 1996. The SOX Report (2002) found 80 enforcement matters in which improper revenue recognition involving fictitious revenue
occurred: "The manipulation of revenue was accomplished through, among other means, the falsification of sales documents with customers that were not recorded, and top-side adjustments by senior management" (p. Hays, Kristen. Likewise, Buca never disclosed a series of related-party transactions involving Gadel in its financial
statements or proxy statements. 66) Furthermore, the Bankruptcy Examiner concluded: Enron should have accounted for the Prepay Transactions as debt rather than as price risk management activities, and . . . As set out in AAER 1133, 1999. Lockheed is presented in this chapter mainly as an example of: (a) Failure to record asset impairments. The
unintended consequences of cutting costs to increase short-term profits can easily cause long-term losses. Managers simply couldn't achieve the unrealistic numbers, but they felt there would be repercussions if they didn't agree to them. Purchase of Inventory—The Company has entered into a vendor relationship with Parasole whereby the Company
purchases bread products and a majority of the dessert products offered at the Company's Minneapolis-Saint Paul metropolitan area restaurants. The SEC states that senior management provided "approximate dollar adjustments that they [i.e. staff] were required to make to various accounts in the balance sheet and income statement, including
 expense categories, specific shows and fixedasset accounts." In addition, the SEC found that Drabinsky, Livent's former CEO, and Gottlieb, the company's former president, "... from at least 1994 through the first quarter of 1998 ... engaged in a deliberate manipulation of Livent's books and records." As a result of these manipulations, which were
orchestrated together with other officers and employees of the company, expenses were understated for the purpose of inflating profits. The banks alleged that their risks in loans they had securitized and in CDSs that were understated for the purpose of inflating profits. The banks alleged that their risks in loans they had securitized and in CDSs that were understated for the purpose of inflating profits.
used herein are the property of their respective owners. LR 19719. It is calculated by adding back interest and taxation expense to net income and dividing that amount by the entity's interest expense. As previously mentioned, post Enron, accounting for SPEs was updated by the Financial Accounting Standards Board Interpretation FIN 46 (R) as
 amended by FASB No. 167 (2009). 059402_01_ch7_p226-291.indd 270 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the securitizations signal for Xerox, as discussed in Chapter 7 • Enron and the Tale of the Golden Goose 271 (As a case in point, the Securitization Securit
time, Enron's accounts receivable and its PRMA grew as a percentage of revenues," respectively. Table 4.1 summarizes Sensormatic's misstatements over a two-year period. The two major accounting for contracts in progress. Further, in
 June 1996, a sale of $750,000 with a 60-day right of return was recognized without an allowance for returns. • Identify and explain the general signals of Enron's overstatement of earnings, overstatement of ear
 June 13, Fannin and the outside directors met secretly. Schapiro cited the conclusion of the Bankruptcy Examiner's Report that Lehman's "motive for the transactions was ultimately to reduce its leverage: to temporally remove tens of billions of dollars in assets from its balance sheet at the end of financial reporting periods and use the cash to pay
down liabilities as a means to reduce its reported leverage2" (p. Dunlap "cut him off and accused him of not knowing the details of his businesses." Dunlap snapped at anybody who hesitated. The deontologist chooses moral action not because of its consequences, but because it is the right thing to do. Simon, Bernard. "Former Rite Aid Vice Chairman
Sentenced to 10 Years in Fraud Case," The Daily Item. Ben Campbell, the prosecutor at this trial, pointed out that "EBS' highly touted core software packages never worked properly and failed to generate much income" ("Enron Defendants Not Guilty for Charges," 2005). xxii) 7 8 OSHA is the Occupational Safety and Health Administration Division income" ("Enron Defendants Not Guilty for Charges," 2005). xxii) 7 8 OSHA is the Occupational Safety and Health Administration Division income" ("Enron Defendants Not Guilty for Charges," 2005). xxii) 7 8 OSHA is the Occupational Safety and Health Administration Division income" ("Enron Defendants Not Guilty for Charges," 2005). xxii) 7 8 OSHA is the Occupational Safety and Health Administration Division income" ("Enron Defendants Not Guilty for Charges," 2005). xxii) 7 8 OSHA is the Occupational Safety and Health Administration Division income "Enron Defendants" ("Enron Defendants") and Health Administration Division income "Enron Defendants" ("Enron Defendants") and Health Administration Division income "Enron Defendants" ("Enron Defendants") and Health Administration Division income "Enron Defendants" ("Enron Defendants") and Health Administration Division income "Enron Defendants" ("Enron Defendants") and Health Administration Division income "Enron Defendants" ("Enron Defendants") and Health Administration Defendants ("Enron Defendants") and H
the United States Department of Labor. January 30, 2007. A few days after the new quarter began, Lehman would borrow the necessary funds to repay the cash borrowing plus interest, repurchase the securities, and restore the assets to its balance sheet. United States Bankruptcy Court Southern District of New York in re:WorldCom Inc. Taking
 advantage of problems in public schools throughout the United States, Edison Schools, headquartered in New York City, was founded on the premise that privatesector corporations could run public schools more efficiently and effectively. "Enron Trader Pleads Guilty to Conspiracy," New York Times. The SOX Report (2002) found that this method of
                expense recognition accounted for 25 SEC enforcement matters in the study period. 278) The entries, which were passed after the close of each quarter, amounted to $3.8 billion, mainly reducing line costs and overstating property, plant, and equipment (PPE) over the period January 2001 to March 2002. 113. Amended Complaint Chargin
Five Enron Executives with Fraud and Insider Trading Relating to Enron's Broadband Subsidiary. On the other hand, Vince Kaminski, Enron's chief research analyst (who had an MBA and a PhD in mathematical economics) was shocked to discover this hedge maneuver. Calculate the sales/PPE ratio for quarters 1-4. • Read the Accounting and
Auditing Enforcement Release (AAER 2884) for Beazer Homes, 6 given below. However, the SEC reported that because such sales were a significant change in approach for Sunbeam and the likely return amounts were not known, it should not have reported these sales. Trading of Livent stock was suspended, and when trading briefly recommenced
after the restatement, Livent's stock "plummeted 059402_01_ch6_p191-225.indd 195 7/7/14 9:05 AM 196 Chapter 6 • Abracadabra over ninety-five percent from $6.75 (US) per share to approximately $0.28 cents per share and business journalists
adopted an increasingly skeptical attitude toward Enron's financial statements. 62). Scheme #1: Improper Use of Merger Reserves WorldCom's favored method of creating false reserves was on the acquisition of companies. 059402 01 ch6 p191-225.indd 208 7/7/14 9:06 AM Chapter 6 • Abracadabra 209 Signal #5: Unusual Restructuring
Charges Restructuring charges in a current period can indicate that the company failed to recognize impairments of assets in previous periods. Furthermore, duty-based ethics may seem somewhat lacking to those who regard motivation as a crucial factor in ethical decision making. 5). (b) Tax reserves. Signal #7: Straying from Core Business
When a company misrepresents the nature of its core business or when a large portion of its profit is dependent on a type of business that is not its core business that is not its core business or when a large portion of its profit is dependent on a type of business that is not its core business that is not its core business, it should be regarded as a signal that the company's ability to maintain its earnings is more risky than it wants to disclose. Signals of Adelphia's Fictitious Reporting Schemes A number of
signals could have alerted readers to the schemes that Adelphia was using to present the company in a more positive light. Capital expenditure changes one asset, cash, into another asset.) But if Sullivan did not want to own up to the scheme that the cycle of acquisitions had been paid for with overpriced WorldCom stock based on overstated
earnings, what else could he do? Key Terms Cost of goods sold 199 Days' sales in inventory 203 Improper deferral of expenses 192 Improper expenses 192 Improper expenses 192 Improper expenses 192 Improper deferral of expenses 193 Improper expenses 193 Improper expenses 194 Improper expenses 195 Improper deferral of expenses 195 Improper expenses 195 Improper expenses 195 Improper expenses 196 Improper expenses 196 Improper expenses 197 Improper expenses 197 Improper expenses 198 Improper expenses 199 I
the Rite Aid Crisis" by Anne Federwisch. By the following year, the banking industry had successfully lobbied Congress to scrap Glass-Steagall, and in November 1999, the Financial Services Modernization Act was passed. The original Krispy Kreme company, founded by Vernon Rudolph in North Carolina in 1937, slowly developed a small string of
franchises with what has been described as "an almost legendary product and a loyal customer base" (O'Sullivan, 2005). That was the day that Sunbeam announced the actual details of the massive downsizing. Enron would use the infamous 059402_01_ch7_p226-291.indd 234 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 235
system of prepays to facilitate overstatement of earnings and cash flow by essentially borrowing against future receipts for future deliveries of commodities and related party transactions. ORDER INSTITUTING CEASE-AND DESIST PROCEEDINGS PURSUANT TO SECTION 8A OF THE SECURITIES ACT OF 1933 AND SECTION 21C OF THE
SECURITIES EXCHANGE ACT OF 1934, MAKING FINDINGS, AND IMPOSING A CEASE-AND-DESIST ORDER I. White's leaving represented one of the unintentional consequences of indiscriminate downsizing: Due to "declining morale," the most talented employees leave. Scheme #4: Recognizing "FOB Destination" Sales at the Time of Shipment
When a sales order stipulates "FOB destination," it means that there is a sales agreement specifying that ownership passes to the customer only when the purchased goods arrive at their destination. PCAOB (Public Company Accounting Oversight Board), 34, 35, 37 Pember, Anne, 129 Peregrine Systems, Inc., 38, 135-143 Perelman, Ron, 89, 96 Perry,
Lee Tom, 75 Petty, George, 73 Polverari, Mary Sattler, 126, 127, 129 Potential employees, 54 Powers Report, 248, 249, 251, 252, 256-257, 260-261 PPE (property, plant, and equipment), 170-172 Premature revenue recognition, 121 The process of formally recording a revenue item in the financial statements in an earlier period than the period in
which the item should have been recorded. New York Stock Exchange, 373 U.S. 341, 366 (1963). Insurance companies such as AIG and some investment banks began to write instruments that gave the holder of the instrument to Rise
Again for Livent at OSC." Financial Post. I'm no different than you. Kirk Shelton Is Guilty," 2005). This was not an isolated problem. In 1990, Skilling left McKinsey & Company to join Enron as chairman and CEO of a new division known as Enron Finance. unconsolidated affiliates especially partnerships, trusts, joint ventures, and company-sponsored
corporations as opposed to established independent corporations. www. The company system then falsely recorded shipments as having occurred on the last day of the prior quarter (AAER 1017, 1998). • Read the extracts from the SEC Complaint filed on June 7, 2006, against the former chief financial officer and the former controller of Buca, Inc.
Restate the company's income state- ment for the year, taking the creation of the restructuring reserve into account and assuming that it does not change the company's income tax expense. The city had given Sunbeam the rent-free use of the building for the plant. Skilling chuckled over California's plight while schools and companies closed down
during rolling blackouts and Pacific Gas and Electric filed for bankruptcy. "Mass. • October 26, 1997. CONSOLIDATED STATEMENTS OF OPERATIONS (IN THOUSANDS, EXCEPT PER SHARE AMOUNTS) YEAR ENDED MARCH 31, 2001 Revenues: Licenses Services Total revenues Costs and Expenses: Cost of licenses Cost of services Amortization
of purchased technology 2000 1999 $ 354,610 210,073 564,683 $168,467 84,833 253,300 $ 87,362 50,701 138,063 2,582 111,165 11,844 1,426 51,441 1,338 1,020 31,561 50 (continued) 12 Extracted from 10-K filings for Peregrine Systems, Inc. In respect of Enron's SPEs Chewco and Jedi, the Powers Report identified three sources of fictitious
income streams: a fee, management fees, and revenue recognized on Enron's own stock. The board was looking for a replacement for its CEO, Roger Schipke, who was considered too placid to provide the assertive leadership that the troubled company needed. (c) When a note to the financial statements on "Related Party Transactions" refers to
transactions with unconsolidated, specially constructed entities such as partnerships or trusts. • Stricter regulations for credit rating agencies. Jenkins, Carri P. S. See if a clear decision is evident. The company estimated the total number of TriStar aircraft that it would sell and then calculated an average
development cost per airplane. Cooper and Smith then questioned David Myers, the controller, who acknowledged that he had known about the incorrect accounting. Kenneth Lay—indeed the whole gas industry—needed someone who could figure out a way to make the deregulated gas industry profitable. The problem is you have no way of telling
precisely who is going to be affected." (Qtd. • They transferred production costs to fixed assets. Bush had named him) worried too much about the existence of debt—it was the appearance of debt that he did not like. www.cnnmoney.com. The credit balances in land inventory accounts were debited, i.e., zeroed out, and a cost of sales expense
credited, i.e., reduced. On May 24, 1999, Belden negotiated a deal to sell 2,900 megawatts of power to CAL PX, and "he identified a transmission route called Silverpeak as the means for getting the electricity to the state" (McLean & Elkind, 2004, p. Clearly, EBS would not let a little obstacle like the falling price of fiber capacity mess up its rosy
picture of growth. What is the ethical evaluation of the alternatives? (a) The company concealed rampant selfdealing by the family that founded and controlled Adelphia. Therefore, senior management was highly motivated to communicate positive information on Sensormatic's financial position and prospects to stock analysts. Enron had just received
$330 million cash and had to repay $394 million. If XYZ goes ahead and secures the backdated order and recognizes it as a bill and hold sale in its December 31 financial statements, which of the following is correct? Schilit, Howard. This "due diligence" study had picked up on the fact that major Sunbeam customers were overstocked with Sunbeam
inventories and that Sunbeam's sales were going very slowly in the first guarter of 1998. The Independent System Operator (ISO): When there were emergency energy shortages, power had to be purchased and sold though ISO auctions, subject to 2 Information on these rules is from Swartz and Watkins (2003, p. Signal #4: Accounting Policy
Indicating Slow Asset Write-Off Accounting pol- icy notes to the financial statements indicating that the company has a policy that is slower than other companies in the industry to write off assets—such as development costs or start-up costs—should alert the reader to the possibility that the company is aggressive in its efforts to overstate the value
of assets. The recoveries could include . . . disgorgement for the fees WorldCom made this payment by taking on billions of
dollars of more debt. (d) Incorrectly describing payments to a lobbyist as consulting services. However, because Mariner Energy was a private company, it had no verifiable market price. Signal #3: Increase in Accounts Receivable as a Percentage of total current assets,
it could be a signal that the company is not writing off bad debts or is not appropriately estimating its reserve for doubtful debts. alleged: "The Defendants Materially Overstate Basin's Q2 2007 And Year-To-Date Revenues By Engaging In A Sham $3.8 Million Sale To A Special Purpose Entity They Directly Or Indirectly Cause To Be Created" (section
F). After the AT&T breakup, LDDS wasn't the only company to get the idea of long-distance discounting. Panella, Special Agent in Charge for the New York Regional Office of the U.S. Department of Labor's Office of the New York Regional Office of the U.S. Department of Labor's Office of the New York Regional Office of the U.S. Department of Labor's Office of Labor Regional Office Offi
York Regional Office of the U.S. Department of Labor, Employee Benefits Security Administration (DOL-EBSA), announced that Peter Madoff, the former chief compliance officer and senior managing director of Bernard L. With its Prepay Transactions, Enron would enter into a contract to deliver a commodity in the future at a specified price.
Unconfirmed rumors had swirled for a while that Ebbers, the pious Sunday school teacher, had been having an affair. Having pushed ahead with cutting jobs and closing plants, Dunlap began to apply his trademark brand of motivation—the fear and the dreams of stock option riches—to put the pressure on management. However, the accounting and
financial problems were "solved" with the help of Andrew Fastow's SPE named LJM2. However, this did not happen in spite of Mark's optimism and her large development teams. The complaint alleges that Tyco inflated its operating income by $567 million from its fiscal year 1998 through its fiscal quarter ended December 31, 2002, by means of
connection fees that Tyco's ADT Security Services, Inc. He completed his three-year military obligation, during which time he married Gwyn Donnelly when he was 24 and she was 19. www.securitiesdocket.com. From here on, mortgage loans issued with dubious credit, MBSs, CDOs, and CDSs took off on a steep trajectory. Here, as distinct from
utilitarian or deontological theory, the most important issue in morality is having the right set of dispositions or virtues. (Parasole), to provide for certain management and administrative services. "If you lose you lose, and if you win you lose because the house can't pay your winnings" (qtd. Case No. 04 CV 2002 JAH (RBB). December 21, 1970. This
signal ought to have alerted users of the financial statements to the possibility that, eventually, Lockheed would have to recognize a huge expense to write off this asset. In early 2001, Enron's entire international division was sold. Enron was in such a rush to complete the purchase that most of the deal was accomplished in four days and "most of it
done with heavy drinking in London bars" (McLean & Elkind, 2004, p. In the criminal trial of founder John J. At your two-year review, she recommends you for promotion. In fact, it is even possible to sell that contract today on the futures market and receive the market price in cash. U.S. Securities and Exchange Commission Accounting and Auditing
Enforcement Release, June 30, 2000. has a loan portfolio with the following loans at December 31, 2013: 1% of (loan principal plus accumulated negative amortization) $1 million Accumulated negative amortization at beginning of 2006 (none of this was paid during the year) What is the amount of loans held for investment net of allowance for loan
losses on the balance sheet at December 31, 2006? 059402 01 ch6 p191-225 indd 219 7/7/14 9:06 AM 220 Chapter 6 • Abracadabra warranty reserve. However, there are other reasons that are not guite so apparent. These loans became known as subprime loans are loans with a higher risk of default are not guite so apparent.
Furthermore, Skilling's angry response to Grubman alerted everyone on that conference call to the fact that something sinister lay behind the late financial statements. Assignments True/False Questions Answer the following questions with T for true or F for false for more practice with key terms and concepts from this chapter. What was Ruby's
operating income for last year (ignoring taxes)? (c) The transactions resulted in the reporting of overstated net income. President Obama established the interagency Financial Fraud Enforcement Task Force to wage an aggressive, coordinated, and proactive effort to investigate and prosecute financial crimes. New York: Berkley Books. Kopper later
disclosed that the buy-back provision had even been included in drafts of the original Cuiába sale documents. • Countrywide, once the largest mortgage company in the United States, was acquired by its customers were based
on guesswork and excessively optimistic assumptions. However, a bank that was doing business with Borget became suspicious and contacted Enron. 059402 01 ch3 p069-116.indd 89 7/7/14 9:01 AM 90 Chapter 3 • The Sizzling Saga of Sunbeam Although Jerry Levin did a valiant job in attempting to reverse the destruction of Sunbeam, the
company filed for Chapter 11 bankruptcy protection in 2001, after suffering heavy losses in the previous year. "Larry Fink's $12 Trillion Shadow," Vanity Fair. Buca, Inc. Galbraith, p. Boston: McGraw-Hill/Irwin. First, the investment bank allocated huge amounts of initial public offering (IPO) shares to him when it took other companies public; second
Salomon favored Ebbers by providing him with unusual financial assistance. (c) An asset's price and its earnings increase sharply. 279) However, whether Arthur Andersen should have revealed irregular entries is another matter. If you were to write journal entries to describe how
Rite Aid and Navistar improperly accounted for the rebates, which accounts would be debited and credited in the books or ledger of each company? T F 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom t
makes a number of acquisitions also creates significant reserves. Partington, Richard. Essentially, via contrived sales with an SPE, Enron gave itself revenue that would simply be eliminated upon consolidation of the SPE's financial statements with Enron's 059402 01 ch7 p226-291.indd 254 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the
Golden Goose 255 financial statements. 18-19). At that point, Fastow decided that LJM1 would agree to "purchase" the Rhythms shares at a specific, profitable price on a future date. Revenue Recognition Project Updated July 2013. "Al Dunlap's Disgrace," Australian Financial Review. Undisclosed related-party trans- actions. wsj.com/home-page.
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, former CEO of Countrywide, settled an SEC civil fraud case for $67.5 million in October 2010. October 23, 2002. The SOX Report (2002) stated, "Inadequate disclosure matters may involve situations where the issuer's financial statements
are in conformity with GAAP, but fail in some material way to present an accurate picture of the issuer's financial condition." Edison's Fictitious Financial Reporting Scheme via Inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the case of Edison Schools, Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure In the Contract Inc., the area of inadequate Disclosure Inc.,
Lay's criminal trial in early 2006, his attorney would lament the fact that the banks had wanted their loans to be repaid and argued that if the banks had not made this inconvenient request, Enron would still be in business.) It is unlikely that Kenneth Lay, or "Kenny boy" (as then Texas Governor George W. Scheme #3: Improper Capitalization of
Expenses As an example of improper capitalization of expenses, Livent also transferred preproduction costs for shows to fixed asset accounts, such as those for construction of theaters. Federal prosecutors reportedly determined that Mozilo's actions "did not amount to criminal wrongdoing" (Reckard, 2011). 2003. Norris, Floyd, and Diana B. A
reserve for such returns should be accounted for in the financial statements according to the Financial Accounting Standards Board's SFAS 484. He was "found guilty of conspiracy and 15 counts of securities fraud and two counts of bank fraud" (Crawford & Dunbar, 2004). The third factor is that the organization use reasonable efforts to exclude
from any position of leadership any individual who has engaged in conduct inconsistent with an effective compliance and ethics program—in other words, that the fox is not guarding the henhouse. While in the case of Adelphia all seven elements appear to have been neglected, in your opinion, which three of the elements discussed by di Florio would
have been most useful in preventing the improper business practices at Adelphia? There's never been a technology model with such an extraordinary rate of growth like this before." (Quotes from Malik, 2003, pp. This occurred after Xerox Brazil changed its emphasis from sales-type leases to operating leases. What if the market price the utilities had
to pay for the power went above the fixed price at which they were forced to sell the power? Witter, Lon. (c) Recording of fictitious revenue. Xerox sold accounts receivable without disclosing it immediately. In April 2012, the Supreme Court rejected another appeal by Skilling (Lattman, 2012). Sensormatic's overstatement of earnings via holding its
books open after the close of a reporting period is an example of: (a) Recording fictitious revenue. Rumors of problems in the company began seeping into the media. 2002. However, behind this fantasy, Whitewing was borrowing money to transfer to Enron in such a manner as to disguise the loan as the sale of Enron assets. Instructed by the financial
meltdown of 2008, we now know that if a lender's allowance for loan losses does not increase significantly when house prices stall or begin to fall, it is a strong signal that the allowance for loan losses is underestimated. Signal #2: Cash Flow from Operations Falling Behind Operating Income The second signal of inappropriately recorded sales is
when cash flow from operations (CFFO) lags or falls behind operating income or net income. www.sec.gov 059402 01 ch5 p144-190.indd 184 7/7/14 9:04 AM 185 Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom Wizardry: From WorldCom Wizardry: F
financing activities Net increase in cash and cash equivalents CASH AND CASH EQUIVALENTS AT ENDED SEPTEMBER 30, SEPTEMBER
Reversals 6. 1) The Countrywide Story3 To a large extent, the journey of Countrywide Financial Corporation, from its inception in 1969 to its collapse in 2007 and its purchase by Bank of America in 2008, mirrors the evolution of the mortgage industry. By the end, Whitewing owed $2.43 billion in respect of the Osprey notes. However, while legitimate
sales will be paid relatively soon by the 2 Obtained from AAER 1017, 1998. It was later revealed that in 1999 Xerox had sold approximately $400 million of its accounts receivable. The final factor is whether the organization takes reasonable steps to respond to any criminal conduct and to prevent its recurrence, including making any necessary
modifications to its compliance and ethics program. Scheme #1: Improper Use and Misleading Disclosure of Related-Party Transactions Adelphia used related-party transactions to hide debt, boost earnings, and loot the company. The stock market plummeted. Other Rite Aid Manipulations According to the SEC, Rite Aid also employed a number of
other methods to overstate its reported income. Al Dunlap did not seem to care; he was out of Scott's as a very rich man—and a lucky one. A Colossal Failure of Common Sense: The Inside Story of the Collapse of Lehman Brothers. "Adelphia's Sale Plan Suffers a Blow," Wall Street Journal. Schickel, Joel A. Which of the following would not be a signal
that a company may have understated its reserve for doubtful debts? • March 18, 1997. The plant remained empty and useless for five years, a stark symbol of incompetence and greed. The two limited partners that put up a joint amount of $15 million in the financing of LJM1 were Credit Suisse First Boston Bank and National Westminster Bank.
Then in late 1990, Enron signed a 23-year contract—valued at over a billion dollars—with the New York Power Authority (NYPA) (Bryce, 2002, p. It is important to note that with mark-to-market accounting, these contracts were valued using these estimates for the balance sheet and that the expected future profit was recognized in current-period
income statements. Exercises 38. The charter of an SPE limits its activities, while its assets and debts are its own and "off balance sheet" (that is—off the sponsor's balance sheet as long as the sponsor is not at risk for more than its invested capital). 059402 01 ch8 p292-324.indd 300 7/7/14 9:10 AM Chapter 8 • Tall Tales 301 The bribery and
accounting provisions frequently overlap because bribery payments are usually misclassified in the accounts, records, and financial statements. The same note to the 1999 Annual Report also revealed that "Whitewing acquired $192 million of merchant assets from Enron. No part of this publication may be reproduced, stored in a retrieval system, or
transmitted in any form or by any means, electronic, mechanical, photocopying, recording or otherwise, without either the prior written permission of the publisher or a license permitting restricted copying in the United Kingdom issued by the Copyright Licensing Agency Ltd, Saffron House, 6-10 Kirby Street, London EC1N 8TS. For example,
courage in carrying out a random act of violence would not be considered a virtue. However, Enron also decided to launch into the retail electricity and gas directly to business organizations and households. Washington, DC: Georgetown University
Press. In addition, Kopper had also received $1.5 million in management fees for running Chewco for a few years. New York: Penguin Books. In spite of her desperate plans to shore up the drowning company, the Enron board had lost confidence in her. So WorldCom went after Sprint. However, the sale of the receivables to a lender caused the
revenue to be recognized immediately and the cash to be received immediately. (c) Decreasing the deferred revenue amount on the balance sheet. U.S. Securities and Exchange Commission Accounting and Auditing Enforcement Release, August 5, 2010. 059402_01_ch5_p144-190.indd 157 7/7/14 9:04 AM 158 Chapter 5 • WorldCom Wizardry: From
WorldCom to WorldCon Shareholders approved the deal at their April 28, 2000 meeting. One of these adjustments was the misstatement of the inventory shrink, discussed previously. 24) Edison's Choice of Accounting Treatment and in this case did not have specific signals. Azurix
was still desperate for new business, and it seemed as though the answer lay in Argentina. In order to develop meaningful and principled decision-making practices, it is necessary for accountants to understand the fundamental approaches to the philosophy of ethics. 059402 01 ch8 p292-324.indd 316 7/7/14 9:10 AM Chapter 8 • Tall Tales 317 8.
As such, these were sales that may, in fact, have been loans masquerading as sales. Beazer's policy was to reverse any unused portion into income at that time. • The audit firm could lose an important client, which could cause other
employees at the audit firm to lose their jobs. 2 Current U.S. GAAP has many industry-specific and transaction-specific rules. In the opinion of the Examiner, the board would probably have approved this purchase even with better information. Past SEC Chairman Arthur Levitt (1998) stated that numerous companies "operate in the gray area between
legitimacy and outright fraud." He also noted, "Integrity may be losing out to illusion." Keeping Levitt's comments in mind, consider a situation in which a company's operating performance and its financial position. • Lockheed Martin was ranked
59th on the 2013 list of Fortune 500," 2013). "A Big Sales Gain for Sunbeam Proves Costly to Investor," New York Times. Sullivan and Ebbers had to have more acquisitions in order to maintain the mirage of soaring earnings and stock value. March 22, 2010. Available online via LexisNexis database. That same day,
Sunbeam's stock fell almost 25 percent, to $34.38. According to the Commission, BellSouth was well aware that "its payments to the lobbyist could implicate the Foreign Corrupt Practices Act ('FCPA')." Furthermore, the SEC found that: • Telefonia had "created false books and records" by describing the payments to the lobbyist as "consulting
services" and • BellSouth had neglected "to devise and maintain a system of internal accounting in Violations." (Quotes from AAER 1494, 2002) Improper Accounting in Violations of the FCPA violations of the FCPA violations."
the bribery can have serious consequences. www.nymag.com. Enron's Bankruptcy Examiner concluded that the "Prepay Transactions" may have been Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source of cash during the four-year period prior to Enron's single largest source 
with smoke and mirrors—and accounting magic. Insignia Solutions. Identify how the U.S. Attorney's office addresses egoism in the case of Peter Madoff. Stock markets, 55 Stock options, 31, 76-77 Stupka, John, 164 Subprime loans, 329, 335-337, 336t, 340-342 Loans with a higher risk of default. Both possessed the need to impress. Malik, Om
2003. Therefore, once again, CFFO lagging or falling behind operating income is a signal of this method of fictitious reporting. 7/7/14 9:04 AM 178 Chapter 5 • WorldCom Wizardry: From WorldCom Wizar
prosecution witness in the Lay and Skilling trial in Houston, Texas. SIGNAL #3: ALLOWANCE FOR LOAN LOSSES NOT INCREASING SIGNIFICANTLY AS HOUSE PRICES FALL If the allowance for home loan losses does not increase when the value of houses decreases, it is a signal that the company may be understating the allowance for loan
losses. Federwisch, Anne. If adjustments are made to the company's documentation or accounts or to schedules after they have been audited via massive journal entries for the preparation of the financial statements, it is futile to audit the underlying information in the first place. Once uncovered, those values and principles renew their sense of
purpose at work and act as a springboard for shrewd, pragmatic, politically astute action. (d) Adding its line-cost expense to inventory to reduce cost of goods sold. (d) Improper use of cookie-jar reserves. The vast majority of these receivables were volume-based rebates that Navistar obtained from its suppliers at the end (or even after the end) of these receivables were volume-based rebates that Navistar obtained from its suppliers at the end (or even after the end) of these receivables were volume-based rebates that Navistar obtained from its suppliers at the end (or even after the end) of these receivables were volume-based rebates that Navistar obtained from its suppliers at the end (or even after the end) of these receivables were volume-based rebates that Navistar obtained from its suppliers at the end (or even after the end) of these receivables were volume-based rebates that Navistar obtained from its suppliers at the end (or even after the end) of these receivables were volume-based rebates at the end (or even after the end) of these receivables were volume-based rebates at the end (or even after the end) of these receivables were volume-based rebates at the end (or even after the end) of these receivables were volume-based rebates at the end (or even after the end) of the end (o
fiscal * The findings herein are made pursuant to Respondents' Offers of Settlement and are not binding on any other person or entity in this or any other proceeding. It equips the PCAOB with disciplinary powers and requires the PCAOB to inspect and investigate registered accounting firms and to enforce compliance with the established standards.
The activity in the allowance for loan losses is summarized in the following table: Year Ended December 31 2008 Balance at end of year Allowance for loan losses as a percentage of net loans 2007 (Dollars in thousands) $ 66,540 $ 33,129
84,790 65,382 (90,398) (33,037) 2,288 1,066 $ 63,220 $ 66,540 2.27% 2.24% 2006 $ 30,870 6,053 (4,107) 313 $ 33,129 1.09% We generally discontinue funding is required to protect our collateral. The failure to accrue the full amount of incentive compensation
expense in accordance with the company's incentive plan. It can indeed involve difficult and perplexing thinking and deliberation.... Cultivation of an ethical person, then, is very largely a matter of developing the rights. (b) Do you think your manager's
dutybased approach to ethics supports or undermines her status as an ethical person? The utility companies were caught in a bind: They were paying astronomical prices for power on the CAL PX auctions and the ISO emergency auctions because the utilities had been
forced to sell their own power plants and had not been allowed to sign any long-term purchase contracts. Herein lay a problem: If Enron purchased CALPERS' share, it would own 100 percent of JEDI and would have to consolidate JEDI's assets and debts into its group balance sheet, because Fastow could not find another party willing to buy
CALPERS' half of JEDI. To economists, economic goodwill is an ability to earn future supernormal profits on its net assets. However, in early 2005, Mark "was one of 10 former Enron officers and directors who settled a lawsuit by shareholders—she contributed $5.2 million of the $13 million settlement" (Lavelle, 2005). This is an indication that false
cookie-jar reserves may have been created and released back into earnings to falsely boost post-acquisition profits. 059402 01 ch2 p047-068.indd 68 7/7/14 8:59 AM chapter 3 The Sizzling Saga of 1 Sunbeam Learning Objectives After studying this chapter, you should be able to: • Recognize how a record of problematic executive leadership and a
flashy leadership style may signal potential problems within a company. However, instead of writing off the entire $500 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installments of $50 million, Lockheed wrote off that amount in annual installment in annua
9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 241 Next, Enron attempted trading in metals and bought the British metals company, MG Plc. What signals can you identify to indicate that Beazer Homes overstated its revenues? (b) To regulate financial products. 7/7/14 9:15 AM 382 References SEC Complaint. Third, MacIntyre noted
the New Testament virtues of faith, hope, love, and humility that also focus on the good of humanity, but here the good includes a spiritual or mystical good. 17). Invoices from Vendors Related To Buca 29. The next problem Mark had to face involved development costs. • Highland Video's "assumption" of debt was a sham because it never received
any economic benefit from it and was not dealing at arm's length. in McLean & Elkind, 2004, p. 19). This is a clear example of both reporting fictitious revenue and overstating assets. Singer, Peter. 278). Several times, Skrypek instructed employees as to whether certain Paisano Partners contributions should be billed back to Buca through a change
order, or whether the amount should be built into the vendor's bid on a Buca project. Dodd-Frank Wall Street Reform and Consumer Protection Act. AAER 2234. This is legal. Ebbers and Sullivan continued their acquisition frenzy. "'Real Time' Enforcement: Recent Trends in SEC Enforcement Actions." Glasser Legalworks Annual Conference on SEC
Disclosure, Accounting and Enforcement. (c) Spread the irregular amount over a number of months and over a number of asset accounts. WorldCom's major gatekeeping failure. The accounting section of the FCPA clearly requires that publicly traded companies operating overseas must "make and over a number of asset accounts."
keep books, records and accounts, which, in reasonable detail, accurately and fairly reflect their transaction[s] and disposition of assets, and devise and maintain a system of internal accounting controls...." (AAER 1494, 2002). Dodd-Frank also revised and increased the responsibilities and power of the SEC. However, there was a problem with the
option because Nicaraguan law prohibited foreign companies from holding a majority of the stock in a telecommunications company. Chapter 2 of this book, "Ethics at Work," examines the major ethical frameworks and how they apply to the business world. 059402 01 ch1 p025-046.indd 33 7/7/14 8:58 AM 34 Chapter 1 • Introduction to the
Problem of Accounting Fraud Internal Controls However, even if every one of the gatekeepers previously discussed failed in their duties, were there no other checks and balances in the form of internal control systems and internal audit departments to guard against the production and publication of fraudulent financial statements? "Shell Game,"
Forbes Magazine. While Dunlap was talking up Sunbeam as part of the road show to drum up support for the debt offering, Morgan Stanley's "due diligence" team had been speaking to Sunbeam managers as well as to Arthur Andersen, the external auditors, 059402 01 ch3 p069-116.indd 86 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of
Sunbeam 87 and to Sunbeam's biggest customers. Beasley, Mark, Joseph V. Lippincott had already publicized a downsizing plan that would require laying off more than 8,000 employees over a number of years. All the top executives assembled for a meeting in the boardroom of the Fort Lauderdale, Florida office. • The family members of the auditor
are potential stakeholders because they could suffer due to the auditor losing his or her job; for example, they may have to move to a different house or change schools. Undertakings 24. According to an article in The Wall Street Journal, it is expected that 1 While not all corporate fraud is accounting fraud, accounting fraud is the most prevalent and
most damaging form of corporate fraud. In fact, while the previously regulated gas business had been steady and predictable, the process of semi-deregulation had produced some unintended consequences. In such a case, as soon as information is released that a company has factored its accounts receivable, one should realize that this, in itself,
could be a signal that the company has accelerated its sales. The borrower remained current on these repayments for all 12 months of 2006. c. Dodd-Frank established the Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Stab
its fate was inexorably tied up with Enron's fate. However, just after Dunlap left the company, "Nitec's auditors at the accounting firm of Arthur Young & Co. reported that the anticipated profits that Dunlap had been promising were apparently the result of massive falsifications and fraudulent accounting entries on the company's books." Even though
there is no evidence that Dunlap had anything to do with the falsification, there had been no real turnaround. Bankruptcy Report #1: First Interim Report of Neal Batson, Court-Appointed Examiner. By the end of his time at Lily-Tulip, Dunlap had cemented his public image as a ruthless downsizing and turnaround specialist—and he was proud of it.
onlinewsj.com/home-page. Unfortunately, as a review of the U.S. economy was naïvely misleading at best and blatantly fraudulent at worst. A consequentialist framework always is able to predict every foreseeable outcome of
any given action. Available online via InfoTrac OneFile (Gale). Choose one asset that Enron used to employ both of these methods and describe how the asset was used to overstate earnings via contrived sales and to overstate earnings via mark-to-market accounting. AAER 2237. Before finalizing its financial statements for the year, Jupiter Company
decides to create a restructuring reserve of $20,000 in preparation for a downsizing to be implemented the following year. Toward the end of 1998, Livent declared bankruptcy in both the United States and Canada. • Examine the Statements of Income and Statements of the Statement of Financial Condition (i.e., Balance Sheets) for Navistar's fiscal
years ended October 31, 2002 and 2003. Lawyers, instead of warning about fraudulent statements, can delight in crafting disclosures that are "technically legal but completely incomprehensible," Fastow said. 059402_01_ch7_p226-291.indd 269 7/7/14 9:08 AM 270 Chapter 7 • Enron and the Tale of the Golden Goose contributed to newly-formed
entities (the Entities) assets valued at approximately $1.2 billion, including $150 million restricted shares of outstanding Enron stock." Although Enron was not forthcoming about the fact that it was moving losing assets to these SPEs at values that hid the losses, the mere disclosure of the magnitude of the
transactions—together with the involvement of Enron officials in the SPEs' transactions with Enron—should have alerted interested parties to the following: • There was the opportunity for hiding losses in these transactions. In 1996, the company set its sights on becoming a major Internet provider and turned its attention to UUNet, which was the
leading Internet provider in the world at that time. Also, they were sold at huge discounts to dispose of the products fully. Later, at Gadel's direction, Buca set up a capitalization account for invoices under $1,000. "Five Days: Smiles at Morgan Stanley," New York Times. As a result, Gadel's compensation, like Micatrotto's, was materially understated
in Buca's proxy statements. Drabinsky "served 18 months of a five-year sentence before being released from jail on day parole last October [i.e., 2012]. Which of the following might undermine the independence of a member of the board of directors at Fermented Fruits? At this stage, Enron was not doing any related-party transactions with JEDI,
which was doing its own successful transactions with outsiders. April 2010. 1 The Securities and Exchange Commission, as a matter of policy, disclaims responsibility for any private statements by its employees. "SEC Refocuses on Accounting Fraud," Accounting Today for the Web CPA. On July 12, it was officially announced that EBS would be
merged into Enron's wholesale division. Gadel and Daniel 059402_01_REF_p365-382.indd 378 J. "Speech by SEC Chairman: Remarks at the Practising Law Institute's SEC Speaks." U.S. Securities and Exchange Commission. I n your view, which theory better identifies the salient moral issues at stake? "Beyond a Code of Professional Ethics: A Holistic
Model of Ethical Decision-Making for Accountants," ABACUS, Vol. Sensormatic's reported estimate in press release. Coincidence? April 19, 2006. In August 2005, he was sentenced to one year plus one day in prison (Bureau of Prisons, 2005). Describe Peter Madoff's duties as a company officer and the ways he
fell short of fulfilling his obligations. Power Company acquires 80 percent of the shares (80 shares) in Emperor Company for $20 million on January 1, 2012. in Frank & Lublin, 1996) Surprisingly, for the first time Wall Street was not impressed with a Dunlap slash-and-burn announcement. By 1979, he was president of the company, and by anybody's
standards, the once poor farm boy was rich. Second, Enron used Chewco and JEDI to overstate its earnings with related-party transactions—it boosted its profits by essentially doing transactions with itself—since JEDI and Chewco were really part of Enron. According to the Financial Accounting Standards Board (FASB) Statement of Financial
Accounting Concepts No. 5, two conditions must be satisfied before entities can recognize revenue: i. One ploy was that it failed to write off capitalized costs, such as legal services and title searches in respect of possible new stores, when it decided not to construct such stores. Key risk and control functions, such as compliance, ethics and risk
management, are the second line of defense. 059402 01 ch4 p117-143.indd 130 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 131 discussed in the Sunbeam." The second two signals listed are related specifically to manipulation of the allowance for returns. It may even be argued that if a company is
not likely to produce a supernormal return on its tangible assets, the net value of all its intangible assets is zero. In some instances, certain Engine Division employees also generated side-letter arrangements with vendors that detailed that the rebates were contingent on future purchases and/or the vendor could recoup the rebate through inflated
future prices by which the Company would forego agreed-upon price reductions. November 8, 1996. • Lea Fastow, Andrew's wife, completed a one-year sentence "on a misdemeanor tax charge for failing to report her husband's kickbacks" ("Status of High-Profile Corporate Scandals," 2005). The only 059402 01 ch7 p226-291.indd 250 7/7/14 9:08
home loan product ever created" (Der Hovanesian). Indeed, Mark managed to hold on to the golden goose just long enough to snatch a golden egg. As long as LDDS publicly reported increasing profits and increasing sales in its financial statements, it could carry on acquiring companies, and there would be no limit to the growth of its stock price.
accounts receivable and does not turn into like an honest sale. 059402 01 ch9 p325-360.indd 341 7/7/14 9:11 AM 342 Chapter 9 • Mortgage Mayhem Table 9.4 Allowances for Loan Losses on All Loans Held for Investment and Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amounts* 2005 Amount as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 2004 Amount of Pay-Option ARM Loans Expressed as a Percentage of 200
Amount Allowance for loan losses on all loans held for investment Total pay-option ARM loan portfolio held for investment 2006 Amount as a Percentage of 2004 Amount 151.3% 209% 556% 700% * Table 9.4 is derived from Exhibits 9.1, 9.2, 9.3, and 9.4 which are given below. The Company received a payment of $200 in connection with this note in
That a Company May Be Concealing 1. On January 6, 2006, Verizon Communications, Inc., completed its merger with MCI. (2) Other real estate owned and repossessed asset balances are shown net of related loss allowances. The company is no longer in existence. Also, according to the contract, after 18 months, Lay would replace Segnar as CEO of
InterNorth. December 7, 2005. (b) The packing case should be included in Ace's December 31 inventory. Tidrick, Donald E. Aristotle believed we are happiest when we act ethically. You know the recommendation is rooted in her sense of duty and not her kind feelings for you. Securities and Exchange Commission Accounting and Auditing
                                                                             . Gadel and Skrypek knew of the purchase and approved payments in connection with the purchase of the villa. However, the stores decreased by 10 percent in year 11 compared to year 10. Undeterred, he got a job as
chief operating officer at Nitec Paper Corp. Krispy Kreme is presented in the text as an example of: (a) Improper accounting for related-party transactions. LR 21548. in Kellenberger, 1995, p. Available o nline via ProQuest database. December 13, 2012. 059402_01_ch3_p069-116.indd 109 7/7/14 9:01 AM 110 Chapter 3 • The Sizzling Saga of
Sunbeam Beazer Homes USA, Inc. Federal Bureau of Investigation. The company had state-of-the-art warehouses and an innovative robotic pharmaceutical system industry leading technology, unique store design, and was very active in acquisitions. WorldCom focused on the use of acquisitions to overstate reserves at the point of acquisition or in the
period soon after acquisition. • Adjust for sales of accounts receivable in order to ensure that such sales do not dilute the signals that could alert you to an overstatement of sales. The Consequentialist/Utilitarian Approach to the Decision-Making Model The consequentialist theory of ethics and morality, as previously discussed, is a particularly
practical ethical decision-making approach because it stresses that the most important aspect of morality is to do the right act, and it specifies that the right act is the one that produces the best consequences considering all the parties affected. The FASB Summary of Statement No. 167 (2009) identifies the primary beneficiary as: [T]he enterprise
that has both the following characteristics: 1. Instead, it decided to write off the uncollectible accounts receivable in quarterly installments. Www.playbill.com. This calculation incorporated certain "above-the-line" items
including well-established or known steps (e.g., implemented engineering fixes) that were viewed, based on historical trends or data, to have effectively reduced warranty costs. When a company will be aggressive in trying to overstate the value of
assets when it has a policy to write-off assets that is slower than those of other companies in the industry. It would have looked very suspicious if so much had been reallocated out of line costs that the expense actually declined as a percentage of sales. 65). • The book is written in a lively and engaging style, with interesting background information that the expense actually declined as a percentage of sales. 65).
on many of the companies and their executives. The good being distributed in this context is very broad and applies to benefits generally or, conversely, to the general avoidance of burdens or hardships. (c) Without any supporting documents and explanation. [and] constructing a plant in China." Soon Enron was working on a pipeline that was
intended to go all the way from Bolivia to Brazil. ISO also administered California's electricity transmission lines. ** For 1997 to 1999, this is the amount referred to in the Enron notes as "sales of merchant assets and investments," and according to Enron's 1998 Annual Report, "Some of these sales are completed in securitizations." Not all of these
sales were completed as securitizations, and there could have been other securitizations. Lay saw a highly regulated business in which the price of gas was mandated. He set up traders to buy and sell these financial instruments. Of course, add easy credit—in the form of easy mortgage loans— to this recipe, and you have all the ingredients for a
spectacular boom-bust cycle. In other words, it may be largely ignored by the market because it was related to the previous management, and the current thinking tends to be that the new owners are going to turn things around. In April 2000, a few months after the formation of Enron Online, EBS had signed a 20-year contract with Blockbuster. (b)
Adjusting gross profit entries to reduce cost of goods sold. • Livent, Rite Aid, Allegheny (AHERF), and Lockheed are presented as examples of understatements of expenses (see Table 1.1 on p. www.munroefoundaton.com. So Enron joined the rush to lay fiber-optic lines and to acquire small telecommunications companies with broadband capacity. July
21, 2001. • Enron's exploitation of California's electricity problems. From NOTES to Consolidated Financial Statements 2000: Note 9 9. Possible overstatement of reserves back into income. main?id=271. However, the floundering investments moved to the Raptors
continued to fall and Enron's stock price continued to decline. www.sec.gov 059402_01_ch7_p226-291.indd 285 7/7/14 9:08 AM 286 Chapter 7 • Enron and the Tale of the Golden Goose December 31, December 
revenue, net of current portion Contract loss reserve, net of current portion Redeemable convertible Series A preferred stock, no par value—5,000,000 shares authorized, 0 and 1,734,125 shares issued and
outstanding 10 24 387 2,404 — 6,878 40 439 — 2,250 — 6,529 10,315 19,989 — 7,927 20 — 95,002 (15,285) 79,737 $ 90,052 — (4,118) 3,809 $ 23,798 Total liabilities Commitments and contingencies Stockholders' equity Common stock, no par value—40,000,000 shares authorized, 10,303,047 shares issued and outstanding Common stock, $0.001
par value—100,000,000 shares authorized, 19,887,672 shares issued and outstanding Additional paid-in capital Accumulated deficiency Total stockholders' equity Extracts from FORM 10-K7 For the fiscal year ended December 31, 2007 BASIN WATER, INC. (c) Brace must write down the asset by $4 million in
the first quarter's quarterly financial statements. Convertible subordinated notes Total liabilities Stockholders' Equity: Preferred stock, $0.001 par value, 500,000 shares authorized, no shares authorized, 160,359 and 109,501 shares issued and outstanding, respectively. However, in
Table 5.3, we see that the "line-cost" expense remained amazingly close to 41 percent throughout the period. A few months after recording millions of dollars in profits on the Braveheart project, Enron cancelled its deal with Blockbuster. All that stuff comes into play. He is now in his late fifties and reportedly resides in Florida, where he "is a
principal in a real estate firm and in a company that makes hair-care products" (Miller, 2011). We are not yet finished calling to account everyone responsible for the epic fraud of Bernard Madoff and the epic pain of his many victims." FBI Assistant Director in Charge Janice K. Salomon earned a fee of $7.5 million from its work on the WorldCom/MFS
merger. "Report Shows How Krispy Kreme Sweetened Results; Panel Says Doughnut Maker Used 'Egregious' Practices, Blames Ex-CEO, Directors," Wall Street Journal. If WorldCom could snag MCI, it would then be the only telecom company with a huge local service, while at the same time
being the second-largest long-distance service in the United States. • In 2006, BellSouth was acquired by AT&T, creating a "telecommunications behemoth ..." (Belson, 2006). So the bubble breaks. Should companies abide by the letter of the law? He wrote that the world before the Great Crash was "a world inhabited not by
people who have to be persuaded to believe but by people who want an excuse to believe" (1997, p. In fact the company incurred a loss of more than $20 million in that year. This process of selling its loans could be accelerated if Fannie Mae were allowed to pool together large quantities of loans and sell interests in those loans to investors in the form
of securities in a process known as securitization. 7/7/14 9:01 AM (c) With a bill and hold sale, the seller recognizes revenue in its income statement but does not recognize cost of goods sold. It had contracts with public school day, in
the contracting schools. March 4, 2005. He did not merely arrange for LJM1 to sell Enron the put option for Rhythms stock, he also created LJM Swap Sub L.P. and LJM Swap Co for the transaction. Explain how the improper writeoff of accounts receivable as "acquisition costs" would affect the signal of accounts receivable increasing as a percentage
of sales. July 8, 2004. There were bar-coding problems with shipping to its biggest customer, Wal-Mart, as well as a failed delivery of 150,000 irons, among other items. The lobbyist had received a total of $60,000, which included a severance payment. • Explain the utilitarian approach to making ethical decisions. (b) Share price and EPS. Byrnes,
Nanette, Mike McNamee, Diane Brady, Louis Lavelle, and Christopher Palmeri. (c) To use mark-to-market accounting to revalue its investment in the Cuiaba Power Plant to LJM1. The exchange was heated, with Skilling
losing his temper and swearing at Grubman: [Grubman] pointed out: "You're the only financial institution that cannot produce a balance sheet or cash-flow statement with their earnings." Skilling very eloquently responded, "Well, you're—you—well, uh thank you very much. On September 15, 2008, disaster at Merrill Lynch was averted when it was
acquired by Bank of America in a U.S. governmentassisted sale (Financial Crisis Report, p. Chapter 6 "8-Year Sentence for Rite Aid Exec." May 27, 2004. Sullivan apparently liked the idea of acquisitions as much as Grubman and Ebbers did—but for a different reason. U.S. Securities and Exchange Commission Litigation Release No. 18205A/June 30,
2003* Accounting and Auditing Enforcement Release No. 1808/June 30, 2003 Securities and Exchange Commission v. Past SEC Chairman Mary L. (3) Loans delinquent more than 60 days, including non-accrual loans. This dramatically inflated reported profits. FINANCIAL STATEMENTS UNITED STATES SECURITIES AND EXCHANGE
COMMISSION Washington, D.C. 20549 Extracts from FORM 10-K11 Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the fiscal year ended March 31, 2001 PEREGRINE SYSTEMS, INC. AICPA National Conference on Current SEC and PCAOB Developments. Jarden Corporation. They had chosen Hattiesburg
because it looked like a rural area's hub town on the map and it didn't have a long- distance phone company. • Identify the top 20 methods used to manipulate financial statements. To bring this wife a rural area's hub town on the map and it didn't have a long- distance phone company. • Identify the top 20 methods used to manipulate financial statements. To bring this will circle, we must not forget that Enron invested its original $250 million in JEDI in the form of Enron stock. Madoff also arranged for his wife
to have a "no-show" job at BLMIS from which she received between approximately $100,000 and $160,000 per year in salary, a 401(k), and other benefits to which she was not entitled. They are often partnerships, joint ventures, or trusts, and sometimes they are corporations. The following transaction occurred near Ace Company's December 31
fiscal year-end date: A packing case containing products costing $10,000 was found in Ace's branch office warehouse when the physical inventory count was taken on December 31. (AAER 1095, 1999) Specific invoices were periodically identified as part of the effort to adjust reported profits. Defendant's Memorandum in Support of Settlement,
United States District Court Northern District of California, San Jose Division. Rite Aid, however, had been paid for these medications by the customers' insurance carriers. September. The choice between treatment of revenues on a gross or net basis does not affect net income. In addition, his sentencing included six months of home confinement
electronic monitoring, and a total of 300 hours of community service. The Collapse of Wizard World Like most financial frauds, WorldCom's problems began with relatively small steps down the slippery slope. Explain. At the end of fiscal 2006, Beazer had leased 557 of its 793 model homes or 70%. In the relationships between Enron
and some of these affiliates were described briefly, whereas others were not named or described at all. The failure to keep proper records is sufficient cause for an enforcement action. However, the allowance for loan losses in Countrywide's financial statements did not increase in the percentage of delinquencies reported
on pay-option ARM loans, or in proportion to the increase in the high-risk pay-option ARM loans or the increase in loans with accumulated negative amortization. On January 14, 1984, the first long-distance telephone call was made on LDDS's system. Also, the investment bankers often held tranches of the pools of bonds that they purchased and
securitized; so they invested in CDSs to hedge against losses due to defaults on bonds underlying the mortgage-backed securities that they had pooled but not sold. With Sidgmore, Grubman, and Ebbers screaming about the truth of
Internet traffic growth. "Fortune 500." 2013. Adam Michaelson (2009), in his book The Foreclosure of America, stated that Mozilo and Loeb "had a dream that they could build a new kind of mortgage company and one day be in the position to help all Americans achieve the dream of home ownership" (p. Eventually, the debt had to be repaid. If you
then offer the child extra candy to play and some additional candy as a prize for winning, he or she may be more inclined to put extra effort and concentration into the game. Some studies categorize the fictitious reporting methods in terms of how the method manipulates income (revenue or expense), whereas other studies categorize the fictitious
2009). The report said that the features caused a higher risk of default regardless of the borrower's credit score" (Nixon, 2006). He knew the company was operating in gray areas. In addition, one should be aware that this factoring of accounts receivable would have concealed Signal #1 because the factoring would have reduced the buildup in
accounts receivable. The company began facing enormous difficulty in meeting these phenomenal growth projections from at least the first quarter of its 1994 fiscal year. In addition, the Examiner's First Interim Report identified at least another $633 million in the release of reserves to satisfy Wall Street's expectations. The fact that Clinton's city hall
had been the site of General Sherman's headquarters during the siege of Jackson struck a chord with the competitive young Foster, who enrolled in the school. The family paid under half a million. One thing was certain: the deal provided yet another
windfall for LJM's investors. In such a case, the company may reopen the value placed on goodwill at acquisition by a complementary amount. Stock Options Because management has ultimate responsibility for the preparation of a company's financial
statements, it is not surprising that the huge rise in the incidence of fraudulent financial reporting enforcement actions at the turn of the millennium was associated with huge increases in incentives for management to present financial statements, it is not surprising that the huge rise in the incidence of fraudulent financial reporting enforcement actions at the turn of the millennium was associated with huge increases in incentives for management to present financial statements, it is not surprising that the huge rise in the incidence of fraudulent financial reporting enforcement actions at the turn of the millennium was associated with huge increases in incentives for management to present financial statements.
"Adelphia Founder John Rigas Found Guilty" (2004), BR-6413 (2002), and Goldsmith (2005). Endeavor News. However, if the decrease in current liabilities does not seem to be explained by efficiency or by a form of longer-term financing on the balance sheet and Signal #1 is also in force—that is, expenses show a decrease as a percentage of sales—
the warning signs get stronger. (c) Legal reserves. Fedarcyk, the Assistant Director in Charge of the New York Field Office of the Internal Revenue Service, Criminal Investigation (IRS-CI); Robert L. The SEC's complaint also
alleged that CUC's president and COO, E. In the last quarter of 2001, it sold $101 million of this inventory to Highland Video. "By engaging in this shell game, those responsible for the improper entries stayed several steps ahead of Arthur Andersen in shielding these entries from the auditors." (Quotes from Third and Final Report, 2004, pp. Polverari
agreed to pay a civil penalty of $25,000 (Norris & Henriques, 2000). See Fictitious financial reporting fraud. "Enron Prosecutors, after Plea Bargain,
Can Reduce Technical Jargon in Trial," Wall Street Journal. These findings do not reflect a coordinated scheme by senior management to manipulate the Company's reported results or conduct committed with the intent of personal gain. The Bankruptcy Report provided the goodwill allocation schedule outlined in Table 5.1. In its interim investigation
                                                                                                                                                      Accumulated negative amortization (from original loan balance) $26,122,952 $4,701,795 $13,973,619 $ 32,818 $ 142,034 $ 29 (continued) 8 Obtained from U.S. Securities and Exchange Commission. Scott Paper had had the
guts ripped out of it. Insignia's understatement of its allowance for returns is an example of overstating revenue via: (a) Improper valuation of revenue recognition. Skrypek knew that Gadel had this ownership interest in the information technology company. The jury deadlocked on some charges and found the defendants not guilty on the other
they should have realized that it was unclear as to why and how these entities were being used. September 5, 2010. Countrywide has faced a barrage of lawsuits over the years. The first phase began producing power in May 1999, two years behind schedule. According to Schapiro, Lehman was required to furnish growing amounts of security in order
to continue doing business but was unable to keep up with these demands because a number of lenders refused to provide even regular loans to the beleaguered investment bank (p. June 7, 2006. Madoff pled guilty in Manhattan federal court before United States District Judge Laura Taylor Swain. First, these loans charged borrowers high interest
rates to compensate for the higher default risk. Signal #5: Fixed Costs Remaining a Constant Percentage of Sales When major expense items remain identical quarter as a percentage of revenues, it is frequently a signal that the reported expenses and revenues are being manipulated. At the same time, as Lambson pointed out, "When
there's a technological change, or a change in consumer tastes, the changes are reflected in the prices. The SEC further alleged, "In FY 1999, Rite Aid improperly reduced the accrued shrink expense for 2,000 stores resulting in an aggregate increase to income of $5 million" (AAER 1579, 2002). www.bop.gov/iloc2/LocateInmate.jsp. (b) Some of the
revenue relating to the finance charges included in monthly lease payments over the life of the lease agreements and delivery of the goods. According to the SEC, in 2012, the most frequent whistleblower complaints "related to corporate disclosures and financials" ("SEC Receives ...," 2012). Those
involved in the scheme called this "parking" the transaction. Ciesielski. "There is no question that when I went to those interviews, I wasn't fully truthful. 2005-2007. The order would be back-dated as though it were placed on December 28. (Accountants, on the other hand, while having the same concept in mind, have some cursory rules about how to
calculate and allocate a portion of the purchase price of an entity to goodwill.) At the time of the acquisition, the parent company's assets, and its liabilities. On December 31, 2012 on the purchase price of an entity to goodwill.) At the time of the acquisition, the parent company's assets, and its liabilities. On December 31, 2012 on the parent company ascribes a fair value to the 059402_01_ch5_p144-190.indd 153 7/7/14 9:04 AM 154 Chapter 5.
Bronto Company formed an SPE in the form of a partnership that it named SPOCK1. He knew how to find bargain stocks and he felt sure that Sunbeam could be made very profitable again and that its stock price could soar. www.potterleaderenterprise.com. The Powers Report (2002) described how Fastow concealed and disguised the ownership of
LJM1 with a series of interlocking partnerships: "Fastow became the sole and managing member of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which was the general partner of LJM Partners, LLC, which w
the published financial statements. Also in 1997, AHERF overstated its reported consolidated net income by incorrectly recognizing over $54 million of irrevocable trusts' income as its own income. Further, modern consequentialists agree that it is essential to consider the sum or aggregate of all the benefits and disadvantages to all of the
stakeholders. Fastow served the last months of his sentence in a halfway house and was released in December 2011 (Inmate Locator). Beazer's Remedial Efforts 23. inventory as percentage of, 201, 203 reducing, 199-204 Costs capitalization of, 173-174, 198 deferred, 197, 220-221 fixed, 76, 128, 147, 172-173 line, 160, 173 patent, 290 sunk, 207
7/7/14 9:17 AM Glindex 387 variable, 76, 173 write-off of capitalized, 174, 198 Countrywide, 38, 325-348 consolidated balance sheets, extracts from, 342-343 history of, 338 underestimation of allowance for loan losses by, 338-339 Credit easy, 327-328
risk, 336-337 Credit-default swaps (CDSs), 330-332 A financial instrument that gives the holder the right to be paid if the borrowers of specified loans default. The equipment revenue known at Xerox as the "box" revenue. (For example, if a company produces and sells less, the landlord charges the same amount of factory rent; so the rent expense
becomes a greater percentage of the sales revenue amount.) In the case of WorldCom, the line cost was a very significant expense that had a fixed-cost element as well as a variable-cost element. In 2000, the Company entered into a long-term supply contract (the "Agreement") with an automobile manufacturer (the "Automaker") to develop and
manufacture V-6 diesel engines commencing with model year 2002 and extending through 2012. They should be made? Goeken figured out that they should put some microwave towers between St. Louis and Chicago, on the
famous Route 66, to support two-way radio communications, Inc." (MCI). However, the "supersenior" tranches with high credit ratings and lower returns) were hard to sell, and Merrill had to hold a large portion of them. Revenues Year 1 $ 4,000 Year 2 $ 6,000 Year 3 $
                         is an extract from XYZ's notes to its financial statements: Note: Revenues All revenues reported are in respect of sales type leases. • Edison Schools now operates under the name "EdisonLearning." According to the EdisonLearning website, the company is working with almost half a million students in over two dozen states and
also works with a number of schools overseas (2013). Ethical Auditors is on a tight deadline to finish the audit of Stylish Shoes soon after its financial year end. If loans must be repaid by the issue of shares, the more the stock price down. (Goodwill refers to the excess of the
cost of an acquired company over the fair value of its net assets.) This would be done at the exact time of recording the purchase of the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the period immediately following the acquired company (as opposed to the acquired company (as opposed t
electricity market from when it was first deregulated in 1998 until Enron's collapse in 2001, "because I was trying to maximize profit for Enron." (Smith & Wilke, 2002) That same month, another article (in the New York Times) described how Belden admitted to "transmitting energy into a fictional world, complete with bogus transmission schedules,
imaginary congestion in power lines and fraudulent sales of 'out of state' energy that, in fact, came from California itself." As a reward for creating this fine work of fiction, Enron paid Belden large bonuses, "totaling about $5 million . . . 37. FACTS 11. To MacIntyre, virtue can be found in performing an action or a practice for its intrinsic benefits.
Gadel and Skrypek also exploited Buca's unusual relationship with High Wire and EDP to improperly capitalize expenses. Do you think it varies depending on the situation? • We conclude the failures of credit rating agencies were essential cogs in the wheel of financial destruction. He
was regarded as an ingenious visionary and a farsighted genius. Sunbeam created these overstated restructuring ploy and upon its acquisitions of Coleman, First Alert, and Signature Brands. Chainsaw Al, however, was not ready to retire. Issuing Adelphia Shares Directly to Rigas
Entities A number of direct placements of Adelphia shares were made to Rigas Entities. The leading and best-known form of consequentialism is interest expense only. For Aristotle, the human telos is to comprehend the good, and so we will be happiest when we are
achieving our telos. Both had colossal ambition-to-knowledge ratios—always a dangerous set of attributes—and both were newly rich, having come from working-class roots. Kirk Shelton Is Guilty on All Counts of Accounting Fraud." January 5, 2005. The below-the-line items inappropriately included in the reserve calculation caused the warranty
expense to be understated by $17 million in fiscal year 2003 and by $18.5 million in fiscal year 2003. According to SEC enforcement releases, which of the following purposes did Enron not use its investment in Empressa
Productura de Enerain (EPE) and the offbalance-sheet entity LJM1? Explain how deferred revenue can be misused to overstate earnings. The Commodities Futures Modernization Act in 1999: (a) Effectively ended the separation of commercial banking from investment banking. (c) Improper recognition
of vendor rebates. By November 1998, the stock price had tumbled to about $7 (AAER 1393, 2001). Perform Internet or database searches for press releases that revise earlier public statements in quick succession. "Anatomy of a Bankruptcy. • Cut loose almost 90 percent of its product line. in Jenkins, 1997)
Cameron pointed out: In the end, a corporation almost always loses company memory and company energy. 13-15) 059402 01 ch5 p144-190.indd 151 7/7/14 9:04 AM 152 Chapter 5 • WorldCom Wizardry: From Wo
ordinary, old-fashioned dial-up access, and the broadband capacity for demand at that time was being vastly overbuilt. Xerox's internal name for the accounting method whereby it shifted this revenue was its "return on equity" method. Both the note and the related allowance for doubtful accounts have been classified as current assets and are
included in the accounts receivable balance at December 31, 2007 and 2006. 2009. "Adelphia Founder, Son Convicted of Fraud," Washington Post. RISMedia. ERISA refers to the Employee Retirement Income Security Act of 1974, a federal law set up to protect employee retirement plans. "Krispy Kreme Names CEO: Shares Jump." March 8, 2006.
The birth of the "weather derivative" grew out of Enron's attention to fundamental weather information for its gas trading. A legitimate reserve is usually created in recognition of a future liability or loss. Overstatement of Revenue Scheme: Litigation Release (LR) No. 18205A describes the ways in which Peregrine overstated its revenue in its
financial statements. An Overview of Sensormatic's Fictitious Financial Reporting Schemes The SEC found that Sensormatic's revenue and earnings from at least the first quarter of fiscal year 1994 until the third quarter of fiscal year 1995.1 Further, the SEC claimed that Sensormatic's senior management, including Pardue and
Simmons, were "aware of the methods used to effectuate the scheme, [and] also condoned and directed them. For example, the SEC Complaint alleged: Nothing ... informed investors that Countrywide's "prime non-conforming" c ategory included loan products with increasing amounts of credit risk. 059402 01 ch9 p325-360.indd 345 7/7/14 9:11 AM
346 Chapter 9 • Mortgage Mayhem Extract from Note 8 (2007): Following is a summary of negatively amortizing ARM loans held for investment: December 31 2007 2006 (in thousands) Total Pay-Option loan portfolio Total principal balance of Pay-Option loans with accumulated negative amortization $28,973,498 $32,866,475 $26,434,496
$29,074,810 Accumulated negative amortization (from original loan balance) Unpaid principal balance of Pay-Option loans with supplemental mortgage insurance coverage $1,233,165 $18,374,251 $5,729,532 Average original loan-to-value ratio (1) Average original combined loan-to-value ratio (2) Average original FICO score (3) Loans
underwritten with low or no stated income documentation Borrowers electing to make less than full interest payments Loans delinquent 90 days or more (4) 655,453 76% 79% 717 81% 75% 78% 718 81% 71% 5.71% 77% 0.65% (1) The ratio of the amount of the loan that is secured by the property to the lower of the original appraised value or
purchase price of the property. In Enron's case, an examination of the "Merchant Investments" notes in its annual reports revealed important information regarding the sales of Enron's merchant assets. News Release. 059402 01 ch7 p226-291.indd 249 7/7/14 9:08 AM 250 Chapter 7 • Enron and the Tale of the
Golden Goose These transfers were carried out via related-party sales of poorly performing Enron's earnings. The company was caught in an ever-intensifying vicious circle. When Sunbeam simultaneously reported large operating profits in 1997 but negative CFFO, it was a signal to bail
out of the company and its stock as quickly as possible. So the current charge (expense) in the income statement is often "discounted" by analysts and investors. He was recruited by Lily-Tulip, Inc., to cut costs and perform a turnaround of the company that was operating at a loss and had too much debt. Based on aging of the accounts receivable, it
appeared that the reserve for doubtful debts balance needed to be stated at $55,000. the seventh-highest amount of bonuses paid to any executive director of California's Electricity Oversight Board, was emphatic that Enron did not merely
participate in California's energy upheaval, but Enron "was the cause of them" (Peterson, 2005). 10 Obtained from U.S. Securities and Exchange Commission. Smith, Glyn, 164-165, 166 Smith Barney, 329-330 Southampton, 259 SOX Act (Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002), 27, 34-38, 41, 48 SOX Report (Report Pursu
Oxley Act of 2002), 31, 42, 84, 126, 192 Special purpose entity (SPE), 235, 243 A business entity such as a partnership, trust, or joint venture created as legally separate from a company's normal operating activities. The Commission found that for
1997, Livent reported a pretax loss of $62.1 million, when its actual loss was a minimum of $83.6 million. (b) Autonomy. Rev. Tyco International Ltd., AAER 1555. January 26, 2004. Grass was released after seven years and placed on three years'
probation. September 16, 2010. Push Company is a lawn mower manufacturer. Signals of Krispy Kreme's Fictitious Reporting Scheme of Misusing Round-Trip Transactions Signal #1: Accounts Receivable increasing as a Percentage of Sales as measured by,
for example, days' sales outstanding (DSO), is a signal of acceleration of fictitious sales. Navistar, like all issuers registered with the Commission, is ultimately responsible for the accuracy of its books, records, and accounts. Based on some stern e-mails sent by the managing partner in the past, Eva believes that if she tells him Lucas left, he will fire
Lucas. . It is best if the one-time charge has a positive-sounding name, such as a "restructuring reserve." In the future, when the expense actually occurs and is offset against the reserve instead of being recognized as an expense, the earnings are inflated because the expense was moved to an earlier period. http://. August 6, 2007. In such a scenario,
selling CDSs would continue to be very profitable. He was released in October 2011 (Inmate Locator). . "Keynote Luncheon Speech." U.S. Securities and Exchange Commission, 32nd Annual SEC and Financial Reporting Institute Conference. There are "recipient rights," which are the "rights to receive something" (e.g., the right to be paid for services
rendered). Deontology judges right action based on one's duties. Why are multiple-element lease contracts a fertile ground for overstating revenue? If that could be worthwhile to stick around and wait for their stock options to turn into huge financial windfalls. Auditors need to demand
necessary access, and if that demand is not met, they are obliged to give a disclaimer audit opinion or a qualified opinion on the financial statements. In 2004, in connection with the sale of a system, the Company received a $300 unsecured note that provides for interest at a rate of 3% per annum. If she thinks truth-telling is a duty, she will reveal the
fraud because it is her duty to be forthcoming. In a contrived sale to its SPE LJMI, Enron used what it referred to as the price to justify a mark-to-market revaluation of its ownership in the Cuiaba Power Plant. wwvv.washingtonpost.com. About $3.3 billion of reserves was released to reduce line costs inappropriately. In addition, the trading volumes
were so large that even in gas trading—where they had all the advantages—when the traders bet the wrong way, the losses were astounding. Jeter, Lynne W. When CUC transferred some amounts for deferred club membership revenues to current period revenues, it had the following effect on CUC's financial statements. The Financial Crisis Inquiry
Report (2011) concluded that the financial crisis in the United States has been caused by: (a) The collapse of the mortgage securitization. "Slow Canada: Fraud Cases Can Drag On," Wall Street Journal. "Lehman Brother's Probably Won't Ever Be Charged With Anything," New York Magazine. com.
www.nbcnews.com. The Livent case is presented here because it contains some clear examples that alert the reader to the frequently committed, old-fashioned fraud of omitting expenses and the corresponding liabilities by simply failing to record invoices in the ledger during the correct period. 62) 059402 01 ch7 p226-291.indd 264 7/7/14 9:08 AM
Chapter 7 • Enron and the Tale of the Golden Goose 265 Signals of the Enron Frauds A number of red flags in Enron's financial statements indicated that Enron had been using off-balance-sheet entities or SPEs to understate debt and overstate earnings. In addition, Skrypek was Buca's interim CFO for a short period in 2005. In his book Take on the
Street, Levitt discussed the many directors who lacked independence, as well as those directors who were indifferent and had no interest in company activities. Michael Kopper was now in control of Chewco—a phantom entity. (d) All of the above. However, whether by design or by coincidence, the dramatic announcements of cost cutting had laid the
foundation for lending credibility to the suddenly increasing false profits that would be reported in the near future. Thus, we must rely more on the previously mentioned signals for this scam. However, by the end of the following year, seven weeks after Azurix had gone public, the company was shocked when Britain's water regulation agency
announced that water companies would have to drop prices. Calculate the ratio of accounts receivable as a percentage of sales for years 1, 2, and 3 without taking into account what you read about the sale of Blake's accounts receivable. According to the SEC, Telcel recorded a disbursement in its books and records based on invoices. Greg Whalley, a
talented trader in charge of Enron's wholesale trading operation, supervised the acquisition of MG Plc. This scheme of misreporting round-trip transactions is examined further below. According to SEC records, another pivotal individual involved in the execution of the schemes was Mary Sattler Polverari, a CPA who was hired by CUC in December
1995 and became manager of financial reporting in 1997. These indications may be found in references to any of the following: • Loans with negative amortization • Troubled debt restructurings In the Notes to Countrywide's
financial statements (see Exhibit 9.4), the increase in loan repayment delinquencies on pay-option ARM loans, as reported in the years leading up to 2007, preceded the massive allowance for loan losses ($2.3 billion) on all loans held for investment in 2007. This is not to say that moral behavior is only automatic or spontaneous. Securities and
Exchange Commission Litigation Release, May 14, 2004. The board of directors was criticized for not performing due diligence before its approval of the acquisition. Causey began his prison sentence in January 2007 at a minimum-security prison near Austin, Texas (Stinebaker, 2007). Allowance for loan losses as a percentage of all loans held for
investment actually decreased from 2004 to 2005, whereas loan delinquencies on pay-option ARM loans increased dramatically. For the first two quarters of fiscal 2007, Beazer understated its cumulative revenue by $2.6 million and overstated its cumulative net loss by $3.9 million due to the improper sale-leasebacks accounting. For a few years after
high school, both spun their wheels doing odd jobs such as delivering milk. www.unicomm.fsu.edu/Florida-State-Times. In the absence of a current appraisal, all relevant and current information known at the time must be used. Revenue recognition, 81 The process of recording a transaction in the financial statements indicating that the conditions
have been met for the earning of revenue. He eventually cooperated with investigators and pleaded guilty to a "misprision" charge for not reporting the fraud. Which of the hundreds of thousands of mortgages inside each security"
(McLean & Nocera, 2010, p. The SEC explained: In approximately February 2000, Fastow and others caused Enron to buy out the partnership interests of LJM1's limited partners, Credit Suisse First Boston and National Westminster Bank (NatWest). (a) CFFO will increase by $15,000. In the case of Edison Schools, Inc., its inadequate disclosure did
not affect the amount of net it reported. Scott. Sunbeam emerged from bankruptcy under the control of Michael Steinhardt of the Steinhardt Partners Fund. Consolidated Statements of Income (in thousands, except per share amounts) Year Ended September 30 Total revenue Home
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construction and land sales expenses Gross profit Selling, general and administrative expenses Goodwill impairment Operating income taxes Provision for income taxes Net income taxes Net income taxes Net income taxes Provision for income taxes of the content of

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45,634 39,879 42,485 39,812 44,345 $ $ 5.91 5.59 0.13 9 Extracted from 10-K filings for Beazer to report earnings, i.e., allowing Beazer to report earnings that still met or exceeded analysts' expectations for its
quarterly net income and earnings per share ("EPS") while permitting it to improperly defer a portion of its income to future periods. The overstated reserves are released in future periods to fictitiously understate future periods. The overstated reserves are released in future periods to first income to future periods. The overstated reserves are released in future periods.
WorldCom's subsequent mergers, Salomon earned over $100 million in fees and Ebbers made over $12 million. Simply put,
holding books open enables a company to report the next quarter's sales in the current period's books and records open for a few extra days after the close of a reporting period to record additional sales. 68084–68097. Adjust for the sale of accounts receivable in year 3 and calculate CFFO as a percentage of
operating income for years 1-3. "What I would share today is whenever you get yourself into these situations, you're better off right up front facing the issues. While Foster waited for the coach in a bank, he picked up a brochure lying on a desk in the lobby—a seemingly trivial, distracted act that changed the course of so many lives. With an improper
use of reserves, companies usually over-accrue a liability in one period and then reduce the reserves in later periods. 58, 59) Indeed, many articles in the business press had alerted readers to the high risks associated with pay-option loans. We purchase the products at rates which management believes approximate market rates. Livengood was
reportedly such an avid fan of the doughnuts that he had a huge cake made entirely of doughnuts when he got married in 2002. Holdings of between 20 percent and 50 percent, where the investor is deemed to have significant influence, but not control, unless information to the contrary exists. Nova Southeastern University. (Refer to Chapter 2 for a
description of the justice approach.) 059402 01 ch3 p069-116.indd 96 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 97 Assignments True/False Questions with T for true or F for false for more practice with key terms and concepts from this chapter. The period during which the Rhythms stock could not
be sold by Enron had passed, the stock had fallen in value, and its price continued to be volatile. 7. Make your decision. One dramatic example of this can be found in 1997, when CFFO was stated as $211 million, but after adjusting for possible securitizations, it was reduced to negative $128 million. United States District Court, Southern District of
New York. Galbraith explained that during a speculative boom, investors purchase an asset or the use of it, but for the purpose of selling the asset at a higher price. Consider some of the ways in which the different links in the chain (from borrowers to mortgage lenders, insurers, and investment bankers) that led to the
financial meltdown of 2008 may not have fully disclosed risks to parties with whom they dealt. April 2012. His dress rehearsal with Chewco had given him practice in the exploitation of SPEs. It had shown him how easy it was to create artificial revenue in Enron's books—simply by charging an amount (for example, for a management fee or a contrived
sale) to an SPE that he ultimately controlled. In June 2003, the Commission filed a civil injunctive action against Steven S. The public could now buy the right to purchase gas or to supply gas at fixed prices in the future. The Commission acknowledges the assistance and cooperation of the Manhattan District Attorney and the New York City Police
Department. "Ethical Decision Making in the Public Accounting Profession: An Extension of Ajzen's Theory of Planned Behavior," Journal of Business Ethics, Vol. Net sales Cost of sales Gross margin Selling, general, and administrative expenses Operating income Interest expense Interest before tax Tax Net Income Year 1 Year 2 Year 3 $100,000
\$90,000\ \$80,000\ 60,000\ 58,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 40,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56,000\ 56
located in a small building opposite the University of Southern Mississippi. Under the equity method of accounting, the invester includes its share of the investment is increased by a corresponding amount on the balance sheet. August 2006. Fastow forfeited $24
million. As the housing market took a nosedive and housing prices plunged, countless homeowners who had toxic mortgages (mortgages that were likely to go into default) began to lose their homes, and the problem caused a domino effect. A company could be using the SPEs to move poorly-performing assets off its financial statements to avoid
dilution of reported earnings or to generate gains. Rather, he presented a frank account of an ethical lapse that he wished he had avoided. The Myth of Internet Growth Everyone accepted the enthusiastic claim that Internet growth was not accurate.
Extracts from Complaint against TierOne Bank* Civil Action No. 12-cv-00343 Filed September 25, 201210 IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF NEBRASKA Omaha Division SECURITIES AND EXCHANGE COMMISSION PARAGRAPHS 3 and 7: 3. Provide supporting calculations. (Improper deferral of expenses refers to
any technique that avoids the recording of an expense in the current period by shifting the recognition of the expense to a later period's financial statements.) The Sarbanes-Oxley (SOX) Report's study of SEC enforcement actions found that the most common method of misstating financial reports was improper expense recognition via a "lack of
accrual" of expenses and their corresponding liabilities. • Eliminate the majority of its offices. Signal #4: Large One-Time Charges in Income Statement, especially around the time of an acquisition period, because these often signal that the company is creating false
reserves to boost later earnings. In addition, information available to Sunbeam management did not provide any basis for projecting net sales in excess of those achieved in the first quarter of 1997" (AAER 1393, 2001). He is described as a lifelong German shepherd lover and apparently despises his infamous nickname of Chainsaw Al (Florian &
Adamo, 2010). "The company was a great company. The process in which many loans are pooled together and interests in these pooled loans are sold to investors is known as ___
                                                                                                                                                                                                                                         _. New York: Public Affairs. For an analysis of these numbers over the four-year period from 1997 to 2000, refer to Table 7.5. With these adjustments, the CFFO lagged
operating income in each year of the period from 1997 to 1999, and the CFFO as adjusted was, in fact, negative for two of those years. This signal is a huge red flag. The Company also leases office space and equipment from two individuals, one of whom is a director and employee and the other an employee, under month-to-month agreements. These
adjustable-rate mortgage loans allowed for a variety of payments options, one of which was "a minimum payment which was insufficient to cover accruing interest" (SEC Complaint, June 4, 2009, par. The SEC also alleged that Xerox increased its reported earnings by changing estimates of the residual values of its leased assets. Push offered Pull a
significant discount for placing the order early and said that it would hold the inventory for several months before shipping it to Pull in May the next year. Explain Xerox's possible incentive for selling those accounts receivable. No government-sponsored plan was successfully executed for the sale or rescue of Lehman Brothers, which filed for
bankruptcy on September 15, 2008—the same day that Merrill Lynch was acquired by Bank of America (Financial Crisis Report, p. In 1996, British Telecom (BT) made an offer of $24 billion for MCI, and GTE also put in an offer. 059402 01 ch7 p226-291.indd 281 281 Multiple-Choice Questions 21. From 2000 to 2003, Gadel received more than
$96,000 in compensation arising from improper reimbursement requests. He decided to chop up Enron's long-term supply contracts, as well as its long-term purchase contracts, into smaller ones and offer all of them sale. Report Pursuant to Section 704 of the Sarbanes-Oxley Act of 2002. List the major alternative courses of action, including those
that represent some form of compromise or point between simply doing or not doing something. A few days after Sunbeam and rescue the current
management team from Sunbeam's mess. Micatrotto, Sr. ("Micatrotto"), Buca's former Chief Executive Officer, President, and Chairman of the Board of Directors. The category of "Financial traud/Issuer Disclosure" (i.e., accounting fraud) involves violations related to financial statements and financial disclosures released by "issuers" of financial traud/Issuer Disclosures related to financial statements and financial disclosures released by "issuers" of financial traud/Issuer Disclosures related to financial statements and financial financial st
statements. Source: www.sec.gov/news/newsroom/images/enfstats.pdf new SEC Chairman Mary Jo White, who assumed leadership of the SEC in April 2013, will be more likely to shift SEC focus back to accounting fraud in future years (Eaglesham, May 27, 2013). 059402 01 ch6 p191-225.indd 214 For Discussion 31. Before the passage of the
Secondary Mortgage Market Enhancement Act of 1984, there were regulations that prohibited
                                                                                                                                     investors from investing in mortgage-backed securities that were not backed by GSEs. 17. Enron Creditors Recovery Corp. Whiteman, Lou. As a consultant to InterNorth, which subsequently became part of Enron, Skilling began to realize that
without stable, long-term gas prices, energy users—including industrial plants, utilities, and private customers—would not want to be dependent on gas. Such transactions between two parties that do not have a relationship (such as a business or family
relationship) with each other. Enron sold the contract to the conduit, Mahonia—owned by JP Morgan Chase—for $330 million. The Company began deferring some of these start-up costs in the fourth quarter of fiscal 2001 and as of the fourth quarter of fiscal 2001 and as of the fourth quarter of 2002 had accumulated $57 million of deferred preproduction costs. LR 17692. 47). Nevertheless
on the last day of FY 1999, Rite Aid reduced cost of goods sold and accounts payable by $42 million and, in the same way, reopened its books to recognize the other $33 million of those rebates after the close of FY 1999. The economy plunged into a deep recession. Approaching ethics from a deontological framework, discuss whether or not Xerox's
management was unethical in issuing financial statements that accelerated Xerox's revenue recognition. Mariner specialized in highly speculative deepwater exploration, which made the value of its shares even more volatile. This trend would eventually be destructively expanded and manipulated to bring the U.S. housing market to the brink of
disaster because a lender who sold a loan no longer had a direct interest in future principal and interest payments on the value of the inventory." Sunbeam even guaranteed a profit of 5 percent to the "customer" on any future resale of
this inventory. G. • Adelphia remained jointly and severally liable for the debt. Steele, an analyst for Buckingham Research Group in San Francisco, downgraded Sunbeam to a neutral rating in July 1997 based on the increase in inventories and on him noticing that "changes in cash from working capital were negative" (Byrne, 2003, p. (Quotes from
Kellenberger, 1995, p. • Identify the signals in financial statements that could alert one to the possibility that future periods' revenue has been recognized in current periods' revenue has been recognized in current periods' revenue has been recognized in current periods. And although he told them some of what he knew about pharmacy rebates, "I didn't fully tell them all I knew." After Noonan's third meeting with investigators, he said, rumors
ran rampant, innuendoes abounded, and he decided to speak directly with government officials. www.freddiemac.com. Deontology The word deontology is derived from the Greek deon, which means "duty." The deontology to the eventual peril of the
company, the trading arm expanded trading to a variety of businesses and commodities in areas that Enron knew absolutely nothing about. Possible overstatement of revenue, or fictitious revenue, or fictitious revenue, or fictitious revenue, or fictious revenue, 
benefits and bonus (subject to satisfaction of certain criteria determined by the Compensation Committee of the Board of Directors). Employee Loan—In March 2001, we entered into a $150,000 unsecured loan with one of our officers. Certain anticipated fixes were incorporated into the CPU calculation before they had even been implemented.
"Former Enron Exec Causey in Prison." Washington Post. The case is being handled by the Office's Securities and Commodities Fraud Task Force. And how was he going to slash costs? Available online via EBSCOHost. For years he certified that periodic reviews established the firm's compliance with internal and regulatory rules. For example, the
Commission revealed that in a 1999 presentation to potential investors in a stock offering, Adelphia's cable plant was only approximately 35% rebuilt at the time"
(BR-6413, 2002). On July 19, the day after the announcement of Dunlap's appointment as CEO, Wall Street analysts gave buy ratings to the stock and its market price jumped from $12.50 to $18.63. www.cnn.com. Additionally, in November 2005, Beazer announced an increase to 10 million shares of its prior repurchase plan which resulted in 3.65
million of its shares being repurchased during fiscal 2006 for an aggregate purchase price of $205.4 million. 4 Loeb died in July 2003, at the age of 79. The InterNorth board soon regretted the merger and blamed Segnar for persuading them to agree to it. • In September 2011, former Los Angeles Laker Magic Johnson announced that the Magic
Johnson Foundation would be partnering with EdisonLearning to develop Bridgescape Learning Centers for at-risk students ("Magic Johnson," 2011). The SEC, in a subsequent discussion of Enron's approach to the non-publicly traded businesses in its portfolio, alleged: Enron valued the businesses according to its own internal "models." Enron then
manipulated these models in order to produce results necessary to meet internal budget targets. This includes considering the risk that conflicts of interest present throughout key business units and individual business leaders. January 29,
2007. Either way, what both stories have in common is that the first meeting about starting a company to resell long-distance phone service was in a coffee shop in Hattiesburg and that Waldron was present. It was not clear that the revenue in the income statement needed to be reported net of the district-paid expenses for those cases in which
                                                  . • Detect and explain the signals in Countrywide's financial statements that could have alerted readers that Countrywide's allowance for loan losses may have been underestimated. "Enron-related litigation has so far resulted in settlements of over $21.7 billion" ("Payments to Date," 2011). "Jack Grubman Is
Back. www.gpo.gov. Salomon Smith Barney (SSB), 33, 167-169 Saltmarsh, Erik, 247 Sambol, David, 348 Sarbanes-Oxley (SOX) Act, 27, 34-38, 48 executive compensation and, 35 internal control requirements, 36 provisions of, 35-38 Section 301, 35 Section 302, 36 Section 404, 36, 41 SARS (stock appreciation rights), 201
Schapiro, Mary L., 26, 38, 40, 333, 334 Schickel, Joel, 53 059402 01 GLINDEX p383-401.indd 398 Schipke, Roger, 71, 74 Scott Paper Co., 71, 73-74, 90 SEC. Mark-to-market accounting refers to the revaluation of an asset or a liability on an entity's balance sheet to its market or fair value. Not satisfied with creating grand fantasies on stage, it
seems they may have, according to the SEC, also performed some creative artifice on the company's financial statements. In July 2005, several EBS executives were tried on various charges of fraud, insider trading, and money laundering. The vendor had never before done business with Navistar. (a) Action rights. 059402_01_ch3_p069-116.indd 106
7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 107 Beazer's Anti-fraud Violations: Section 17(a) of the Exchange Act and Rule 10b-5 Thereunder 18. High Wire provided voice-over internet protocol primarily to companies other than Buca. These transactions could be used to do any of the following
• Hide the company's debt. www.washingtonpost.com. "Dunlap's Ax Falls— 6,000 Times—At Sunbeam," Wall Street Journal. Based on this analysis, she decides that it had been hard to explain to members of his 4,000-person sales force why investors were told
that WorldCom's revenue was increasing while the sales force knew that revenue was declining (Faber, 2003). To this day, it remains a mystery as to why the SEC did not object to that subsequent letter from Enron. Beazer consented to the entry of this Order without admitting or denying the findings. Consolidated Balance Sheets (In thousands,
except per share data) Years Ended December 31, 2007 2006 2005 Revenues Cost of revenues Co
from operations Other income (expense) Interest expense Interest income (loss) before taxes Income (lo
2,215 18,784 17,114 12,231 13,790 10,698 443 24,931 (6,147) 564 13,685 (20,396) 12,161 7,522 423 20,106 (2,992) 634 6,827 (10,453) 4,467 2,323 340 7,130 5,101 651 3,334 1,116 (98) (2,781) 2,736 2,061 2,500 - 8 6 5,146 (714) (15,250) (11,167) - - + (15,250) (11,167) + (621) 52 - 16 (553) 563 - 563 + 8 0.06 0.04 (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.76) + (0.7
20,185 (0.70) $ (0.70) $ (0.70) $ 16,048 16,048 9,924 12,849 Basin Water, Inc. 28). Jackson to be identified as the author of this work have been asserted by him in accordance with the Copyright, Designs and Patents Act 1988. The Third and Final Report of 2004 did not recommend that claims be pursued against the Internal Audit Department staff. "But it's
not always easy to know when you're doing that." Indeed, it was not as if Fastow acted alone. The company could be hiding a buildup in receivables by accelerating a portion of their liquidation into cash. Mulligan, Thomas S. "The Monster That Ate Wall Street," Newsweek.
059402 01 ch1 p025-046.indd 46 (b) One of the outside directors is a high school teacher. The whole point in auditing schedules is to test their support of the financial statements. At December 31, 2007, long-term notes receivable consist of non-interest bearing notes receivable from VL Capital, due in 72 monthly installments of $63 beginning April
2008, with a net present value of $3,353, calculated using an imputed interest rate of 5.0% per annum. • Cosmo Corigliano, Anne Pember, and Casper Sabatino, three of Shelton's co-conspirators, each pleaded guilty in federal courts under plea agreements in which "the three defendants admitted participating in the conspiracy and acting under the
instruction of their superiors" ("E. Shortly after the final 059402 01 ch3 p069-116.indd 104 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 105 house in a development had been sold, the balance in the land inventory account would be at or near zero. In December, Push approached Pull with the suggestion that Pull place its upcoming
April order immediately. In respect of its acquisition of Coleman, Signature Brands, and First Alert, Sunbeam planned to eliminate 6,400 jobs and close 8 of 24 plants. Cooper noted this as suspicious, but not clearly illegal. "Fast and Loose at WorldCom: Lack of Controls, Pressure to Grow Set Stage for Financial Deceptions," Washington Post. In
December 2008, when the collapse of BLMIS was virtually certain, Madoff agreed with others to send the $300 million that remained in the IA accounts to preferred employees, family members, and friends. Sham Donations from Vendors Billed Back to the Company 25. Lehman used the cash from the Repo 105 transaction to pay down other
liabilities, thereby reducing both the total liabilities and the total assets reported on its balance sheet and lowering its leverage ratios. Using this sale as evidence of the market value of its investment in Emperor, recognizing the alleged appreciation in value as current income
When a customer ordered items for the next quarter, Sensormatic sometimes shipped the goods early in order to receive a fair, independent opinion and on the relationship between the auditors and all those who may use the financial statements,
should lead auditors to better understand their duties and to better understand why they must not accept limits on the scope of their audits without qualifying their reports. A criminal investigation against Mozilo was never officially announced and was quietly dropped in February 2011. In fact, the company's true loss in fiscal 1997 was at least $83.60 and their audits without qualifying their reports.
million. Examine these extracts from Collin Company's income statements of cash flow for the previous three years. Explain what is meant by a "round-trip transaction." (b) Improper disclosure of non-GAAP financial measures. The investor accounts for its share of the investor accounts from Collin Company's income using the equity method. Furthermore, he had to
work out how LJM1 would handle the loss if the Rhythms shares fell in price. • Identify the role of easy credit in the way. Financial Accounting Standards Board. CUC is presented in this chapter as an example of overstating revenue by the use of
fictitious revenue. Deferred revenue decreases as a percentage of total revenue decreases as a percentage of total revenue decreases as a percentage of total revenue recognition. This could indicate improper revenue recognition. This could indicate improper capitalization of expenses; for example, the classification of expenses as PPE. "Ex-WorldCom Executive Sentenced to Prison." August 5, 2005. "Adelphia Founder John Rigas
Found Guilty." July 8, 2004. Pickert, Kate. "The Big Lie: Inside the Rise and Fraud of WorldCom," CNBC News Transcripts. In the case of employment compensation, many would argue in favor of extra distribution of benefits on the basis of merit, contribution, or effort. The transactions discussed in the previous paragraph raised suspicions among the
more junior members of Buca's accounting staff. Enron's expertise did not 059402_01_ch7_p226-291.indd 239 7/7/14 9:08 AM 240 Chapter 7 • Enron and the Tale of the Golden Goose transfer well to the retail division of supplying and managing electricity services, and this venture became rather problematic. In addition, FINRA Rule 3130 requires
the CEO of a member firm to certify annually, inter alia, that the member has established, reviewed and tested written compliance with the federal securities laws. The Land Inventory Accounts. It was extremely difficult to get a foothold in this industry, and Azurix was
plagued with problems from beginning to end even though Mark was a hard worker and was always ready to fly around the world to drum up business. Describe the role of Cynthia Cooper and the rest of WorldCom's internal audit team in revealing the accounting frauds at WorldCom. ("Financial Crimes Report," 2011) The number of corporate frauds
cases pursued by the FBI has grown steadily since 2007. • Examine extracts from the selected financial statements from Basin Water, Inc., for the fiscal years ended 2005, 2006, and 2007. She developed these international projects with gusto. This way, if the stock price fell by the end of 1999, Fastow reasoned that he did not have to devalue this
investment because he had the right to sell it at $56 per share in June 2004, www.lockheedmartin.com. While the business model evolved, the control framework did not and that exposed these firms to significant risks. They decided that they should get rid of Dunlap and Kersh by accepting their offers to resign as tendered at the previous board
meeting. agreed that it was no longer possible to disguise WorldCom's rising ratio of expenses to revenue by reducing various reserves on WorldCom's general ledger. "Dodd-Frank and the Need for Ethics." ABA Trusts and Investments, July/August. According to numerous reports, Angelo Mozilo (cofounder of Countrywide with David Loeb4)
established Countrywide with the passion of a true believer in the benefits of homeownership. The SOX Report succinctly stated Edison's situation: The Commission did not find that Edison's revenue recognition practices c ontravene GAAP or that earnings were misstated. Taking this into consideration, the Examiner pointed out, "Given this focus on
operational issues, it was a credit to the personnel of the Internal Audit Department that they investigated the line cost capitalization issue in 2002" (First Interim Report, 2002, p. Therefore, hints in financial statements and notes are instructive for telltale signs of problematic SPEs. Enron's SPEs were hidden mainly among its investments in
with a fixed-cost element had remained a suspiciously constant percentage as sales revenue declined. 059402_01_ch1_p025-046.indd 34 7/7/14 8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud 35 The expensive, complex, and often vague internal control requirements of the contentious and much-maligned Section 404 of SOX
in the development of Enron's "Get Shorty" scheme, which "involved Enron's selling power to the state at high prices in the day-ahead market and then buying it back the next day at much lower prices. When the sales-to-total-assets ratio declines or the ratio of sales to a specific asset declines, the user of financial statements should be alert to the
permission from the SEC to use mark-to-market accounting. There was no fully deregulated market to produce market prices. To get a truly dramatic, aggressive cost-cutting plan together, Dunlap turned to a long-trusted consultant at Coopers & Lybrand to head the project. If the days' sales in inventory increase significantly, even if the cause is not
the actual overstatement of inventory, it is an alert to the fact that sales are not keeping up with production. Comment on the risk inherent in this form of financing. 243). Beginning at least by the second quarter of 2006, Beazer, acting through certain officers and employees, began to reverse the excess reserves existing in the land inventory
accounts, which increased then-current period earnings. In attempting to sell its electricity, Enron had to aggressively seek business by promising various other companies and state organizations that it could provide their power supplies at rates that were cheaper than the rates they were currently paying. When a company sells its accounts
receivable, it is important to deduct the amount received on the sale from CFFO before comparing CFFO to operating income when looking for signals of overstatement of bad debt expense. The partial settlement provides that the amount of disgorgement and/or civil penalty to be paid by Peregrine
if any, shall be determined at a later date. In another area, response to the meltdown of the mortgage-backed securities market, the SEC has proposed rules that will protect investors by: • Increasing dramatically investors' visibility into the assets underlying all types of asset backed securities. (d) Meeting employees' expectations. Berthelsen,
Christian, and Mark Martin. Haddad, Annette. This is a prevalent method of moving expenses from current periods to future periods. Sullivan commuted from his home in Florida to a condo in Mississippi, where he seemed to be almost obsessive about his job and often worked into the early hours of the morning. In May 2010, he was awarded the
prestigious Evan C. (b) Expanding the mandate of Fannie Mae to include the purchase of mortgages that were not government-guaranteed. The Board estimates a final update will be issued in the second half of 2014. For example, Enron purchased a couple of paper mills to begin a market for trading pulp and paper. Levitt, Arthur. Allegheny (AHERF)
is presented in this chapter mainly as an example of understating expenses via: (a) Improper capitalization of expenses. According to the SEC, Highland Video did not operate a cable service and did not need the digital converters. This could present a misleading picture. If the value of a company's beginning inventory is overstated but its ending to the SEC, Highland Video did not operate a cable service and did not need the digital converters.
inventory is correctly stated, then: (a) Its cost of goods sold expense will be understated. . 111) However, in the mortgage industry, more and more nonconforming loans were urchased, pooled, and segmented into tranches of different grades of risk and then sold to p investors as mortgage-backed securities. IRS-Criminal Investigation is proud to
bring our financial investigative skills to this complex joint investigation and be part of the team that is helping to untangle the web of lies and sort out the culpabilities of the individuals involved. It was now 1996, and these were giddy times for Wall Street. The salient lesson was that these gatekeepers can also act as enablers. By late 1975, Lockheed
had capitalized $500 million in TriStar development costs (Schilit, 2002). For example, in December 2000, the Mahonia project produced $330 million of illusory CFFO on one contract alone. "BofA's Countrywide Found Liable for Defrauding Fannie Mae."
engines and the company would sell these engines only to Ford for certain specified vehicles. External auditors were collecting ever-escalating consulting fees from the same clients for whom they performed "independent" audits. from 1997 through 2000" (LR 19191, 2005). The stick ingredient in Dunlap's carrot-and-stick approach was the raw fear
he instilled in everybody who worked for him. Kirk, 126, 129 Shipments false recognition of early, 120 slow shipping, 120 Shore, Andrew, 72, 87, 90 Shrinkage, 199 The loss of inventory between the point of production or purchase from the vendor and the point of sale. Ebbers decided that he had to get more customers and bandwidth—and sell the
bandwidth cheaper than the other small-town competitors. 7/7/14 9:15 AM 370 References SOX Report. October 2007. Signal #1: Rise in Franchise acquisition rights" could be an indication that too many franchises have been sold and that some are being repurchased because
franchisees are encroaching on each other. Gadel ("Gadel"), Buca's former Chief Financial Officer and Daniel J. In August 2000, Enron's stock was at an all-time high, trading at $90 a share. He was the 16th ex-Enron executive to plead guilty" (Hays, 2006). 353 32. Give reasons for your answer. For example, one can invest in a copper derivative
security that requires that the holder must be paid an amount determined by reference to the level of a copper price index on a specific date. "Conflicts of Interest and Risk Governance." U.S. Securities and Exchange Commission. Allowance for loan losses not growing in proportion to increases in riskier loans or in proportion to increases in troubled
loans. On the contrary, however, now neither the CEO nor his deputy had any deep broadband knowledge or experience, and the result was disastrous. Commenting on the convoluted, contrived set of SPEs involved in the exchange, the Powers Report (2002) concluded, "We do not know why Swap Sub was used, although a reasonable inference is
that it was used to shield LJM1 from legal liability in any derivative transactions with Enron" (2002, p. PARAGRAPHS 33-43 FROM AAER 3165 Warranty Reserve 33. By June 2000, BellSouth owned 89 percent of Telefonia. Henriques, Dana. (d) Decreased net income. Adamo. The growth of Enron's guaranteed liabilities over the three-year period from
1998 to 2000 was quite staggering, as can been from Table 7.3. 5 In post-Enron accounting, we are less likely to find a disclosure of such a guarantee would probably lead to the entity being classified as a VIE and to its consolidation by the entity's primary beneficiary in terms of FIN 46(R).
encouraged others to tamper with financial statement disclosures—and misled those who trusted them. The improperly capitalized payments involved both the mischaracterization of the work of genuine independent contractors as a capital expense. The new
management team began what would be a recurring theme for Sunbeam—team members instituted an aggressive downsizing program whereby they cut one-third of the company's jobs and sold off a number of the product lines. At the core, both schools have the concept of equality in common: "Distributive justice, both universalism and
communitarianism agree, is treating persons equally" (Kellenberger, 1995). Dunlap managed to sell Scott Paper to Kimberly-Clark in July 1995 and he left Scott Paper $100 million the richer. On January 1, Khaan Company obtained a $30,000 loan from Raptorex Company. Boards of directors, 32-33, 37 7/7/14 9:17 AM Glindex 385 Boom-bust cycles
326-327 Borget, Louis, 230 Born, Brooksley, 331 Boston Business Journal, 48 Boynton, Richard, 77 Brazil, Cuiába Power Plant in, 257-259 Bribery, 301, 302 Brown, Karen, 204 Brown, William, 264 Bubble, 326-327 An inflated price for an asset that is not
justified on the grounds of its actual value. Rite Aid failed to write down its inventory amount for the full amount of the
                                                                                                                                                                    that it suffered. Framed this way, ethics is a topic of enormous significance to anyone whose job it is to seek to promote compliance with the federal securities laws. With wry humor, Galbraith observed that indispensable
aspects of the speculative boom mood include "an inordinate desire to get rich quickly with a minimum of physical effort" (p. "Dad, you're not famous," he said, "you're infamous." Fastow, who served more than five years in federal prison for securities fraud, recounted the arc of this journey with candor and conciliation to Tuck students on October 8
during an event moderated by Richard Shreve, adjunct professor of business ethics at Tuck. (c) CFFO will be stated as $39,000. Nonperforming loans are loans on which interest recognition has been suspended until realized because of doubts as to the borrower's ability to repay principal and interest. aggressive policy of, 93 conditions for, 81
fictitious, 126-129 improper, 117-131 improper, 117-131 improper timing of, 80-84, 90-94, 119-120, 122-125 premature, 121 Revenue shifting, 123 Revenue streams, changes in, 125 Rhythms NetConnections, 255-257 Rice, Ken, 242 Richter, Jeffrey, 246, 277 Rigas, James, 300 Rigas, John J., 295, 296, 298, 300 Rigas, Timothy, 298, 300 Rigas Entities, 296-298 Rights, 246, 277 Rigas, James, 300 Rigas, John J., 295, 296, 298, 300 Rigas, John J., 296, 298, 30
classification of, 56 Rights-and-duties decision-making approach, 55-57 Risk management, 349-350 Rite Aid, 199-204, 202t, 209-212 7/7/14 9:17 AM 398 Glindex Round-trip transactions, often of the same product, in order to create a false impression
of business activity or revenue" (Sox Report, 2002, p. While senior management did receive oral assurances from Navistar senior managers that the * The Company did not file an adjusted consolidated statement of operations for fiscal year 2002 or for the 2002 quarterly periods. Foley FCPA Enforcement: SEC and DOJ Enforcement Actions and
Opinions. For instance, is it permissible to do the right action for the wrong reasons (e.g., to gain fame or acclaim) or to do the wrong thing for good reasons (e.g., to embezzle money from a Fortune 500 company and give it to the poor)? Angelo Mozilo, David Sambol, and Eric Sieracki.SACV09-03994. March 18, 1998a. Specifically, in his capacity as
2012. Although Enron did not fully disclose all the guarantees or the fact that it was likely the entities would default and that Enron itself would be liable for the guaranteed amounts, these notes were unmistakable red flags due to the magnitude of Enron's unconsolidated affiliates and its related-party transactions with them. TierOne was shut down
by OTS on June 4, 2010, and filed for bankruptcy later that month. Carolyn B. WorldCom's was the fuel that WorldCom's was the fuel that worldCom's biggest original lender of single-family mortgages, and the company continued to grow. The ethics, ability, management
style, and track record of the leadership of the company should be the first piece of evidence an analyst or investor looks at in conjunction with examining financial reports for credibility. Knigge, Michael. In a speech to the AICPA National Healthcare Industry Conference in August 2000, SEC attorney Stephen Weinstein pointed out that "the
Disclosure Reports were made available to the public through the Repositories and were the most easily accessible source of information for investors and potential investors and potential investors in AHERF bonds." 059402_01_ch6_p191-225.indd 204 7/7/14 9:05 AM Chapter 6 • Abracadabra 205 AHERF's Fictitious Financial Reporting Schemes AHERF's Fictitious
Financial Reporting Scheme of Understating Bad Debts According to the SEC, during 1996, AHERF's senior management became aware that there were significant problems with the collection of Delaware Valley's patient accounts receivable. Community Foundation for Palm Beach and Martin Counties. Were they something that you could have
looked at and seen? (b) Recording contingent sales as current- period sales. Between his military training and his angry management style, he was soon giving unpopular orders for layoffs. Lublin, Joann S., and Oscar Suris. It later "discovered" that these reserves were not needed, and it then released those cookie-jar reserves back into earnings. 45).
Pearson Education Limited Edinburgh Gate Harlow Essex CM20 2JE England and Associated Companies throughout the world Wisit us on the World Wide Web at: www.pearsonglobaleditions.com © Pearson Education Limited 2015 The rights of Cecil W. liaison between the companies, and much of the work was . The obligation to absorb losses of the
entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity of the right to receive benefits from the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity that could potentially be significant to the variable interest entity or the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the entity of the right to receive benefits from the right to receive benefi
Releases." U.S. Securities and Exchange Commission. WorldCom needed to continue recording unnecessary reserves. Do you believe that principles-based accounting standards would be more effective than rules-based accounting standards would be more effective than rules-based accounting standards for financial reporting? Power Failure: The Inside Story of the Collapse of Enron. First, it had to be controlled
by someone independent of Enron. "Xerox, KPMG Settle Investor Suit." CFO.com. Contracts in process Inventories Deferred income taxes Property, PLANT AND EQUIPMENT, NET GOODWILL AND OTHER INTANGIBLE ASSETS, NET LONG-TERM INVESTMENTS DEFERRED
of fictitious revenue. The assets that had been transferred to the Raptors fell in value, and Enron's stock plunged at the same time. By November 2001, an Enron share was worth less than $1. Krispy Kreme's internally appointed independent investigation into its business practices concluded that the company's accounting errors were intentional. Van
Lobels Sels. Eaglesham, Jean, and Liz Rappaport. Buca, through Gadel and Skrypek, improperly capitalized at least $1 million in payments to independent contractors. June 27, 2011. In October 2002, the Wall Street Journal reported: Timothy Norris Belden, 35 years old, pleaded guilty to a single count of fraud. Securities and Exchange Commission
Accounting and Auditing Enforcement Release, April 27, 1998. Ebbers's acquisition price of over $6 billion for Intermedia in July 2001 was generally considered an overpayment. "Edison Schools Leaving Publicly Traded Stage." July 14, 2003. In your opinion, what role does intention play in moral decision making? The CEO and CFO debate how best
to spend the money. Relevant accounting rules provided that such start-up costs could be deferred only if there existed an objectively verified and measured contractual guarantee of reimbursement. A shift toward riskier loans could be evidenced by disclosure of an increase in the percentage of: (a) High LTV loans. Not surprisingly, there were
numerous problems with this devious plan. McGowan took over from Goeken as CEO in 1974. Phillipa Foot emphasized the "four cardinal virtues: courage, temperance, wisdom, and justice" (qtd. In most cases, senior management compensation agreements included stock options that would provide significant additional remuneration if analysts'
earnings expectations were met. At December 31 Nonperforming loans (1) Real estate owned, net (2) Total nonperforming assets Troubled debt restructurings 2006 2005 (Dollars in thousands) $30,050 $14,405 5,264 2,446 35,314 16,851 8,904 5,180 Total nonperforming assets and troubled debt restructurings $44,218 $22,031 (1) Includes all loans
90 or more days delinquent and all uncollected accrued interest is fully reserved. 7/7/14 8:59 AM 64 Chapter 2 • Ethics at Work equal treatment of the sexes, do you think that the business environment is sometimes unfair to women? In effect, Enron was actually recording the appreciation of its own stock on its income statement
059402_01_GLINDEX_p383-401.indd 392 Improper expense recognition, 192-198 The omission of expenses or movement of expenses from the financial statements in the period in which they should be recorded to an earlier or later period. www.fbi.gov 059402_01_ch1_p025-046.indd 29 7/7/14 8:58 AM 30 Chapter 1 • Introduction to the Problem
of Accounting Fraud Increasingly, corporate frauds are also being exposed through the relatively new Dodd-Frank Whistleblower Program. March 24, 2007. Andrews, Suzanna. It also had natural gas exploration plants, productions plants, hundreds of gas wells, and other energy businesses. (c) Improper use of merger reserves and improper
capitalization of expenses. In spite of this, the company still raised $750 million on the debt offering. Ebbers was aware of the leases that AT&T was forced to option out. Because of his long-term doubts about Dunlap, on the morning of April 3, 1998,
just before Sunbeam's press release that it was not going to make its estimates for the first quarter of 1998, Shore was the first analyst to put in a downgrade on Sunbeam stock. Signal #6: The Use of "Death-Spiral" Financing when a company uses death- spiral financing, it is a signal that the company's future earnings per share could be diluted by
financial analysts, Adelphia misrepresented the extent to which it had upgraded its cable plant. Fool's Gold. ** NI = net income. Ethical Auditors determines that Stylish Shoes has an unexpected surplus of $200,000. A number of employees left. Byrne reported conversations with employees and managers at the McMinnville, Tennessee plant
indicating that this was one of the most profitable plants at Sunbeam. New York Stock Exchange Press Release. Other SOX Regulations In addition to Sections 404 and 302, SOX established legislation covering a variety of other issues. CASE STUDY TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read extracts from the SEC Complaint filed on September 25, 2012, against TierOne Bank • Read ex
Bank. When a company has multiple-element contracts and there is a proportional increase in a revenue stream that is more quickly recognized more slowly. 152). According to White's friends, he "despised Dunlap" (Byrne, 2003, p. • Explain the main elements of Dodd-Frank reform. Management
believes that the warranty reserve is appropriate; however, actual claims incurred could differ from the original estimates, requiring adjustments to the reserve. 2. This trick worked, and Enron was able to buy up spot oil and offload enough of Borget's contracts in the next 60 days for the company to survive. • Requiring securitizers—in conjunction
with our banking colleagues—to keep skin in the game, giving them an incentive to double-check originators' underwriting practices. (Jeter, 2003) Virtually every U.S. business magazine, newspaper, and journal was impressed with Ebbers and gushed that he was a brilliant entrepreneur. Show supporting calculations for your answer. As a result,
Buca effectively capitalized the expense of the conference. Report and Recommendations by the Majority Staff of the Joint Economic Committee. This occurred a few days after the announcement of Sunbeam's acquisition of three companies in one day:
Coleman, First Alert, and Signature Brands. (b) Utilitarianism. After reading paragraphs 21 and 22 of the SEC's Complaint filed against Buca, what, if any, internal control weakness do you see that was 315 allegedly present at both
companies? . (Gallu, 2012) According to the Wall Street Journal, "no former Lehman top executives, including CEO Richard Fuld, have been charged with any criminal behavior" (Eaglesham & Rappaport, 2011). (Bankruptcy Report #2, 2003, p. The merchandise was received by the retailer on January 3. November 13, 1996. Michaelson, Adam. It was
signed by the ousted CEO after he left the company, backdated almost a year, and worth millions of dollars more than his official deal. The Engine Division booked these rebates, often using the same form letter (which in certain instances was back-dated) that falsely stated that the rebate was based on past purchases and had no contingencies. The
intellectual virtue of practical wisdom is, according to Aristotle, a prerequisite for all the other virtues. First, as Bryce (2002) explained, JEDI had to be kept out of Enron's financial statements. • Employees may choose to contribute to retirement plans that invest in a company's stock, but they may decide on different plans if they were presented with
correct financial statements. said it would restate prior period financial statements to reflect the consolidation retroactive to 1999, which would have the effect of decreasing Enron's net income by $95 million in 1999 and $8 million in 2000. The Company's eventual restatement of these rebates and receivables totaled $9.7 million of pre-tax income in
2004 and $8.5 million in 2003, which represented 27.7 percent, respectively, of the restated loss before income taxes for those years. www.dailyitem.com. Sullivan, 2002) Then in the first quarter of 2001, in his desperation, Sullivan began a further ploy. 256, 266). It had an electrifying effect. The CPUC initiated a 10 percent price cut
for the end users and capped the amount paid by the utilities to the power companies at $750 per megawatt hour, but did not cap the amount paid for power purchased from outside California. Signal #5: Securitization of Current Assets — Securitization of Current 
instrument assets— indicate that a company may be experiencing cash-flow problems and that it needs to accelerate the realization (or liquidated in the ordinary course of business. Ebbers is scheduled to be released from prison in July 2028 ("Ebbers' wife files . . . ," 2008). 2007. It is now
the sixth-largest bankruptcy in U.S. history (Ovide, 2011). 303). With the help of lobbying from Arthur Andersen, the Securities and Exchange Commission (SEC) granted its permission to Enron to use mark-to-market accounting in its Gas Services division. Overstatement of Revenue Scheme: (Note: This question refers to the Sale-Leaseback
Transactions.) According to AAER 2884, Beazer Homes overstated its 2006 revenues by $117 million and understated its cumulative revenue for the first two guarters of 2007 by 2.6 million. September 24, 2008. The amounts for 2006, in Table 9.3, are the amounts stated in the original 10-K report's balance sheet that was first available to users. But
             middle of March its stock has fallen nearly 50% from $52 to a recent $28.... 059402 01 REF p365-382.indd 375 Eichenwald, Kurt, and Matt Richtel. 059402 01 ch5 p144-190.indd 181 7/7/14 9:04 AM 182 Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom FINANCIAL STATEMENTS UNITED STATES SECURITIES AND
EXCHANGE COMMISSION Washington, D.C. 20549 Extracts from FORM 10-K2 Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the fiscal years 1998-2002 TYCO INTERNATIONAL LTD. Healthcare System Open for Patients." www.ncbi.nlm.nih.gov. Modern philosophy is skeptical of Aristotle's understanding
of the human telos that grounds his virtues, and others worry that deriving virtues for a certain group may lead to moral relativism. As 059402 01 ch5 p144-190.indd 161 7/7/14 9:04 AM 162 Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom Wizardry: From WorldCom to WorldCom t
stated the following: The evidence is not in dispute: Arthur Andersen had no knowledge of the improper capitalization of line costs or the Company's improper manipulation of its line cost, revenue and other reserves to inflate its earnings. Perhaps he believed that the problems had not been caused by the downsizing. An auditor who knowingly fails to
qualify incorrect financial statements fails to justly distribute the correct information. However, the high number of SEC enforcement actions revealed too many auditors who either accepted scope limitations on their audits—such as not demanding full access to the entire general ledger and not issuing a disclaimer or qualified report on the financial
statements—or who knowingly vielded to incorrect financial statements. Boston: Harvard Business Press, In 1997, Livent transferred preproduction costs and operating expenses "totaling $15 million from six different shows in thirty locations to three different fixed asset accounts" (AAER 1095, 1999), 059402 01 ch7 p226-291, indd 237 7/7/14 9:08
AM 238 Chapter 7 • Enron and the Tale of the Golden Goose Mark worked hard to renegotiate the contract and get the venture back on track, lowering the MSEB a 15 percent share in the project. Although Kopper was not a senior officer at Enron, the fact that he was an Enron employee meant it was likely
that Chewco would fail the off-balance-sheet SPE test on the grounds that Chewco was not controlled independently of Enron. Auditing and Monitoring. (A put option is a financial instrument that gives the owner the right to sell an ownership interest, usually an equity interest in another company, at a specified price on a specified future date.) The
owner of the interest has the option, or choice, to sell the interest at that price on the future date. Beginning in September 2001 and continuing until October 2002, when the Automaker cancelled the Agreement, Company management repeatedly sought such a guarantee in the form of a letter. Acceleration of future quarters' sales of Sunbeam into
the present quarter provided a correct impression of the company's results of operations in the present period. 105, 106) An Overview of WorldCom used to overstate its earnings: 1. What were they thinking? The goods were
shipped to Pull in May the next year. On the deontologist, the most important issue in morality is to do the right to be honest, then avoiding lying and telling the absolute truth is always right, irrespective of the
consequences. In its early years, Edison managed approximately 130 elementary and secondary public schools in about 22 states. The Rhythms transaction was actually the motivation for the formation of LJM1. (Discounted future cash flows refer to the present value of the future cash that a company expects to receive or pay.) By choosing a
particular discount rate, a leasing company can manipulate its reported 4 KPMG consented to the entry of this order without admitting or denying the finding therein, except as to the Commission's jurisdiction over it and the subject matter of these proceedings. 17 059402 01 FM p001-024 indd 17 7/7/14 8:57 AM 18 Preface Intended Audience This
book has been written for instructors and students of undergraduate and graduate courses to be used in the following areas: • Accounting Ethics and Business Ethics • Financial Accounting Ethics and Business Ethics • Accounting Ethics and Business Ethics • Financial Accounting Ethics and Business Ethics • Accounting Ethics and Business Ethics • Financial Accounting Ethics and Business Ethics • Financial Accounting Ethics • 
Features of Detecting Accounting Fraud: Analysis and Ethics • In addition to analyzing the more well-known case studies (Sunbeam, WorldCom, and Countrywide), the book presents a number of new and unusual real-world case studies for students to examine. Signal #3: Regular Vendor Not on Accounts Payable List If you have access to the
company's internal records, you can test lack of accounts payable, and then reconciling the amount accrued with the vendors' statement of amounts owing. According to examples given by the prosecutor, Rigas used Adelphia's funds to purchase two
Christmas trees for $6,000 and to spend $26 million on 3,600 acres of land surrounding his house to ensure that the view would never be obstructed. When WorldCom was doing well in the 1990s, Ebbers began applying for bank loans on his own behalf or for his other business interests. The producers would later have to deliver an assured supply of
gas at fixed prices, and Skilling knew what price to set for the supplies of gas in order to make a profit on the spread because Enron already had contracts to sell the gas at fixed prices in the future. Asks students to address relevant ethical issues in the "Ethics at Work" sections throughout the book. 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry:
From WorldCom to WorldCom to WorldCom to WorldCom to WorldCom to SEC found that Rite Aid allegedly "improperly reduced cost of goods sold in this way, it did so for the first three quarters of the
year and then reversed the entries in the fourth quarter of each year. 33. This point is actually not in dispute. At the same time, Enron could account for 50 percent of JEDI's profits in its income statement. Of course, we now know that Enron was burning through cash at an amazing rate while it was pretending to have a healthy CFFO. Borget had
committed the company to delivering a staggering $1.5 billion of oil—oil that it did not have. Ultimately, the reason that a company invests in assets is to generate revenue with those assets. Perhaps Kimberly-Clark's troubles with Scott Paper, after Dunlap's alleged turnaround, had left Wall Street a little wary of Dunlap's cost-cutting strategies. He
became convinced that it was time for LDDS to go public. Indeed, Sunbeam, in an April 3 press release just after its debt offering, announced that it expected to show a loss for the first quarter of 1998. Mondout, Patrick. AAER 1133. For Discussion 31. Some of TierOne's real estate loans were eventually foreclosed upon and the underlying collateral
became the property of the bank, or OREO. Considering justice in terms of Case Study Peter Madoff, Former Chief Compliance Officer and Senior Managing Director of Bernard L. Abide attached an article from the Fort Worth Weekly Online of May 16, 2002, about Kim Emigh, a WorldCom 059402 01 ch5 p144-190 indd 164 7/7/14 9:04 AM Chapter
5 • WorldCom Wizardry: From WorldCom to WorldCom to WorldCom to Eccounting for PPE. Knowing the financial difficulties of a number of company employees, the CEO thinks that the greatest good for the greatest number will be best served if the excess is split among the employees. Use the
following data for Questions 25 and 26: XYZ Company has finalized its financial statements for its fiscal year ended December 31. A potential whistleblower who is deciding whether or not to reveal unethical or unlawful practices may use one of the three approaches. It is important for users of financial statements to be aware of different
methods and to question why one method was
                                                                          rather than another. The Powers Report (2002) stated: "As a result of the buyout, Kopper and Dodson received an enormous return on their $125,000 investment in Chewco. 238), Eichenwald (2005, p. The first problem was that Mark got an up-front bonus on the signing of many of these huge
deals. Securities and Exchange Commission v. We appreciate it." Whereupon Skilling snapped, "Asshole." (Qtd. Between spectacular losses and extravagant expenditures, corporate profits soon evaporated and the unfortunate Buckley was fired in 1986. It was nothing we were paid for, so who cares?" (qtd. BLMIS
collapsed before the funds were ever disbursed. In the last quarter of 1996, it took a very significant restructuring charge. Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges Peregrine Systems, Inc., Civil Action No. 03 CV 1276 K (LAB) (S.D. Cal.) (June 30, 2003) SEC Charges P
the market, which was blinded by the dazzling stock prices. Signal #8: Press Releases Stating Inability to Meet Sales Estimates Press releases indicating that previous sales growth estimates will not be met are clear warning signals. Grubman, for example, had 059402 01 ch5 p144-190.indd 148 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry
From WorldCom to WorldCom to WorldCom 149 lied about having "attended the Massachusetts Institute of Technology" (Jeter, 2003, p. BellSouth is a telecommunications corporation headquartered in Atlanta, Georgia. Like Fannie Mae, Freddie Mac also accelerated the funding and issue of mortgage loans by buying up loans from mortgage lenders, freeing up
these lenders to make further home loans. Calculate Navistar's "Product Warranty Accrual" as a percentage of sales of 059402 01 ch6 p191-225.indd 215 manufactured products for fiscal years ended 2003; then comment on your results. The responsibility of management to institute controls ensuring the integrity of the accounting
information captured was not clearly defined. GADEL and DANIEL J. TierOne's stock price dropped a further 54 percent over the next three trading days, from approximately $1.71 per share to $0.78 per share. Furthermore, via tranching traders could create securities that paid interest or principal only or made payments on whatever innovative
parts of the loans one could imagine. Special Purpose Entities (SPEs) are used to overstate earnings and understate debt via contrived transactions. Since March 1994, Beazer's common stock has been registered with the Commission pursuant to Section 12(b) of the Exchange Act and listed on the New York Stock Exchange under the symbol BZH.
059402 01 ch7 p226-291.indd 258 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 259 Riding high on his make-believe business acumen, Fastow also used LIM1 to make a brief investment in Osprey, which was part of the infamous Whitewing entity, one of Enron's wildest and most ambitious off-balance-sheet entities. AAER
1095. 0.\overline{5}94\overline{0}2 01 ch6 p191-225.indd 220 7/7/14 9:06 AM Chapter 6 • Abracadabra 221 Automaker had in fact committed to reimburse the Company should not have allowed the deferral because it had not received the
aforementioned written guarantee of reimbursement. WorldCom prepared its financial statements to meet the expectations of securities analysts despite needing to report actual earnings and accurate financial results. United States Bankruptcy 7/7/14 9:15 AM References 373 Court Southern District of New York in re:WorldCom Inc. The company
expected to receive a large order for $40,000 of lawn mowers from Pull Company, a major customer, in April the next year, for goods to be delivered to Pull in May. www.acfe.com. e. 43) Chapter Outline • The Electricity Fiasco in California • Enron's Fictitious
Financial Reporting Schemes • Signals of the Enron Frauds • Key Terms • Ethics at Work • Assignments • Case Study: Basin Water, Inc. "Make That 'Dr. Chainsaw." BloombergBusinessweek. . Wall Street applauded, but back home the workforce was restless. If Sunbeam was operating at such a great profit, why would it be burning through
operating cash? Zee wanted the goods to be shipped only in March the next year (FOB destination), and a clause to that effect was included in the sales contract. When such transactions involve off-balance-sheet entities, it is especially troubling. Scheme #2: The Abuse of SPEs The Powers Report (2002) of the U.S. Congressional Special Investigative
Committee on Enron stated that many of Enron's transactions involved "an accounting structure known as a 'special purpose entity'" (p. While important, this branch of ethics is beyond the scope of our discussion. In May 2002, the SEC issued a cease-and-desist order. 1 Whether a company has zero revenue and zero expense or positive revenue and
an equally positive expense—leading to zero net income—can influence an investor's or lender's perception of the company's results and financial position. June 22, 2004. What happened? T F 059402 01 ch9 p325-360.indd 350 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 3. The daily fluctuating spot prices of natural gas were just too volatile
Pervasive fear and silence. Because it was now guaranteed that Enron would make that minimum profit from selling the stocks to LJM1, Enron could use mark-to-market accounting to revalue the Rhythms stock and it could book at least that amount of profit. Ironically, California's bizarre regulations came into effect on April Fools' Day—April 1,
1998. AHERF grew very rapidly from its inception in Pittsburgh in 1983 to the largest nonprofit healthcare provider in Pennsylvania before its sudden decline and bankruptcy in Iuly 1998. VIEs must be consolidated into a company's group financial statements if the company is a primary beneficiary of the VIE. Specifically, in various guarters during
fiscal years 2000 through 2005, Beazer over-allocated land inventory expense to individual properties sold. Securities and Exchange Commission Accounting Enforcement Release, March 25, 1998. Refer to Beazer's financial statements for the following fiscal years: 2004–2007. On June 27, 2000, the U.S. Department of Justice filed a suit
to put a stop to the merger of the two telecom giants. 059402 01 ch5 p144-190.indd 185 7/7/14 9:04 AM 186 Chapter 5 • WorldCom Wizardry: From Wizardry: From Wizardry: From Wi
September 30, 2002 and 2001, respectively) (58.8) — 4.654.0 — Cumulative effect of accounting changes, net of tax $ (9.411.7) NET (LOSS) INCOME 2000 252.5 (9.411.7) NET (LOSS) income before cumulative effect of accounting changes 2001 (6.282.5) — (683.4) $ 3.970.6 — 4.519.9 — $ 4.519.9 Tyco
International Consolidated Balance Sheets 2001-20026 (in millions, except share data) SEPTEMBER 30, 2002 2001 ASSETS Current Assets: Cash and cash equivalents Restricted cash $ 6,186.8 $ 1,779.2 196.2 — Accounts receivables, less allowance for doubtful accounts ($629.1 at September 30, 2002 and $550.4 at September 30, 2001 5,848.6
6,453.2 Inventories 4,716.0 5,101.3 Deferred income taxes 1,338.1 980.2 Other current assets 1,478.9 1,532.3 19,764.6 15,846.2 — 10,598.0 581.6 2,342.4 Total current assets Net Assets of Discontinued Operations Tyco Global Network Property, Plant and Equipment, Net Goodwill, Net 9,969.5 9,970.3 26,093.2 23,264.0 Intangible Assets, Net
6,562.6 5,476.9 Other Assets 3,442.9 3,524.8 $66,414.4 $71,022.6 TOTAL ASSETS LIABILITIES AND SHAREHOLDERS' EQUITY Current Liabilities: Loans payable and current maturities of long-term debt.... (4) Based upon unpaid principal balance. Staff Report, U.S. House of Representatives, 111th Congress, Committee on Oversight and
Government Reform. Gadel and Skrypek eventually allowed Buca accounting employees to put any small repair or maintenance invoice that the company received into this account, regardless of whether the invoice represented a capital expense. LDDS suffered from high fixed costs coupled with a lack of technical knowledge and expertise in
optimizing the configuration of circuits, which resulted in high line costs. But mysteriously, a disclosure of these losses was nowhere to be found in Enron's financial statements. The company denied the bribery charges, which were never proven, but the nameless writer certainly proved to be correct in one respect: MSEB refused to pay for the power
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from Dabhol, saying it could not afford it. ("The Wall Falls," 1999) In hindsight, however, opponents of deregulation often cite the rescinding of Glass-Steagall as the biggest single regulatory cause in creating an environment for the financial meltdown of 2008. Calculate servicing revenue and financing revenue as a percentage of total revenue for

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years 1-3 and then comment on your findings. Signal #5: Parent Company Makes Later Adjustments to Increase Goodwill after an Acquisition — Adjustments that increase goodwill in a later period with respect to an acquisition — Adjustments that increase goodwill in a later period with respect to an acquisition — Adjustments that increase goodwill in a later period with respect to an acquisition — Adjustments that increase goodwill in a later period with respect to an acquisition are further signs that a company may be creating false reserves. In doing so, it incurred the after-tax charge of $544 million
($710 million pre-tax) that Enron disclosed on October 16, 2001, in its initial third quarter release" (Powers Report, 2002, p. With that purchase, LDDS became a public company's assets or liabilities with personal assets or liabilities of its major shareholders, officers, or directors is
a signal of poor internal control. "E. The housing bubble could be described as an inflated price for houses in which a house's price is not supported by the rents it could earn. Litigation Release No. 17837. • Explain Rite Aid's method of understating cost of goods sold. He learned that Sunbeam might contravene its debt covenants by the end of the
month and that huge loans could become repayable. "Into the Maw," Barron's. Flanagan and Clarke point out, "Rather than relying essentially on an imposed set of external regulations, guidelines and exemplars, the professional accountant's decisions, while reflecting community expectations, will of necessity be derived from each practitioner's
individual internalized decision-making processes" (2007, p. At one stage in Lay's early childp hood, after his parents' feed store had gone bankrupt, Lay and his family "bounced 059402_01_ch7_p226-291.indd 227 7/7/14 9:08 AM 228 Chapter 7 • Enron and the Tale of the Golden Goose around Missouri and Mississippi. Enron also invested 250,000 inve
shares of its preferred convertible stock in Whitewing, as well as $135.2 million of Enron notes. The SEC would later file charges "against nearly 100 individuals and Freddie Mac" (Schapiro, 2012). Enron should have reported the cash
received as cash flows from financing activities instead of from operating activities. Refer to Exhibit 7.4 for a copy of this diagram. The lack of enthusiasm was exacerbated by the superior attitudes of the Internet division. Furthermore, instead of paying cash for additional acquisitions, LDDS could pay for new companies simply by issuing LDDS
shares to the shareholders of those companies. He was looking for a new company to "turn around." (Quotes from Byrne, 2003, pp. Lou Pai, one of Skilling's chief traders, decided to take a huge gamble that prices would decrease. Do you see it primarily as a method of "improper timing of revenue," or as "fictitious revenue," or as "improper valuation
of revenue"? The main problem was that Talon was really another division of Enron and Enron was just shifting its losing assets to another part of itself; after all, what sort of a business would purchase only investments that were on the verge of collapse? Case Study BASIN WATER, INC*. Rhodes incurred other administrative expenses of $10,000 for
the year (ignoring taxes), which it paid itself. (c) Misclassifying part of its line-cost expense as goodwill. Gene Morse contrived to be testing a new software program in order to retrieve the journal entry source of items in the general ledger. October 24, 2012. Consolidated Balance Sheet 1999 (in millions, except share data) SEPTEMBER 30, 1999
CURRENT ASSETS: Cash and cash equivalents Receivables, less allowance for doubtful accounts of $329.8 in 1999 and $317.6 in 1998. LR. "Six Former Senior Executives of Xerox Settle SEC Enforcement Action Charging Them With Fraud." www.sec.gov. Sunbeam enticed customers to place future periods' sales orders early and recorded these as
current-period sales as part of its financial reporting scam. Business ethics is a type of applied ethics. In spite of that fact that Enron was hiding massive amounts of debt and interest via SPEs, the times-interest-earned ratio extracted from Enron's reported income statement was, nevertheless, a signal that the company may not have been able to
sustain its debt with its operating plan. In July 1998, Azurix purchased Wessex Water for $2.88 billion. 192). Indeed, they were compared unfavourably [sic] with Al Capone. Although Gadel and Skrypek knew of Micatrotto's improper reimbursements and helped prepare Buca's proxy statements, Buca's proxies never reported the payment of these
personal expenses as compensation to Micatrotto for the years 2000 through 2003. (An impaired asset refers to an asset whose carrying value is less than the fair or recoverable value.) This evidently inadvertent accounting failure certainly drew the attention of the Shareholders when the company suddenly wrote off over $400 million of the TriStar's
development costs in 1981, after the program had been losing a fortune for over a decade. According to the Examiner, the auditors—Arthur Andersen—did not demand total and simultaneous access to all of WorldCom's general ledger and journal entries. The press ran several articles on Dunlap in 1984, indicating that he was instilling fear into his
                                                                                            date by two days. Pursuant to Statement of Financial Accounting Standards ("SFAS") No. 5, Accounting for Contingencies - Appendix A; With Respect to Obligations Related to Product Warranties and Product Defects, warranty reserves must be established when it is
probable that a liability has been incurred and the amount of the loss can be reasonably estimated. Enron would a contract to a financial institution for the amount of the loss can be reasonably estimated. Enron would get the cash up front. Testosterone Inc. The loan accrues interest at a rate of 8 percent per annum with a term of two years. Adelphia
accounted for the transaction by reducing its debt by $101 million and crediting inventory by a corresponding amount. 75) The Bankruptcy Examiner concluded that the Whitewing Associates should have been climinated.
Maloney, Vice Chair. Through a concerted and deliberate effort to conceal information from the auditors, company executives "caused accounting records to be falsified, made false statements to the independent auditors, and intentionally circumvented the company's internal accounting controls" (AAER 1020, 1998). The company also paid over $24.
million in "personal margin loans and other debt of the Rigas family" (BR-6413, 2002). However, "The elevated number of exceptions resulted largely from Countrywide's use of exceptions as part of its matching strategy to introduce new guidelines and product changes" (June 4, 2009, par. Rep. One of Sunbeam's fictitious financial reporting schemes
was formally recording a revenue item in the financial statements in an earlier or later period in which the item should have been recorded. in Byrne, 2003, p. Crafty allocates the full cost of the printers that it purchases from Tricky to inventory. With reference to an off-balancesheet entity discussed in the text, explain how Enron
recognized profit on the appreciation of its own stock. January 14, 2004. The actual inception of WorldCom occurred when Murray Waldron, a businessman from Tennessee, decided to get into the business of reselling long-distance phone service in country towns. www.reuters.com. "These things were few and far between, but they did happen.
Clearly, companies must respond to changes and initiate changes. It is therefore important to examine the company's debt-equity ratio. The phony fees earned by Enron via the management and financing of the bogus entities really amounted to Enron managing and financing itself. Then their former high school coach took Brent Foster on a trip to
Seattle. Kellenberger, James. Ebbers (the CEO), Scott Sullivan (the CFO), and David Myers (the controller), as well as other members of WorldCom's senior personnel, were the toast of the town; they had almost everyone fooled. Meanwhile, all that happened after the restructuring was that the company did not have to account for the expenses that
were offset by the overstated cookie-jar reserves that had been created earlier. www.globalsecurity.org. September 28, 1998. GAAP also requires this revenue to be recognized over the life of the lease. Virtues, 51-53 Volcker Rule, 41 WilTel, 150 WorldCom, 30-31, 33, 34, 36, 144-175 acquisitions by, 149-156, 166-167 adjustments, 160t collapse of
162-166 failures at, 166-169 fictitious financial reporting schemes, 158-162 outcomes for, 175 problems at, 156-158 quarterly statements and balance sheets, 172t ratios, 171t signals of fraud at, 169-174 wizards of, 145-149 W X Waldron, Murray, 146 Walker, Richard, 126 Wal-Mart, 79 Warranty reserve, 218-220 Water privatization, 238 Watkins,
Sherron, 278 Weather derivative, 236 Whalley, Greg, 241 Whistleblowing, 30, 35, 40-41 White, Mary Jo, 28 White, Newt, 79-80 Whitewing Associates, 261-263 Xerox, 122-125, 271 059402 01 GLINDEX p383-401.indd 401 Y Yates, Buford, 165, 166, 175 Z Zisman, Stuart, 260 7/7/14 9:17 AM 059402 01 GLINDEX p383-401.indd 402 7/7/14 9:17 AM
059402 01 GLINDEX p383-401.indd 403 7/7/14 9:17 AM 059402 01 GLINDEX p383-401.indd 404 7/7/14 9:17 AM 059402 01 GLINDEX p383-401.indd 408 7/7/14 9:17 AM 059402
Deontology. Gadel and Skrypek participated in drafting Buca's proxy statements that materially understated the compensation of both Gadel and Joseph P. The deficient internal controls failed to provide adequate checks on certain employees' efforts to meet the Company's financial targets. Kant did not think that right action was necessarily
rewarded on Earth or that right action was accompanied by happiness in this life. January 17, 1999. In 1977, he combined with a few friends and began an expansion that led to nine hotels by failing to increase the reserve for bad debts.
the net accounts receivable is larger than it should be. In fact, he knew of such a man—Al Dunlap—who had done all this for Scott Paper to Kimberly-Clark at a huge profit. Waldron, Singleton, and Ebbers met with Waldron's friend, Bill Fields, in a coffee shop in Hattiesburg, Mississippi. In August
1997, Sidgmore had stated in an interview with Telecommunications Magazine, "We're seeing growth at an unprecedented level. Swibel. Nixon, Ron. The only changes to its working capital balances over the last year were that accounts payable increased by $1,000, and accounts payable increased by $5,000. This is a unprecedented level. Swibel.
transfer would allow WorldCom to defer recognizing a substantial portion of its current operating expenses, thereby allowing WorldCom to report higher earnings. The America DecisionMaking Model. "Madoff Is Sentenced to 150 Years for Ponzi Scheme," New York Times. However, "What investors didn't
know would have caused Sunbeam stock to suffer a total collapse" (Byrne, 2003, pp. (d) Bolt should not recognize a sale for either Item I or Item II. Dunlap's Carrot-and-stick Approach Dunlap structured control over his management team at Sunbeam with one of the most severe carrot-and-stick combinations ever implemented in U.S. business.
(Mark-to-market accounting refers to the revaluation of an asset or a liability on an entity's balance sheet to its market or fair value and the corresponding recording of the increased amount as income on the income statement or as other comprehensive income.) Although Enron was not primarily a financial services company, Skilling
believed that he had an argument for his division to use mark-to-market accounting on the grounds that if you perceive telling the truth as a duty, then it is an unassailable duty, and telling a lie is always wrong, irrespective of the consequences. (b) Pay-option ARM loans.
White could not tolerate the thought of a long stay in the environment that Dunlap was creating. Further, in an effort to make the Los Angeles production of Ragtime look more successful, senior management of Livent arranged for outside associates to purchase approximately $381,000 of tickets on personal credit cards and to make future ticket
purchases using personal checks. • Explain the rights-and-duties approach to ethical decision making. In the early years, after the introduction of the pay-option ARM loan product, before many of the loan payments reset, these loans had a lower
delinquency rate than the rest of the portfolio. Associated Press. • Describe Lockheed's failure to record its asset impairment. • It is "probable" that the company's books—for example, a liability for taxes or litigation or employee
severance payments. Understatement of bad debts expense. Eventually, Enron used vast interlocking sets of SPEs to borrow huge amounts of money and to transfer the money to itself. (See Signal #1.) 2. "Countrywide Financial Corp. He now works as an "independent accounting professional" ("The Defendants of the Enron Era," 2011). (d) Justice.
New York: Harper Business. According to the SEC's AAER 1555, Edison disclosed the existence and amount of its District-Paid Expenses, but did not properly offset them from revenues. The $12.8 million and the $13.3 million totals represent 12.5 percent, and 25.4 percent, respectively, of the Company's previously reported loss before
income tax if adjusted to reverse these deferrals for each of the first three quarters of fiscal year 2002. No restatement was needed for this in 1995 because there was a large enough allowance for returns at that point. Special charges in the income statement that write off previously capitalized costs are always a sign that a company has become
conservative in recognizing earnings and that the quality of its earnings is increasing. February 20, 2005. (Refer to Sunbeam's signals in Chapter 3, "The Sizzling Saga of Sunbeam.") Signal #2: CFFO Falls Behind Operating Income Also, CFFO lagging reported operating income or net income is a strong signal of a possible overstatement of revenue
in the income statement. The SEC maintained that Polverari carried out instructions that "included adjustments increasing revenue . Wright. 059402 01 ch3 p069-116.indd 72 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 73 In Dunlap's own autobiography, he relates that soon after assuming this new position, he began receiving
death threats. Originally, Enron had set up Whitewing and another major share trust entity, Marlin, in order to create "in the aggregate, $3.8 billion dollars in off-balance-sheet financing using support provided by Enron's preferred stock, related contractual obligations of Enron, and Enron notes." The Examiner concluded that "the Whitewing
transaction functioned more like revolving financing with the aggregate amount of advances 059402_01_ch7_p226-291.indd 262 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 263 made by Whitewing entities to Enron over a two-year period exceeding $2.7 billion." (Quotes from Bankruptcy Report #2, 2003, p. The company
also may be blending the disclosure of these SPEs with regular investments in independently established companies were going public with no records of profits—sometimes not even of sales—and a time when a simple
click on a website was enough to be counted as a customer. He saw the virtues as those dispositions or traits that were in accord with the golden mean or the middle course. Management fees of approximately $348,000 and $222,500 were charged in 1998 and 1999, respectively. (These SPEs were named for the Raptor Golf Course where the scheme
was devised, but ironically, raptor is also the name of a type of dinosaur believed to have been egg thieves and 059402 01 ch7 p226-291.indd 259 7/7/14 9:08 AM 260 Chapter 7 • Enron and the Tale of the Golden Goose predators. In order to finance Chewco as an SPE that did not have to become consolidated into 6. As a way for Buca to meet
analyst earnings estimates, Gadel orchestrated a scheme to inflate income through improper capitalization, which Skrypek helped to execute. March 12, 2011. In the succeeding quarter, the expenses and related liabilities would be re-entered in the books as original entries. Clearly, each year the allowance for loan losses was not growing nearly as
quickly as the high-risk pay-option ARM loans were growing over the same period of time. —His-Tang Chih Tsang, Chinese Zen Master In July 2010, in the wake of the mortgage crisis and financial tsunami that had hit the United States in 2008, Mary L. By December 31, 2001, WorldCom showed an asset named "Goodwill" on its balance sheet in the
amount of $50.5 billion. Question: Carlo di Florio discusses seven elements of an effective compliance and ethics program for corporations. The former franchise holder immediately transferred the amount "back to Krispy Kreme as payment of the management fee" (AAER 2941, 2009). What do we know or need to know, if possible, that will help
define the problems? Enron saw this as an opportunity and began trading weather derivatives with the utility companies. First, LJM2's $30 million investment in Talon was not at risk, as the SEC later pointed out: Fastow allegedly entered into an undisclosed side deal in which Enron agreed that, prior to conducting any hedging activity with Raptor later pointed out: Fastow allegedly entered into an undisclosed side deal in which Enron agreed that, prior to conducting any hedging activity with Raptor later pointed out: Fastow allegedly entered into an undisclosed side deal in which Enron agreed that, prior to conducting any hedging activity with Raptor later pointed out: Fastow allegedly entered into an undisclosed side deal in which Enron agreed that, prior to conducting any hedging activity with Raptor later pointed out: Fastow allegedly entered into an undisclosed side deal in which Enron agreed that, prior to conducting any hedging activity with Raptor later pointed out: Fastow allegedly entered into an undisclosed side deal in which Enron agreed that, prior to conducting any hedging activity with Raptor later pointed out: Fastow allegedly entered into an undisclosed side deal in which Enron agreed that, prior to conduct a side of the conducting and the conducting and the conducting activity with Raptor later pointed out: Fastow allegedly entered into an undisclosed side of the conducting and the conducting activity with Raptor later pointed out and the conducting activity with Raptor later pointed out and the conducting activity with Raptor later pointed out and the conducting activity with Raptor later pointed out and the conducting activity with Raptor later pointed out at the conducting activity with Raptor later pointed out and the conducting activity with Raptor later pointed out at the conducting activity with Raptor later pointed out at the conducting activity with Raptor later pointed out at the conducting activity with Raptor later pointed out at the conducting activity with Raptor later pointed out
Enron would return LJM2's investment ($30 million), Comment on the new calculation as a signal of overstatement of sales. "Andrew Fastow, Former Enron CFO, Talks Ethics With Students." Tuck School of Business at Dartmouth. There is another similar accounting trick that a company can employ to use
acquisitions to present false earnings and a false balance sheet. 17. Bank of America Corporation, successor to Countrywide Financial Corporation, Countrywide Home Loans, Inc., and Full Spectrum Lending. As a result of the overstatement of the doubtful debts reserve in the acquisition period, what is the bad debt expense in the period following
the acquisition? Management fees of approximately $111,000 in 2000, $91,000 in 2000, $91,000 in 2001 and $131,000 in 2002 were paid to such director. CALPERS was willing to do this as long as it was bought out of its share of JEDI. Presto! With a wave of a magic wand, the power was no longer from California. WORLDCOM 15. The original purpose of Fannie Mac
was to stimulate the funding and issue of government-insured mortgage loans. (Quotes from Malik, 2003, p. 059402_01_ch3_p069-116.indd 115 7/7/14 9:01 AM 116 Chapter 3 • The Sizzling Saga of Sunbeam September 30 2005 ASSETS Stockholders' Equity: Preferred stock (par value $0.01 per share, 5,000,000 shares authorized, no shares issued)
Common stock (par value $0.001 and $.01 per share, 80,000,000 and 30,000,000 (pre-split) shares authorized, 41,844,414 and 53,605,047 issued, 41,701,955 and 41,191,419 outstanding) Paid in capital Retained earnings Treasury stock, at cost (142,459 and 12,413,628 shares) Unearned compensation Accumulated other comprehensive loss Total
Stockholders' Equity Total Liabilities and Stockholders' Equity 059402_01_ch3_p069-116.indd 116 2004 — -4254534,523990,341(8,092)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,874741,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,516593,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,51659,87474,701(88,150)(12,126) - 1,504,688 $3,770,5160,87474,701(88,150)(12,126) - 1,504,688 $3,770,5160,87474,701(88,150)(12,126) - 1,504,688 $3,770,5160,87474,701(88,150)(12,126) - 1,504,688 $3,770,5160,87474,701(88,150)(12,126) - 1,504,688 $3,770,5160,87474,701(88,
• Explain the various methods that Sensormatic and Xerox used to recognize future periods' sales in current periods. The notes also disclosed a significant increase in the pay-option ARM loans with accumulated negative amortization in its loans held for investment. 17, No. 26. money.cnn.com/magazines/fortune. Positive leadership role models were
lacking. When a previously overstated reserve is reversed in a later period, this increases operating income but not net income in the later period. WorldCom also transferred the false assets out of certain accounts into other accounts into other accounts according to when Arthur Andersen planned to review the financial records. 059402 01 ch4 p117-143.indd 123
7/7/14 9:02 AM 124 Chapter 4 • Hocus Pocus income. The Foreclosure of America: The Inside Story of the Rise and Fall of Countrywide Home Loans, the Mortgage Crisis, and the Default of the American Dream. When these facts were revealed, it became clear that the SPEs' debts should have been consolidated with Enron's other debts and this
ultimately resulted in Enron being forced to restate its financial statements. He was ready to listen when he got the call from Singleton. (Buca 10-K 2002; pages F-16, F-17) 059402_01_ch8_p292-324.indd 324 7/7/14 9:10 AM Chapter 9 Mortgage Mayhem Learning Objectives After studying this chapter, you should be able to: • Explain the role of
mortgage-backed securities in the financial meltdown of 2008. A witness at the trial described how Adelphia had paid for a lavish family wedding, as well as for a personal trainer and masseur who worked full-time for John Rigas and his sons. He has worked for two leading public accounting firms and qualified as both a CPA and Chartered
Accountant. Sorkin, Andrew Ross. And so are forensic accountants (Blake, 2012). Sometimes the goods remained in the warehouses for several months before they were shipped to the customers. Brite Company's ending inventory values and its cost of goods sold (COGS) amounts for Q1-Q4 are listed below. The misallocation of expenses could also go
to other assets. Securities and Exchange Commission Complaint-in-Intervention of the United States of America vs. KPMG was also ordered to develop reform plans to ensure that SEC violations do not recur (LR 19191, 2005). Price-earnings ratios are therefore usually lower for trading companies than for operating companies. As set out in AAER
2234, April 19, 2005. January 4, 2006. One of the methods that Rite Aid used to reduce its cost of goods sold was to pass journal entries that decreased accounts payable by a corresponding amount. In its proceedings against Sensormatic, the SEC examined the roles of a number of former senior executives of the
company, including Ronald Assaf (former CEO), Michael Pardue (former COO and CFO), and Lawrence Simmons (former vice president of finance). Croteau, Brian T., Deputy Chief Accountant. Originally, the term referred to loans that did not conform to GSE underwriting standards. (Quotes from Kellenberger, 1995, pp. He was fired and replaced
with Roger Schipke, who was as laid-back and gentlemanly as Kazarian had been intense. During its first phase, the plant planned to use a fuel known as "naphta," and in the second phase, it would use liquefied natural gas (LNG), a rather expensive form of energy. The impetus for this was the "due diligence" examination that Morgan Stanley had
done in respect of the $500 million bond offering that it was underwriting for Sunbeam. (b) Nonperforming loans. 059402_01_ch8_p292-324.indd 323 7/7/14 9:10 AM 324 Chapter 8 • Tall Tales Each agreement also contains certain confidentiality, non-compete and termination payment provisions, including severance payments of 12 to 18 months
These actions had the effect of reducing Beazer's operating expenses and thereby improperly increasing its net income. Most of the income statements over a number of quarters will alert the investor to suspicious changes in the
gross margin percentage.," 2012). At the meeting, Seidl told Lay that Enron was on the brink of collapse. 293). Enron, while holding itself out as an operating or logistics company, became increasingly dependent on profits from trading, especially in its energy trading sector, whose massive profits had, for a time, concealed Enron's fundamental
problems. 19 Quoted in Business and Professional Ethics for Directors, Executives and Accountants (2009), available at Google Books. Manhattan U.S. Attorney Preet Bharara said, "Peter Madoff enabled the largest fraud in human history. (In 1989, Cendant Corporation had written off previously capitalized membership acquisition costs long before
the company's spectacular problems in 1997. It is a signal that loan loss provisions in financial statements or other indications of troubled loans. 131). either of these signals in the financial statements is a strong alert for an investor to consider a
downgrade of the stock. Each had contributed around $60 million, at the urging of two dealmakers— Paul Kazarian as CEO. The investment bankers attempted to justify the IPO shares, claiming that Ebbers had been one of their best customers. Many of the
banks were both underwriters of CDSs as well as investors in CDSs issued by other banks or insurers. 272). ENRON 17. thestreet.com. May 16, 2005. Why was Al Dunlap so enthusiastic about cutting plants and jobs so ruthlessly? Overstatement of Accruals and Reserves Scheme: According to AAER 2884, Beazer Homes also overstated its earnings by
first overstating accruals and reserves and then releasing the reserves into earnings. Mark Brickell, a J.P. Morgan employee who attended that particular weekend in Boca Raton later commented: "I've known people who worked on the Manhattan Project ... [a]nd for those of us on that trip, there was the same kind of feeling of being present at the
creation of something incredibly important." Unfortunately, the credit-default swap would eventually wreak its own kind of havoc and would later be dubbed by Newsweek as "The Monster That Ate Wall Street." (Quotes from Philips, 2008) Part of the problem was that investors could purchase these credit-default swaps whether or not they owned the
related MBSs or CDOs. This meant that an investor could effectively take a short position on mortgage bonds. Management fees of approximately $111,000 were charged in 2000. By repeating this process again and again throughout their work lives, these executives are able to craft an authentic and strong identity based on their own, rather than on
someone else's, understanding of what is right. Auditors and consultants, instead of raising red flags, can help shape the numbers to comply with generally accepted accounting principles. Likewise, although Skrypek suspected that Buca might be funding High Wire employees through payments to EDP, he simply authorized payment of EDP's bills and
approved the capitalization of those payments. Peregrine routinely kept its books open after fiscal quarters ended, and improperly recorded as revenue, for the prior quarter, software transactions that were not consummated until after quarter end. Harden, Blaine. "Lawmakers Reflect on Sarbanes-Oxley's Effect on Corporate Culture," Journal of
against Sullivan alleged that "the false adjustments and entries, among other things, improperly reduced expenses by drawing down certain reserves" (AAER 1966, 2004). 2000-2002. Fastow, however, wanted to recognize the profit in Enron's books immediately—in May. May 26, 2006. The company has sold off a number of its franchises. * Quoted in
Stephen Cohen, 2004. Over the course of the last two years, you have had many personality conflicts with her, as well as major arguments over what are the best accounting practices. As a result, the company has determined that the timing of the commencement of the V-6 diesel engine program is neither reasonably predictable nor probable.
Describe how Enron misclassified "prepays" as sales. Cohn, Michael. Under the rights-and-duties approach to the decision-making model, the decision maker needs to identify the
                                                                                                                                                                                                                                             affected by a particular decision. If the transaction is completed, the merchandise will be delivered on January 20 and paid for on January 30.
Other Misstatements The SEC also alleged that Xerox boosted its earnings by creating cookie-jar reserves and then reversing those unneeded reserves back into profits in later periods. Your manager at Ethical Auditors is an avid Kantian. Dunlap was appointed CEO of Sunbeam, Inc. (Behind the scenes, of course, many of the wholesale traders
made big profits on California's manipulated electricity prices, but this will be covered in a later section.) It was not too long before some of the problems at EES were noticed by other Enron employees. It has been reported that she once proudly told a party of people that Dunlap did not get heart attacks himself, but he gave them to others. Further
Enron often guaranteed the SPEs' debts. The suspect companies ranged from medical corporations to theatrical companies, from manufacturers of kitchen electricity to conglomerates that sold electricity. www.bloomberg.com Chapter 3 AAER 1393. Additional Miscellaneous Schemes In addition to finding that Livent understated expenses in the
previously noted matters, the SEC also found that Livent misstated revenues. Personal interview with the author. March 27, 2008. As a result, Peregrine's cash flow from operations, and understated its accounts receivable. As a result of the September 2007 acquisition of MPT, the
compliance program, although that is obviously critical. the holding company for TierOne Bank ('Bank')" (p. Defining fraud is a complex legal exercise, and from criminal cases to civil cases. 059402_01_ch5_p144-190.indd 170 7/7/14 9:04 AM Chapter 5 • WorldCom
Dunlap caught in a dilemma: They desperately wanted to leave, but they would be walking away from potentially millions of dollars of stock-option gains, as long as the price of Sunbeam shares stayed up or went higher. Allegedly, because Kaminski objected to the formation of LJM so vehemently, Skilling transferred Kaminski and his group of
analysts to other projects. Conspiracy of Fools: A True Story. In April 2003, the Commission filed a civil injunctive action against Matthew C. Born started pushing hard to get derivatives under her commission, the purchasing agreements had not yet been
legally finalized. List and describe the virtues that you think comprise a "virtuous" accounting Fraud: Analysis and Ethics takes the following eight-step case-study approach: 1. As a result of Beazer's improper recording of these
transactions as sale-leasebacks, Beazer overstated its fiscal year 2006 revenues by $117 million and net income by $14 million. The risks of ownership must have or is unlikely to have a supernormal return on assets. However, the deal still needed approval
from regulators at the FCC in the United States, and European regulators worried that the merged companies would control too much of the long-distance and Internet traffic markets. However, the SEC alleged that in the last week of some quarters, Sensormatic recognized some of its FOB destination sales at the time of shipping instead of the time
the goods reached their destination. (c) Ebber's loans, which were eating cash. Let us examine a few of these signals. As a result of the amount it had previously reported" (AAER 1393, 2001). "Accounting for Anguish," Fort Worth Weekly Online. The FSOC
is tasked with the detection of those institutions that have the power to potentially bring about another financial crisis, whereas the main task of the CFPB is to safeguard consumers. "Fastow Draws on Enron Failure in Speech on Ethics at CU," Denver Post. The very traditional Mississippi College is the oldest Baptist college in America, and the town
of Clinton is lined with tall, old oak trees interspersed with striking magnolias. These include companies such as Beazer Homes, Peregrine Systems, Buca, Inc., and TierOne Bank. In the small town of Bay Springs, Mississippi, Dunlap's decision to close the plant that made the high-quality wire for Sunbeam's electric blankets was possibly his most
economically unfeasible. This measure is calculated or presented in a number of ways. 220-221). 059402_01_ch2_p047-068.indd 67 7/7/14 8:59 AM 68 Chapter 2 • Ethics at Work Judge Swain set a sentencing date for Madoff of October 4, 2012 at 3:30 p.m.3 Mr. Bharara praised the investigative work of the Federal Bureau of Investigation. July 24
2013. Signals of Sunbeam's Fictitious Reporting Scheme #1—Improper Timing of Revenue Recognition via Bill and Hold Sales, Consignment Sales, and Other Contingency Sales Numerous signals could have alerted investors to the fictitious reporting schemes associated with improper timing of revenue recognition. Levitt thought that if companies
had to expense the value of stock options given to executive as compensation, the decrease in earnings reported in the income statement would dampen shareholders' willingness to agree to awarding stock options as an ever-increasing form of executive compensation. It was problematic for WorldCom that its internal department reported to the
CFO, Scott Sullivan, who was the major originator of the company's accounting fraud. As a result of Gadel and Skrypek's failure to ensure disclosure of this information, Buca's proxy statements for the years 2000 through 2003 understated Micatrotto's annual compensation in amounts ranging from 27% to 74%. To make it appear to investors that
Peregrine was collecting its receivables more quickly than it was, a senior officer entered into financing arrangements with banks to exchange receivables for cash. When CUC's major expense items remain identical quarter after quarter as a percentage of revenues, it is a signal that the reported expenses and revenues are being . 23)
059402 01 ch5 p144-190.indd 165 7/7/14 9:04 AM 166 Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom to WorldCom to WorldCom to WorldCom to WorldCom Wizardry: From WorldCom Wizardry: From WorldCom Wizardry: From WorldCom to Wor
                                     information. How did Enron describe the resulting rights and obligations on its balance sheet? 1). It could have been your company, your associations. Skilling expanded his Gas Bank concept by announcing that Enron would get gas producers on board by paying them up front for their contracts to deliver gas in future
periods; Enron was now financing gas production companies. The full loan amount and interest were forgiven in 2002 and recorded as a general and administrative expense. In December 1970, the TriStar took off from Palmdale, California, on its first flight. First, boards of directors authorized huge loans to company officers. This test would have
been hypothetical because Chewco definitely failed the 3 percent outside-equity test anyway. WorldCom is presented in this textbook as an illustration of overstating earnings by: (a) Holding books open after the close of a reporting period. Other virtue ethicists have suggested some different traits as conditions of being virtuous. A number of
professional organizations, as well as individuals, have submitted models that combine and/or adapt the major philosophical frameworks for the evaluation of ethical issues in the business world. Sunbeam's restructuring accrual decreased from $63.8 million in the last quarter of 1996 to $45.3 million in the first quarter of 1997, and then it was
released steadily until it reached zero at the end of the first quarter of 1998. While the system worked well at first, the power companies and traders soon began to see the potential loopholes. Skilling, however, with his unbridled enthusiasm and vision of Enron as a trading company, soon won over the younger man. The Company has reserved $67 of
this note as of December 31, 2007 and 2006. (Refer to Table 1.1, p. **Includes more than 12 acquisitions. Adelphia simultaneously transferred over $423 million of debt off its books and created false documentation for its auditors, claiming that Highland 2000 had paid cash for the securities. Using the Justice Decision-Making Approach in the
Business World In applying the justice approach to an ethical dilemma in the business arena, the decision maker should: • Identify all the stakeholders impacted by the decision, • Identify the different categories of stakeholders, and • Consider whether all persons in the same category are being treated in the same manner—that is, that all are being
treated equally and fairly. By the same token, CALPERS had contributed its 50 percent share of JEDI's equity. Once again, this grandiose plan was not backed by the necessary technology and never even approached fruition. This is done by adding back the securitized amount to accounts receivable and deducting the securitized amount from CFFO.
Skrypek told the assistant controller that he would be an independent contractor for his first three months of employment. In view of the foregoing, the Commission deems it appropriate to impose the sanction agreed to in Respondent Beazer's Offer. a June 1999 email from an Enron accountant named Kent Castleman described LJM as a "short-term
warehouse" for the Cuiába stake. Time and time again, the SEC's AAERs alleged that management orchestrated frauds to meet Wall Street analysts' earnings expectations. 17-21) Certainly, WorldCom's Internal Audit Department failed to properly carry out the function that an internal audit division should fulfill and was rebuked for this by the
                            Mac has an inconclusive sales transaction to supply Donald & Co. with merchandise costing $10,000 and a likely selling price of $15,000. This categorization of the methods of fictitious financial reporting provides a particularly useful pedagogical progression for studying the methods that companies may use to manipulate
their financial statements. Saturn Company's income statement for the current year shows $100,000 as its net income. Without clear explanations, suspicion and skepticism should be aroused. Broadbandits: Inside the $750 Billion Telecom Heist. (b) If a borrower chooses to make monthly payments that do not cover the monthly interest on the loan,
the difference between the interest that is paid is accrued and added to the loan amount as an asset on the balance sheet. Case Study PEREGRINE SYSTEMS, INC. Mark-to-market accounting cannot be used in such situations. "Ex-Rite Aid Executives Face Off in Federal Court." The Patriot-News. However, the questions
as to the validity of Sunbeam's real sales growth and its estimates were now exposed, and with inventory piled up in Sunbeam's warehouses and in its customers' warehouses, the answers to those questions would continue to impede management's efforts to maintain the Sunbeam's real sales growth and its estimates were now exposed, and with inventory piled up in Sunbeam's warehouses and in its customers' warehouses, the answers to those questions would continue to impede management's efforts to maintain the Sunbeam's real sales growth and its estimates were now exposed, and with inventory piled up in Sunbeam's warehouses, the answers to those questions would continue to impede management's efforts to maintain the Sunbeam illusion. Purchase of Inventory—The Company entered into a vendor
relationship with Parasole whereby the Company purchases bread products and a majority of the dessert products offered at the Company's Minneapolis-Saint Paul metropolitan area restaurants. Ebbers, on the other hand, disputed this, claiming that the company's Minneapolis-Saint Paul metropolitan area restaurants.
stock, which would put further downward pressure on the stock price. Capital in excess: Share premium Contributed surplus, net of deferred compensation of $59.4 in 2000 and $30.7 in 1999 Accumulated earnings Accumulated other comprehensive income (loss) TOTAL SHAREHOLDERS' EQUITY TOTAL LIABILITIES AND SHAREHOLDERS'
EQUITY 059402 01 ch5 p144-190.indd 190 4,038.2 835.0 265.7 1,650.3 60.6 11,678.9 9,461.8 1,095.3 791.6 23,027.6 343.5 — 336.9 5,233.3 2,786.3 8,427.6 249.1 17,033.2 $40,404.3 7/7/14 9:04 AM Chapter 6 Abracadabra Learning Objectives After studying this chapter, you should be able to: • Describe Livent's methods of failing to record
expenses and improperly deferring expenses. The Top-Twenty Methods of Fictitious Financial Reporting The first systematic study of the Sarbanes-Oxley Act of 2002 (or SOX Report of 2002). As consideration for the sale of these assets, the Company
received 6,000,000 shares of Empire common stock, which represents an ownership interest of approximately 32% in Empire as of December 31, 2007. Amid rapid expansion, numerous acquisitions, and ultimately, indictments
and convictions of officers of the company. *Obtained Third and Final Report of Dick Thornburgh, Bankruptcy Court Examiner. Ace should recognize a sale in respect of the inventory's selling price. Sunbeam categorically denied its "channel stuffing"—persuading customers to place a later period's orders in the current period. • Examine extracts
from TierOne's Financial Statements (10-Ks) for 2005- 2008. These entries violated GAAP because the credits were unearned as of FY 1999" (AAER 1579, 2002). Richard Boynton, Sunbeam's national sales manager, later said, "He [Dunlap] just yelled, ranted and raved." Dunlap kept this up for the entire first day. Porter, Jane, and Alina Dizik.
059402_01_ch7_p226-291.indd 279 7/7/14 9:08 AM 280 Chapter 7 • Enron and the Tale of the Golden Goose said, is to educate the next generation of business leaders, something that Tuck does with its Ethics and Social Responsibility requirement in the core program. March 28, 2013. • Sherif Abdelhak, former CEO of AHERF, pleaded no contest
to charges of raiding the company's charitable endowments in order to bolster AHERF's deteriorating healthcare system. This chapter is concerned with identifying the most communications, swapping WorldCom stock for MFS stock. Linda
Chatman Thomsen, the SEC's deputy director of the Enforcement Division, commented that the Enron executives "played important roles in perpetuating the fairy tale that Enron was capable of spinning straw—or more appropriately, fiber—into gold" (qtd. Stanaway, in turn, discussed the shortfall with Akers, who in exchange for promising to provide
future business to a particular supplier in 2004, convinced the supplier to agree to pay a $6.2 million signing bonus to the Company and to provide Navistar with a letter that would allow the company to book the full amount in 2003. • Shut down about 40 of its 61 warehouses. Sullivan reportedly admitted "that he repeatedly lied to the board about
the company's financial plight and its fraudulent accounting maneuvers" ("WorldCom's Finance Chief...," 2005). However, this board did not have the power to subpoena, nor did it have any real power to punish wrongdoers, and with the oversigh
board. Assume that you enjoy the game of 059402 01 ch2 p047-068.indd 52 7/7/14 8:59 AM Chapter 2 • Ethics at Work 53 chess. The forfeited assets, including the net proceeds from the sale of the fraud, consistent with applicable Department of Justice regulations. • Same-store
revenue (i.e., revenue of existing franchises) was growing much more slowly than parent-company revenue, which was boosted by the opening of new stores. (d) Repealed or ended the regulations that had required the separation of investment banking from commercial banking. April 24, 2013. By the early 1980s, Houston Natural Gas owned
hundreds of gas wells and had annual revenue of $3 billion. In Table 5.3, note that over the period during which WorldCom manipulated its financial statements by understating its line costs in its income statements by understating its line costs in its income statements.
on Curry's investigation, EES needed to recognize "a loss that would likely total more than $500 million" (McLean & Elkind, 2004, p. This committee had "jurisdiction over the foreign ownership restriction," and the chairman's wife worked primarily "on the repeal of the 4" The SEC issued a cease-and-desist order against BellSouth in which the
Commissioner found that "BellSouth violated the books and record provisions and internal accounting contract provisions" (AAER 1495, 2002). Back in Brazil, Cuiába's problems worsened for the next few years, but in Texas, everything was just swell. His sister said that he "would just spin on you in a second." (Quotes from Byrne, 2003, pp. As so
many before him, Kenneth Lay's route out of poverty was higher education. For loan losses to occur at the alarming rate and extent to which they did, borrowers had to become delinquent on loan repayments and house prices had to fall. This was certainly the case with Newt White, executive vice president for consumer products. • The transactions and house prices had to fall.
include significant securitizations or sales of current assets to accelerate cash collections. Sullivan understood the potential of acquisitions to provide opportunities to manipulate the profits, or earnings, that a company reports in its financial statements. The electricity fiasco in California was concocted by Enron by transmitting energy into a fictional
world of transmission schedules and congestion in power lines. The more dramatically a plan predicted a spectacularly profitable vision of the future, the more the previous applied approaches to the ethical evaluation of alternatives in a decision-making
model address the ethical problems quite clearly and offer paradigms to help identify the following: • The stakeholders • The dominant ethical issues involved (such as benefits and consequences, rights and duties, or justice and equality) • The way in which the decision making may affect the stakeholders
059402 01 ch2 p047-068.indd 58 7/7/14 8:59 AM Chapter 2 • Ethics at Work 59 To choose the right action, each system requires the consideration of the alternatives and the application of principles in an analytical attempt to make ethical decisions and to select appropriate actions. The goods would be delivered on February 28, two months after
identified and addressed needs to be revisited periodically to determine if it is still being appropriately controlled in light of new business circumstances, changing customer profiles, new regulatory obligations, etc. After making this adjustment, anyone looking at the signal of CFFO lagging reported net income should have been suspicious that Xerox
was dramatically accelerating its reported income. You be removed from all positions with the company and its subsidiaries immediately. According to the Financial crisis Inquiry Report, the lack of transparency in the balance sheets of major financial institutions was one of the causes of the financial crisis of 2008. In the case of Edison Schools,
explain why the SEC issued an AAER even though it did not find that Edison's revenue recognition practices did not contravene GAAP. The Examiner did not think so: "The evidence supports the conclusion that Mr. Ebbers would
award Salomon investment banking work" (Third and Final Report, 2004, pp. If a patent is denied, capitalized patent costs are written off in the period in which a patent application is denied. Everyday Repairs and Maintenance 28. Insignia subtracted its allowance for from its gross revenue to arrive at net revenue. "Lockheed Martin Is Only Maryland National Contract of the period in which a patent application is denied. Everyday Repairs and Maintenance 28. Insignia subtracted its allowance for from its gross revenue to arrive at net revenue."
Company on 2013 Fortune 500 List." http:// baltimore.citybizlist.com. This Global Edition preserves the cutting-edge approach and pedagogy of the original, but also features alterations, customization and adaptation from the North American version. In their paper "The Size and Growth of the Internet," Odlyzko and Coffman "proved that the whole
notion of Internet traffic was doubling every 100 days was hogwash." The actual growth rate of the Internet at that time was about 70-150 percent per year. SSB earned $100 million in investment banking fees as WorldCom's stock skyrocketed (before it plunged). With Financial Fraud And Agrees To Partial Settlement The Securities and Exchange
Commission today sued San Diego-based software company Peregrine Systems, Inc., in the United States District Court for the Southern District of California, for a massive financial fraud at the company that spanned 11 fiscal quarters. It certainly must have occurred to Fastow. Why? FINANCIAL STATEMENTS UNITED STATES SECURITIES AND
EXCHANGE COMMISSION Washington, D.C. 20549 Extracts from FORM 10-K11 Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the fiscal year ended December 31, 2008 TierOne CORPORATION Extract from Consolidated Statements of Financial Condition At December 31, 2008 2007 (Dollars in thousands,
except per share data) ASSETS Cash and due from banks $ 73,567 $ 79,561 29,292 — Federal Reserve Bank Investment securities: Held to maturity, at cost which approximates fair value Available for sale, at fair
value Mortgage-backed securities, available for sale, at fair value 11 Extracted from 10-K filings for TierOne Corporation. 059402 01 REF p365-382.indd 381 Philips, Matthew. It is vital to remember that since this test is for understatement, it must begin at the origin. He tells his coworker, Eva Numeral, CPA, that he will be back in an hour
www.jec.senate.gov. However, whereas legitimate sales will be paid only in the next period as accounts receivable instead of turning into cash. The Commission's complaint in that action by the customers and will turn into cash, the next period as accounts receivable instead of turning into cash. The Commission's complaint in that action by the customers and will turn into cash, the next period as accounts receivable instead of turning into cash.
alleges that, from 1996 through 2002, Tyco violated the federal securities laws by, among other things, utilizing various improper accounting practices and a scheme involving transactions with no economic substance to overstate its reported financial results by at least one billion dollars. On December 3, 2001, about 4,000 of Enron's employees were
given notice to leave the company on the same day. However, because the orders were so far in the future, the customers did not want to hold the goods in their inventory ahead of time; so Sunbeam agreed to hold the goods in their inventory ahead of time; so Sunbeam agreed to hold the goods that it had "sold" in the current period until the customers really needed them in the next period. ** For some years, the
amounts stated for "loans held for investment" and for "allowance for loan losses" on the face of the balance sheet changed from the amounts in the year originally stated to the amounts shown as comparatives in the following year's 10-K reports, depending on where they disclosed items such as the pool mortgage insurance receivable. This company
also known as EPE, was building the Cuiába Power Plant in Brazil, and Cuiába was meant to connect to a natural gas pipeline that Enron was constructing through tropical forests from Bolivia to Brazil. Speech. Beginning in the first quarter of fiscal year 2006, Beazer's financial performance began to decline. Also, Sunbeam's schemes—for example and cuiába was meant to connect to a natural gas pipeline that Enron was constructing through tropical forests from Bolivia to Brazil.
understating the reserve for returns and taking the benefits of rebates for future purchases into the current period—would have falsely boosted the gross margins in 1997 and in the first quarter of 1998. 059402_01_ch5_p144-190.indd 172 7/7/14 9:04 AM Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCom to WorldCom 173 When revenues decrease
reserve, and another $5.8 million overstatement of earnings came from the release of the cooperative advertising reserve. Skilling had still bigger plans, intending to transform the gas industry even further. Allowing fraudulent financial statements to be published after corrupt audits does not decrease confidence in the capital markets. In 1981, Layrence in the capital markets and the capital markets are confidence in the capital markets.
was appointed president of the Houston-based Transco Energy. FINANCIAL STATEMENTS UNITED STATES SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549 Extracts from FORM 10-K8 Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the fiscal years 2002-2003 NAVISTAR
INTERNATIONAL CORPORATION Statement of Income 2003 Navistar International Corporation and Consolidated Subsidiaries For the Years Ended October 31 Millions of dollars, except share data 2003 Navistar International Corporation and Consolidated Subsidiaries For the Years Ended October 31 Millions of dollars, except share data 2003 2002 $ 7,033 287 20 7,340 $ 6,493 271 20 6,784 Sales and revenues Sales of manufactured products Finance revenue Other income Tota
sales and revenues Costs and expenses Cost of products and services sold Cost of products and services sold Restructuring and other non-recurring charges Postretirement benefits expense Engineering and research expense Selling, general and administrative expense Interest expense Other
expense Total costs and expenses 6,229 9 6,238 (41) 297 242 487 136 26 7,385 5,817 23 5,840 521 228 260 521 154 29 7,553 (continued) 8 Extracted from 10-K filings for Navistar International Corporation 2002-2003. The second advantage of false reserves is the big payoff. Goodness "there" atones for wrong-doing "here." "They were all
there. Also, because publicly traded shares can be sold easily (if there is no sale restriction), it would have been fair to revalue Enron's shares in Mariner according to the objective market price and to recognize the corresponding profit (or loss) in the income statement. June 15, 2000. Navistar consented to the entry of this Order without admitting or
denying the findings. Signal #1: Quality of Leadership The quality of a company's leadership is an important signal with regard to whether its financial statements are likely to be fraudulently recognized that Enron had lost focus on making money and was more focused on recording profit in its income statement. Also,
outside contractors were billed for work that had not been done, and sometimes friends of employees were hired to do simple data entry work at exorbitant fees. CNBC, April 30, 2009. Lehman Brothers was not so fortunate. Enron was finally trapped and had no method or means of borrowing more money to keep hiding the situation. Baker, and Eric
R. The merchandise is part of a consignment agreement with the retailers. 059402 01 ch1 p025-046.indd 45 45 7/7/14 8:58 AM 46 Chapter 1 • Introduction to the Problem of Accounting Fraud 25. However, fixed costs, by definition, do not respond to changes in scale of operation; hence, the fixed cost becomes a greater percentage of the shrinking
sales revenue amount. Cooper, Cynthia, 157, 164-165, 166 Cooper, Stephen, 256 Core business, straying from, 276-277 Corigliano, Cosmo, 126, 129 Corporate crime, enforcement of, 37 Corporate fraud. He sold off large publishing and printing businesses as well as the company's domestic timberlands and a number of overseas paper mills. Now the
trading arm of Enron really surged, and Enron became predominantly a trading company. The views of the Commission or of my colleagues on the staff of the Commission. • In the opening months of 2006, Krispy Kreme's stocks were trading in the $5.00-$7.00 per
share range—quite a sharp drop from $49.37 per share in August 2003. "No one's going to say, 'Hey, I've got a Ponzi scheme I want you to sign on to,'" he remarked. When the California authorities called Belden to find out whether the choice of Silverpeak had been an error, he was blatant that it had been done deliberately. AIG's CDS model focused
only on estimating actual payment defaults. If you purchased this book within the United States or Canada you should be aware that it has been imported without the approval of the Publisher or Author. Expenses, or a category of expenses, that decline significantly as a percentage of sales. Which of the following statements is not consistent with
Kant's concept of the categorical imperative? If this is accompanied by Signal #1 (an increase in the accounts receivable-to-sales ratio), the alert becomes stronger. There was no need to consolidate JEDI's assets and debts into Enron's balance sheet. 27) In a precursor to what would happen at Sunbeam, big sales discounts were given to accelerate
sales, and "in the final months before the company was sold, the discounts were doubled." The stock price went up dramatically based on reported profits. The article went on to say, "By any traditional valuation, housing prices at the end of 2005 were 30% too high." It warned that "a housing crisis approaches" (Witter, 2006). To illustrate how
the prepays worked, Bryce (2002) described one prepay with JP Morgan Chase in which Enron entered into a contract to deliver $394 million of natural gas to a customer over the period 2001-2005. The NYSE and the NASDAQ have also strengthened corporate governance and filing requirements. In March 2002, John Stupka—of WorldCom's wireless
division—complained to Cooper that Sullivan was taking a reserve for doubtful debts from Stupka's division to use elsewhere. Faber, David. Browne, John. Thornburgh found failure by WorldCom's management and senior accounting staff and its internal control system, as well as failed checks and balances by the following gatekeepers: • The board of
directors, including general oversight failure as well as failures by the audit committee and the compensation and stock option committee. The investment banker's stock analyst 3 However, six years later, in September 2008, Lehman Brothers became the
largest bankruptcy in U.S. istory and Washington Mutual became the second largest. 156). washington mutual became the foundational issues and presuppositions of ethics. LR 17762. 3. (a) Receiving government-based subsidies. One of our core
functions is collecting and making publicly available financial and other relevant information from public companies." The health of our markets—and the very foundation of our financial information. August 11, 2005. In the three fiscal-year span from February 2001 to
February 2004, the number of stores grew from 58 company-owned stores and 86 franchises to 141 company-owned stores and 216 franchises. (SEC Complaint, June 4, 2009, par. To pay his enormous debts, Ebbers began borrowing large amounts from WorldCom. Students are then given the opportunity to identify signals in this company's financial
statements indicating how the company has manipulated its financial statements. in McLean & Elkind, 2004, p. In fact, it is highly likely that "Lehman Brother's Probably Won't Ever Be Charged With Anything" (Coscarelli, 2012). After acquiring a company more than three times its size, WorldCom went on, in 1998, to acquire Brooks Fiber for $2.9
billion and then CompuServe for $1.2 billion of WorldCom stock. The MCI staff had already lost a great deal of morale during the signals for Enron's schemes of using SPEs to understate debt and to overstate earnings, identify the signals of the improper use of
unconsolidated affiliates, or SPEs, that were present in the Enron case and can allegedly be found in Basin Water's notes to its financial statements. This SPE was registered in the Cayman L.P., but was subsequently referred to as LJM1. Krispy Kreme5 and the Missing
Dough6 Krispy Kreme Doughnuts, Inc., is presented mainly as an example of Inappropriate Accounting for Round-Trip Transactions, (continued) 361 059402 01 APP p361-364 indu 361 7/7/14 9:13 AM 362 Appendix The Top Twenty-Five Signals The Schemes That a Company May Be Concealing 10. (c) Which is difficult to identify in financial
statements. "Sullivan Gets Five Years for WorldCom Fraud," August 11, 2005. Eaglesham, Jean. www.vanityfair.com. Michaelson then followed up with a second question, "Are you ... nuts?" It is clear that although Michaelson then followed up with a second question, "Are you ... nuts?" It is clear that although Michaelson then followed up with a second question, "Are you ... nuts?" It is clear that although Michaelson then followed up with a second question, "Are you ... nuts?" It is clear that although Michaelson then followed up with a second question, "Are you ... nuts?" It is clear that although Michaelson then followed up with a second question, "Are you ... nuts?" It is clear that although Michaelson then followed up with a second question, "Are you ... nuts?" It is clear that although Michaelson then followed up with a second question of the pay-option loan was a foolish idea, when he wrote his book, he did not believe that Country wide
and many of the other lenders were "sinister in their intent." He seems have seen Countrywide as having been impelled by the "forces of the market place." (Quotes from Michaelson, 2009, pp. The overriding concern in the justice approach is the absence of partiality and prejudice in the treatment of all persons. Required a. March 11, 2002. That is,
the adjustments were simply entered into Polyerari's spreadsheet at Stamford—no journal entries were created, no entries were made to CUC's general ledger, and the adjustments were made to CUC's general ledger, and the adjustments were made to CUC's general ledger, and the adjustments were made to CUC's general ledger, and the adjustments were made to CUC's general ledger.
overstatement of sales and profit was its bill and hold sales to get customers to place later periods' orders long before they would pay for the goods and long before Sunbeam delivered the goods to the customers to place later periods' orders long before Sunbeam delivered the goods and long before they would pay for the goods and long before Sunbeam delivered the goods and long before Sunbeam delivered the goods to the customers. "I wanted to clean up any of the interviews I had in the past," he said. Spitzer, a former vice president of sales at Peregrine (Litigation
Release No. 18191). On the other hand, what about the rights of the family of the manager or the auditor who may be fired for resisting fraudulent financial statements? The acquired business continues operating as a separate legal entity. 66% 485.7 83.0 Corrected Pre-tax Income/ (Loss) 97.7 44.3 61.0 14.6 Total Adjustments 16.0 31.3 Depreciation
40.5 13.7 94% 74.5 70.2 21.9 N/A (14.7) 214.3 13.8 9.0 Inventory Shrink 22.1 6.6 12.6 Will-Call Payables 3.6 33.2 3.4 SARS 27.8 199.6 10.6 7.0 39.6 1.7 144.7 54% 91.8 49.3 23.8 8.0 17.5 141.1 FY 1999 1st O FY 2000 17.0 6.5 100.4 12.2 135.2 3rd O FY 1999 Dead Deals 5.9 47.1 1.0 151.3 2nd O FY 1999 Litigation Settlement 7.6 530.0 1st O FY 1999
75.6 1.5 5.9 (4.0) 113.7 FY 1998 Vendor Rebates 1.7 26.2 9.0 101.5 3rd Q FY 1998 29.7 2.6 25.3 0.0 114.3 2nd Q FY 1998 Undisclosed Markdowns Undisclosed M
areas on Rite Aid's reported pre-tax income are summarized below. Signal #3: Unconsolidated Affiliates—especially constructed entities such as partnerships—are used to generate a significant profits. When unconsolidated Affiliates—especially constructed entities such as partnerships—are used to generate a significant profits.
manipulate its financial statements. 059402 01 ch1 p025-046.indd 42 7/7/14 8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud 43 Table 1.1 The Top 20 Methods of Fictitious Financial Reporting* Fictitious Reporting* First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The Top 20 Methods of First Fraud 43 Table 1.1 The
overstatement of receivables: 1. Sunbeam also blatantly overstated its sales and deliberately failed to disclose any of the previously mentioned nine manipulations that it had used to present a misleading impression of its sales and profit growth. Ignore taxes. This was the beginning of what would become the long saga of an
angry man who cultivated and was even proud of a tough, ruthless public image that fed his apparently already ruthless streak. Fastow was exactly the sort of Enron executive that Skilling had in mind: "Fastow's motto—'never say no to a deal'—came to mean pushing for any transaction, no matter how complex or how irrational" (Swartz & Watkins,
2003, p. These men were about to embark on a wild roller-coaster ride with their new company. Each presentation allows instructors to offer an interactive presentation using colorful graphics, outlines of chapter material, and graphical explanations of difficult topics. Gadel is 47 years old and a resident of Eden Prairie, Minnesota. CIVIL ACTION
FILE NO. Obviously, this resulted in a further decline in the Enron stock price. "2011 Financial Restatements—An Eleven Year Comparison." Audit Analytics. According to the Commission's complaint, the purpose of the fraudulent scheme was to inflate the company's revenue and stock price. Countrywide's notes to its financial statements did disclose
a large increase pay-option ARM loans as a percentage of its portfolio. Nevertheless, if one had deducted securitizations from the CFFO before comparing it to operating income, the ratio would not have presented 059402 01 ch7 p226-291.indd 272 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 273 Table 7.4 Growth of
Enron's Accounts Receivable as a Percentage of Revenue: 1997-2000 1997 1998 1999 2000 Trade Receivables $ 1.37 B* $ 2.06 B $ 3.03 B $10.40 B Revenues (Excluding Other Revenues * B = billion. The Guidelines list seven factors that are minimally
required. Aggressive recognition of revenue that will be earned only in future periods. Soroosh, Jalal, and Jack T. Examining this approach in the auditor's assignment is to express an independent opinion of the financial statements of a company for users of that company for users of that company for users of that company for users of the external auditor's assignment is to express an independent opinion of the financial statements of a company for users of that company for users of that company for users of that company for users of the external auditor's assignment is to express an independent opinion of the financial statements of a company for users of that company for users of the external auditor's assignment is to express an independent opinion of the financial statements of a company for users of that company for users of that company for users of the external auditor's assignment is to express an independent opinion of the financial statements of a company for users of the external auditor's assignment is to express an independent opinion of the financial statements of a company for users of the external auditor's assignment is to express an independent opinion of the financial statements of a company for users of the external auditor's assignment is to express of the external auditor's assignment of the external
financial statements. New York: Oxford University Press. Oppel, Richard A. Gadel signed all of Buca's Forms 10-K, and the financial statements included in those reports, for the years 2002 and 2003. According to the Report, by the end of
2008, Merrill had provided for $13 billion of losses in respect of the monolines and close to another $44 billion on other mortgage-related business losses (p. 2nd edition. "Proposed SOX 404(b) Changes Could Add to Investors' Risks," AICPA Insights. However, there is little consensus among philosophers on just how far equality in distribution extends
and where merit, contribution, or effort overrides equal distribution in the allocation of material goods. It ponders perennial questions such as what makes the good good and the bad bad? This overstated reported income. TierOne also announced that it intended to restate its second quarter 2009 financial statements, and that the bank's capital ratios
would fall below the levels required by OTS. Some of those costs—the common or allocated fixed costs that support more than one segment of the business and will not decrease if any one segment of the business and will not decrease if any one segment of the business and will simply have to be carried by the remaining divisions. One must be alert enough to note the aggressive capitalization of
costs when a company writes off costs that were formerly capitalized. Stanaway and McIntosh also directed the inclusion in the warranty accrual calculation of anticipated engineering fixes that lacked historical and empirical data evidencing their likely effectiveness. Scott Livengood, the CEO of Krispy Kreme, took the company public with an initial
public offering (IPO) in April 2000 and opened a number of international franchises, with the first European outlet at the Harrods store in London. All these roadblocks did not stop Kenneth Lay from announcing in July 2000 that Enron was about to enter the entertainment business. By 1997, the CALPERS half of JEDI was valued at $383 million—an
increase of $133 million in about four years. Paying the vice president this way for the lease negotiations allowed Buca to effectively capitalize her severance payments. "SEC Charges Kenneth L. Investors should be wary of large charges in the income statement around the acquisition period because these are often signals that the company could be
creating false reserves. Thomas I. • Six former Xerox company officials agreed to pay over $22 million in penalties, without admitting or denying the SEC's allegations (SEC Press Release, 2003). On the second day, Dunlap called Clegg out of the meeting and told him to leave the company and immediately sign the release form that honored his
contract, including his salary for a year and his vested options. Besides the computer clock being stopped to backdate sales after the end of a period, documents were also provided indicating that shipments to the company's own warehouses were 059402 01 ch4 p117-143.indd 120 7/7/14 9:02 AM Chapter 4 • Hocus Pocus 121 Table 4.1
Summary of Sensormatic's Quarterly Misstatements 2 1994-1995 Amount of Improperly Recognized Revenue Net Income as Reported by Sensormatic Over/[Under] Statement of Net Income 4 0 1 $8.5 M $14.8 M [$1.9 M] [5.3%] 1994 Q2 $4.6 M $18.8 M [$1.9 M] [9.1%] 1994 Q3 $15.8 M $16.4 M $3.6 M
28.1\% 1994 Q4 $15.5 M $22.0 M [$0.9 M] [3.8%] 1995 Q1 $12.8 M $20.1 M [$0.5 M] [2.2%] 1995 Q2 $13.8 M $25.3 M $0.3 M 1.2% 1995 Q3 $30.2 M $24.1 M $6.7 M 38.3% 1995 Q4 $29.3 M $18-$21 M** $5.2 M 40.5% * M = millions. The report examined a number of factors contributing to the increase in subprime mortgage foreclosures—for
example, "adjustable rate mortgages with steep built-in rate and payment increases, prepayment penalties, limited income documentation and no escrow for taxes and insurance. A sales contract was not fully agreed upon by December 31. Issuers of financial statements that fail to disclose that accounts receivable have been sold or factored
sometimes attempt to offer the defense that this is only a disclosure issue that does not affect earnings. TierOne was a century-old thrift bank that had historically focused on residential and agricultural loans in the Nebraska/Iowa/Kansas region. In 2009, Dunlap was named the sixth worst CEO of all time ("Portfolio's Worst American CEOs of All
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Time"). This would give WorldCom an additional source of false reserves to reverse back into earnings. He appealed the sentence (Farrell, 2006). Powers Report. As head of ECT, Skilling was an Enron star on the rise. The complaint further alleges that, apart from its
acquisition activities, Tyco improperly established and used various kinds of reserves to make adjustments at the end of reporting periods to enhance and smooth its publicly reported results and to meet earnings forecasts. Finally, if she follows virtue ethics, she will use her character and virtues to guide her. 292). Ace should not recognize a sale in
respect of the inventory's selling price. Statement of Financial Accounting Standards No. 48. In December 2007, the Company sold its rights to purchase these assets to Empire. When Skilling held a conference call on March 22, 2001, in an attempt to allay investors' fears about the $5.06 drop in Enron's stock price the previous day, Grubman
questioned Skilling about the delay. The BellSouth Warning BellSou
 repurchase transaction (repo), a firm "sells" securities for cash with the understanding that the "buyer" will return the securities for a specified price (usually at a 5 percent discount) at a specified future date. So perhaps the real story of Enron starts with the story of Kenneth Lay. Then beginning in the first quarter of 1997, profits were overstated as
these inventories were sold at amounts above the amount recorded in 1996. Nevertheless, GSE loans still dominated the MBS market. Give reasons for your response. Current liabilities that decline significantly as a percentage of current assets and sales. July 2004. "Remarks at the 45th Annual Rocky Mountain Securities Conference." U.S. Securities
and Exchange Commission. With the rumors of Uzzi's departure, as well as the resignation of Richard Goudis, head of corporate planning, Shore thought he had to take the risk of downgrading Sunbeam's stock on a "conference call that linked analysts in New York with more than 5,000 stockbrokers around the world. There were only two
telecommunication companies left of such magnitude: Sprint and AT&T. Moldy Mortgage Corp. 64). "Home Prices Post Record 18% Drop: The task force is working to improve efforts across the federal executive branch and, with state and local
partners, to investigate and prosecute significant financial crimes, ensure just and effective punishment for those who perpetrate financial crimes, combat discrimination in the lending and financial crimes, and recover proceeds for victims of financial crimes, combat discrimination in the lending and financial crimes, and recover proceeds for victims of financial crimes, combat discrimination in the lending and financial crimes, and recover proceeds for victims of financial crimes and recover proceeds for victims of financial crimes and recover proceeds for victims of financial crimes are crimes and recover proceeds for victims of financial crimes are crimes and recover proceeds for victims of financial crimes are crimes and recover proceeds for victims of financial crimes are crimes and recover proceeds for victims of financial crimes are crimes are crimes and recover proceeds for victims of financial crimes are cr
 However, Bronto was not allowed to sell its shares in Saurus until March 31, 2013. [Hint 1: Remember that Signal #2 for Livent's Scheme 1 (understatement of allowance for loan losses or for losses on investments in securities backed
by loans. Caught between a genuine desire to engage in philanthropy and a strong need to assuage an insatiable ego desperate for recognition, Ebbers also pledged his WorldCom controller, pleaded guilty to one count of -
conspiracy to commit securities fraud. For example, from 2000 059402 01 ch8 p292-324 indd 317 7/7/14 9:10 AM 318 Chapter 8 • Tall Tales until late 2004, Buca had very few policies regarding billing travel and entertainment expenses ("T&E") to the company. An increase in current liabilities as a percentage of current assets or of sales is a sign
of an understatement of expenses. Extracts from FORM 10-K12 For the fiscal year ended December 31, 2006 TierOne Corporation Extract from Consolidated Statements of Financial Condition At December 31, 2006 TierOne Corporation Extract from Consolidated Statements of Financial Condition At December 31, 2006 TierOne Corporation Extract from Consolidated Statements of Financial Condition At December 31, 2006 TierOne Corporation Extract from Consolidated Statements of Financial Condition At December 31, 2006 TierOne Corporation Extract from Consolidated Statements of Financial Condition At December 31, 2006 TierOne Corporation Extract from Consolidated Statements of Financial Condition At December 31, 2006 TierOne Corporation Extract from Consolidated Statements of Financial Condition At December 31, 2006 TierOne Corporation Extract from Consolidated Statements of Financial Condition Extract from Co
 equivalents Investment securities: Held to maturity, at cost which approximates fair value Available for sale, at fair value Mortgage-backed securities, available for sale of $19,285 and $8,666 at December 31, 2006 and 2005, respectively) Allowance for loan losses Net
loans after allowance for loan losses $ 86,808 + 83,534 4,500 88,034 90 105,000 12,272 111 102,614 19,752 3,050,160 (33,129) 3,017,031 2,844,670 (30,870) 2,813,800 12 Extracted from 10-K filings for TierOne Corporation. Lockheed's accounting tale is the classic case of misstating earnings by failing to write off an impaired asset
Allegheny (AHERF) is presented mainly as an example of understating reserves for bad debts. Meeting with Gadel About Accounting Abuses 35. (a) To enter into a contrived sale of a percentage of Enron's ownership in the Cuiaba Power Plant to LJM1. Which one of the following statements does not describe the transformation in Countrywide's
reported loan portfolio? One of the notes to the financial statements in the company's 1997 Annual Report mentioned this policy. (b) As loans payable and loans receivable. • Russell Kersh, Sunbeam's former chief financial officer, agreed to a civil penalty of $200,000 without admitting or denying the allegations. Louis Borget, who ran Enron Oil, liked
it that way. 300). Again, this use of company funds for the personal benefit of the Rigas family was not disclosed to investors. In certain acquisitions made in 1996, Tyco officials convinced the companies that were being acquired to make entries to their books and records that understated the assets and overstated the liabilities that Tyco would
acquire. 90 The Great Crash 1929 The great American dream of homeownership turned into a nightmare in late 2007, when the housing bubble burst and house prices began to plunge. Typically, Xerox customer leases generate revenue from three streams: 1. Soon, home loans were pooled with other loans, such as car loans, credit card debt, and
student loans, then carved into tranches and securitized by the investment banks into what became known as collateralized debt obligations (CDOs). • There appear to have been too few independent outside directors to determine strategy and to control management. To answer these questions, we must look at how Sunbeam was performing in the
 1990s as compared with the stock market in general and the company's irrational expectations. Madoff Investment Securities LLC, Pleads Guilty to Falsifying Books and Records and Making False Statements to Investors U.S. Attorney's Office June
29, 2012 Southern District of New York Preet Bharara, the United States Attorney for the Southern District of New York; Janice K. LDDS continued to publicly report increasing profits and sales in the financial statements, which allowed it to acquire more companies with no limit to the growth of its stock price. (d) Adjustments that increase goodwill
in a later period, with respect to an earlier acquisition. However, fixed assets were amortized over periods up to 40 years. AAER 1027. In 1998, Livent was purchased by a U.S. consortium headed by Michael Ovitz, the well-known Hollywood icon. • Mary Polverari settled with the SEC without admission or denial of i llegal behavior. Ultimately,
Lockheed's accounting tale is the story of misstating earnings by failing to write off an impaired asset, which was the development cost of its TriStar L-1011 wide-body jet. Harmon Acting Secretary 059402 01 ch3 p069-116.indd 108 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 109 FINANCIAL STATEMENTS UNITED STATES
SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549 Extracts from FORM 10-K8 Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For the fiscal year ended September 30, 2007 BEAZER HOMES USA, INC. The Chief Wizard: Bernard Ebbers At 6 feet 4 inches, Bernard J. It was a colossal,
unmanageable charade, with $30 billion of debt, stalling revenues, and spiraling costs. "Ex-WorldCom Exec Out of Prison, Back in Area," Palm Beach Post. Enron also used the SPEs to overstate earnings via mark-to-market accounting and to recognize profits on the increase in value of Enron's own shares. Signals of Sensormatic's Fictitious Reporting
Schemes #1-#4 Although Sensormatic used different methods compared to those of Sunbeam, all of Sensormatic's reporting frauds accelerated and overstated sales, which ultimately had the same effect as Sunbeam's accelerated and overstated sales, which ultimately had the same effect as Sunbeam's accelerated and overstated sales, which ultimately had the same effect as Sunbeam's accelerated sales.
Fraud Illustrating Company** Fictitious Reporting Method Miscellaneous schemes: 16. It also involved spending and losing vast sums of money to get started. She is reportedly the president of an oil and gas consultancy firm (Partington, 2012). His talk was part of the Choices & Challenges series organized by the Center for Business and Society
Required a. Rolling blackouts began in June 2000, with schools, companies, and homes experiencing power cuts for two hours at a time during the day. "A Warning by Sunbeam Stuns Wall Street analysts would wait with bated breath to hear what Mozilo had to say about mortgages and the housing market. In terms of
Crafty's agreement with Tricky, Tricky will sell those 100 printers back to Crafty at the same price of $1,000 each in the form of extremely generous options beckoned to the remaining executives with the promise of great riches. If an instrument's market value increases while a financial services company
owns it, the company revalues the asset on the balance sheet (that is— marks it up to market value) and correspondingly records the increased amount as profit on its income statement, a practice known as mark-to-market accounting. With these lines, LDDS could use the Internet to transmit not only data but also voice and video. June 20, 2002. "An
Analysis and Summary of SEC Accounting and Auditing Enforcement Releases (AAERs) Issued in 2011/2012." December 5, 2012. (d) Understatement of reserves for bad debts. 48). Badaracco, Joseph L. The leading deontologist was Immanuel Kant (1724–1804). What ethical system is she predominantly using to make her decision? The CPU was the
primary basis for the warranty reserve amount; the higher the CPU, the higher the cPU, the higher the cPU, the higher the cPU, the higher the compliance and ethics program as a mitigating factor in determining criminal sentences for corporations. Another sign of Xerox's fictitious reporting scheme is that
the notes to the financial statements reflect the following: (a) Reclassification of revenue stream. www.wyomingbar.org. He also received a fine of $5,000 ("Ex-WorldCom Exec Gets a Year . . . ," 2005). In Enron's case, as discussed earlier in the sections on Whitewing, LJM, and the Raptors, Enron used its SPEs to purchase its poorly performing assets
The joint venture then "sold" the rights to another SPE called Hawaii 125-0 at a price that had wildly offtarget estimates of profits for Enron in the contracts. Broadbandits: Inside the $750 Billion Telecom Heist. He will now be jailed well into old age, and he will forfeit virtually every penny he has. Tales of CEOs Gone Wild. The company's business
model seemed like a dream come true: a product that needed no introduction and a customer base waiting to sample the merchandise. . According to a November 2007 newspaper article, "For Mr. Abdelhak, the period after the demise of AHERF has included jail time, a divorce, an aborted oil-buying venture, a personal bankruptcy filing and a recent
U.S. Tax Court order that he pay more than $500,000 in back taxes" (Fitzpatrick, 2007). When released, however, the statement did not capture the severity of the problem. Essentially, deontologists assert that one must do the right thing because it is one's duty to do so. May 4, 2007. Authorized adaptation from the United States edition, entitled
Detecting Accounting Fraud: Analysis and Ethics, 1st edition, ISBN 978-0-13-307860-2, by Cecil W. This should warn the reader that the company may be tempted to hide debt, just as Enron used SPEs to keep what was effectively its own debt off its balance sheet. The team had already come across an item of $1.4 billion in capital equipment that was
suspicious. Sensormatic Electronics Corporation was a publicly traded company, registered in Delaware, with its head office located in Boca Raton, Florida. 107): • Revenue reserves • Line-cost reserves • Depreciation • Purchase acquisition account reserves • Line-cost reserves • Line-cost reserves • Depreciation • Purchase acquisition account reserves • Line-cost reserves • Line-cost reserves • Depreciation • Purchase acquisition account reserves • Line-cost reserves
had gone wild in understating the net value of assets of the companies they were acquiring and overstating liabilities while allocating large portions of the examiner's schedule of the amounts allocated to goodwill, with respect to WorldCom's major acquisitions. The SEC
maintained that when communicating with investors and financial analysts, Adelphia misrepresented the extent to which it had upgraded its cable plant. September 2, 2002. He realizes profits of $4,558,71. I dentify and briefly describe Peregrine's main methods of overstating its revenue.
with itself in an endless hall of mirrors. Michaelson, Adam, 335, 337 Mill, John Stuart, 49-50 Mondout, Patrick, 207 Monoline insurer, 332 An insurance company that insures against only one type of risk. As it pertains to hedonism, the Victorian-era philosopher Henry Sidgwick famously pointed out that when one's objective is pleasure, pleasure
becomes elusive. Scheme #3: The Prepay Transactions Even with all the disguised financing from sales to the SPEs, Enron was still desperately short of cash. Employment Agreement—The Company entered into an employment agreement with one of its officers which requires the payment of annual compensation and certain fringe benefits through
                                                                                                                                                                                                                                                                                                                                 on sales that had not yet occurred. He was controlling on minute details, yet had no macro plan
2003 and includes bonus provisions in the form of both stock grants and stock options. www.foley.com/fcpa-anti-corruption. According to the SEC, one of the methods that Rite Aid used to understate its cost of goods sold was to recognize vendor
or focus for all the acquisitions that he was pushing through management and the board of directors at an unprecedented, frenzied pace. ("Beazer" or "Respondent"). • Deloitte & Touche LLP. The word ethics is used 20 times in Dodd-Frank, emphasizing "the reason for the Act's creation—a compelling lack of business ethics as evidenced by a
growing number of cases involving insider-trading, financial misdeeds and bad corporate governance in the financial services industry" (Peluso, 2012). The put option hedge would fail if the value of both Rhythms' and Enron's shares fell at the same time. Predictably, the co-CEO arrangement did not work and Joe Hirko left the company in July 2000
www.CNNMoney.com. TierOne ultimately disclosed over $130 million of additional loan losses. • And we have established a whistleblower program that is already providing the agency with hundreds of higher-quality tips, helping us to avoid investigatory dead-ends and—at the same time—prodding companies to enhance their internal compliance
programs. AAER 1283. It fell from a high of $64.50 per share in June 1999 to $46.07 in midJuly 2000, after the Sprint merger was called off. Explain why downsizing a company by closing segments or product lines that report an accounting loss often leads to a decrease in profits rather than an increase. The same goes for the duty of management to
 produce honest financial statements in the first place. (3) A FICO score is a measure of borrower creditworthiness determined using a statistical model. This gave WorldCom another boost, and the company grew exponentially that year. In February 1995, Alex Grass handed what he reportedly called "the keys to the kingdom" to his eldest son, Martin
 Grass, who became CEO of Rite Aid. That will not maximize profits; it will produce a profit of zero. The board names a new Chairman of the Board and we expand our ongoing search to encompass a search for your successor.... • The auditor's business partners and employees are also stakeholders, and their reputations could suffer, as could the
entire audit firm as a result of public scrutiny that could follow a failed audit. The indication that a product or program associated with the intangible asset is incurring problems or setbacks can often be found in press articles, notes to the financial statements, the segmented income statement, or the MD&A section of the annual report. (c) Always
treat persons as an end and never as a means. 7/7/14 9:01 AM 100 Chapter 3 • The Sizzling Saga of Sunbeam 29. • Changes to asset-backed securitization practices. With such an incentive, they believed they could stomach anything for a year. "MF Global: Likely Among the 10 Biggest Bankruptcies Ever." . According to the SEC, "Krispy Kreme
booked this fee as income, thereby overstating Krispy Kreme's net income in the fourth quarter by approximately $361,000" (AAER 2941, 2009). Trading ground to a halt. Indeed, we now know that the guarantees relating to special purpose unconsolidated entities actually bankrupted Enron within one year of the issue of its 2000 Annual Report.
Dunlap took his cue from the media: Nothing captured the business press's attention more than a slash-and-burn downsizing. Improper revenue recognition refers to incorrectly recording a transaction in the financial statements, indicating that the conditions have been met for the earning of revenue. For Bernie Ebbers and Brent Foster, best friends
on the team, it looked as though that championship was going to be the peak of their careers. In fact, Peter Madoff conducted no reviews. One rebate contract included an up-front payment in respect of future purchases. In addition to selling power at bargain-basement prices, Enron had to start managing and maintaining electrical power plants—and
it knew almost nothing about this aspect of the electricity industry. U.S. Bankruptcy Court Southern District of New York. http:// money.cnn.com. 1995. Questions 25-28 are about a fictitious shoe manufacturing company, Stylish Shoes, and the audit performed by the fictitious audit firm Ethical Auditors, Inc. By way of further example, Sunbeam's
fourth-quarter earnings were overstated by the release of $1.5 million of the restructuring reserves and by $9 million when the company settled an environmental litigation case for $3 million of the restructuring reserves and by $9 million when the company settled an environmental litigation reserve that it had created (AAER 1393, 2001). FINANCIAL
STATEMENTS UNITED STATES SECURITIES AND EXCHANGE COMMISSION Washington, D.C. 20549 Extracts from FORM 10-K8 Annual reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 For fiscal years 2000-2002 BUCA, INC. Overstatement of goodwill on acquisitions for the purpose of overstating acquisition
reserves in order to release the cookie-jar reserves into earnings later on. Deterring and Detecting Financial Reporting Fraud: A Platform for Action. Fannie Mae and Freddie Mac's mortgage loans enjoyed the support of explicit government guarantees for other loans on the grounds that they were
government-sponsored enterprises (GSEs). The cities in the pilot program were especially chosen because they were located in areas where Enron had found small providers to solve the problem of moving the movie material from Enron into private homes. At this stage, LDDS basically leased bandwidth and resold it for long-distance telephone calls.
 Postretirement benefits liability Dealer reserves Taxes Sales and marketing Long-term disability and workers' compensation Environmental Interest Restructuring and other non-recurring charges Other Total other liabilities Less current portion Other liabilities 2002 2001 $ 273 $ 241 26 79 282 21 206 41 48 10 34 296 34 88 257 22 211 37
48 11 36 90 246 1,562 (1,021) $ 541 155 1,230 (758) $ 472 9 Extracted from 10-K filings for Navistar International Corporation. 29). External auditors collect consulting fees from the same clients. Sudden changes (either increases or decreases) should be
accompanied by simple, logical explanations, such as, for example, a new manufacturing technique or a change in the selling price. 9. "The Wall Falls." October 28, 1999. The Report maintained that in exchange for WorldCom's investment banking business from Ebbers, SSB gave Ebbers preferential treatment in two significant ways. October 12,
                                                                                                                                                                                 information. quite so rosy a picture. Lay believed in free markets. When Company A acquires Company B, does the fact that Company A paid more for Company B than its net asset value mean that "goodwill" has
been acquired? How does one balance these rights against the rights of the employees or other users of the financial statements? Livengood was offered a six-month position as an "interim consultant" (Nowell, 2005). www.business.financialpost.com. Dunlap was the man for the job. (AHERF), 70, 204-206 Allowance for loan losses, underestimation of,
338-347 American Accounting Association Decision-Making Model, 59, 59t American Institute of Certified Public Accountants (AICPA), 32, 36, 48 American International Group (AIG), 38, 332 Analysts' expectations, 128 Animal rights, 56 Applied ethics, 48, 53-58 A branch of ethics that investigates how a normative system plays out in a practical
situation and/ or within a specific field. WorldCom appears to have violated this principle" (First Interim Report 2002, p. 059402 01 ch3 p069-116.indd 95 7/7/14 9:01 AM 96 Chapter 3 • The Sizzling Saga of Sunbeam In September 2007, Dunlap received an honorary doctorate from Florida State University, one year after his $5 million donation to
the university. Sabre Company's summarized income statements for the last three years are presented below. The creation of large reserves via one-time charges, such as restructuring charges, followed by the drawing down of reserves via one-time charges, such as restructuring charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges, followed by the drawing down of reserves via one-time charges (followed by the drawing down of reserves).
resale of any assets that it had "bought" from Enron. He was the chief witness for the prosecution in the trial of Bernard Ebbers. A normative theory makes claims or offers guidelines or norms about how to discern the right action. Special Purpose Entities #5 and #6: Whitewing, yet another illusion devised by Fastow, was
initially concocted with the apparent purpose of purchasing Enron assets. Table of contents : Cover......Page 20Acknowledgments......Page 21Chapter 1 Introduction to the Problem of Accounting Fraud......Page 26 What Is Accounting
Fraud?......Page 27 Civil Accounting Fraud......Page 32 Enron and WorldCom.....Page 32 Enron and WorldCom.....Page 35 Other SOX Regulations......Page 37 External Auditors.....Page 38 Enron and WorldCom.....Page 39 Enron and WorldCom.....Page 30 Enron and WorldCom......Page 30 Enron and WorldCom.....Page 30 Enron and WorldCom......Page 30 Enron and WorldCom.......Page 30 Enron and WorldCom.......Page 30 Enron and WorldCom.......Page 30 Enron and WorldCom........Page 30 Enron and WorldCom.......Page 30 Enron and WorldCom........Page 30 Enron and WorldCom.........Page 30 Enron and WorldCom...........Page 30 Enron and WorldCom.........Page 30 Enron and WorldCom...................
American Accounting Association Ethical Decision-Making Model......Page 60 Assignments......Page 62 Case Study: Peter Madoff, Former Chief Compliance officer and Senior Managing Director of Bernard L. • Identify the various ways in which Enron used off-balance sheet entities to understate debt and overstate earnings. These signals become
stronger still if there is simultaneously a decrease in the value of the assets (such as house prices) securing the loans. Beazer's Record Keeping and Internal Control Violations: Sections 13(b)(2)(A) and 13(b)(2)(B) of the Exchange Act 21. Price prided himself on being an exceptional stock selector. Frank, Robert, and Joann S. It is a strong indication of
a desperate overstatement of sales and sales estimates when a company issues a second press release, downwardly revision of sales estimates. Morgenson, Gretchen. The organization of Table 1.1, which follows, is based on the categories provided by the SOX Report (2002)
and provides a list of the most prevalent methods of fictitious financial reporting leading to SEC enforcement actions. An unscrupulous company can overstate this reserve and manipulate future profits by releasing the Federal Home Mortgage
Corporation, or Freddie Mac. However, according to the SEC, to avoid having the goods arrive at the customer before the requested date, Sensormatic would instruct the carrier to delay the delivery for anything from a few days to a few weeks. Right action corresponds with the act that produces the greatest amount of pleasure. Signal #1: Parent
Company Allocates Large Amounts to Goodwill When Acquiring Other Companies The prospective investor should be on the lookout for large amounts allocated to goodwill on the acquisition of other companies. "SEC Commences a Formal Probe of Krispy Kreme," Wall Street Journal. "Sure," he admitted. In fact, $1.199 billion of the $4.433 billion
was simply described as "other." The notes also stated, "From time to time, Enron has entered into various administrative service, management, construction, supply and operating agreements with its unconsolidated affiliates." • In the 1998 Annual Report, the note titled "Merchant Assets" stated, "The investments made by Enron included public and
225.indd 196 7/7/14 9:05 AM Chapter 6 • Abracadabra 197 decrease reported expenses and liabilities, remember that the expenses will not appear small, relative to sales, to the extent that they include the previous period's omitted expenses. Lay did not realize it then, but
he was peering into a crystal ball and gazing at Enron's future. Philosophers differ as to the principles of distributive justice. In another example, Buca laid off its vice president of real estate but then immediately hired her as an independent contractor. Enron's traders knew better than anyone how much gas was going to be needed, what supplies
were available, and how much was going to be supplied. The first is that there needs to be an effective process, led by a cross-functional leadership team, to identify and understand all conflicts in the business Ethics at Harvard Business School, offers the following
succinct description of those who have the ability to make prudent and ethical decisions in the business world: They are able to dig below the busy surface of their daily lives and refocus on their core values and principles. Which of the following was not a signal in Enron's financial statements of its financial problems? (A talon is a vicious claw—
 BellSouth ran afoul of the FCPA. Failure to Disclose Related-Party Transactions ADELPHIA 19. As mentioned earlier, the Bankruptcy Examiner showed how every single gatekeeping entity failed to perform its function effectively. When the demand for fiber-optic lines grew, it figured that it could save a great deal of money by simply threading
Temperance. * Obtained from U. Brooks, Nancy Rivera. The SEC issues its findings in the form of an Accounting and Auditing Enforcement Release (LR) or a Litigation Release (LR) or both. I believe that this factor, especially as it relates to incentives, goes to the heart of many problematic conflicts, since these often may involve incentives that an
individual has that are inconsistent with duties that he or she owes to the organization, its clients or his or her customers. vs. • Timothy Rigas, son of John Rigas, is now serving a 17-year prison sentence (Gilliland, 2012). • capitalized interest costs (which occur when interest is incurred on amounts invested in assets under construction). Signal #4:
Change in Accounting Policy Any reference in the financial statements' notes to a change in policy regarding the allowance for returns or any changes in estimates for returns that lead to decreasing the allowance for returns or any changes in estimates for returns that lead to decreasing the allowance for returns or any changes in estimates for returns that lead to decreasing the allowance for returns or any changes in estimates for returns or any changes in estimates for returns that lead to decreasing the allowance for returns or any changes in estimates for returns or any changes for returns or a
Issues Task Force Issue No. 99-5, Accounting for Pre-Production Costs Related to Long-Term Supply Arrangements ("EITF 99-5"). However, the Rolls-Royce engine was still in the design stage and the costs for this engine skyrocketed long before it was ready to propel an aircraft. Thus, the side-letter made clear that the supplier's rebate was
contingent on future business with the Company. Larger-than-life CEO. (c) Reversal of accounts payable amounts for "will-call" prescriptions. Clearly, there was often too much familiarity and camaraderie between a former employee of an audit firm and the external auditors, making it difficult for the external auditors to remain entirely independent
can be found in Positivism and the Separation of Law and Morals, H.L.A. Hart, 71 Harvard L. Gallu, Joshua. Did it not occur to any members of the board that the profits that Enron would record on sales to LJM1 would be absolutely meaningless? (c) With pay-option loans, the difference between the interest that accrues each month and the lower
amount that borrowers choose to pay is known and reported in financial statements as the "loan delinquency amount." (d) "Accumulated negative amount of interest that a borrower has paid. (d) The failure to record the full amount of incentive
compensation. What "virtuous" character traits are required of the whistleblowing? The whole toxic mix was simultaneously fueled by reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions in the cash reserves that banks were required to keep, as well as reductions are required to keep, as well as reductions 
inappropriately recorded sales is when CFFO lags behind operating income or when CFFO falls relative to operating income. But there were some items I wasn't truthful about that became part of this case." For example, although he admitted to investigators that he had gotten a severance package, he neglected to tell them about the secret
backdated package (which he never exercised) that the former chief legal counsel and former vice chairman handed him. With growing losses, slowing revenue, and debt spiraling out of control, Sullivan knew the true peril the company was in, and he knew that one way WorldCom could prolong its façade of profits—and prolong its existence—was to
make yet another colossal acquisition. In Enron's Annual Report, the note titled "Unconsolidated Equity Affiliates" reflected the of unconsolidated Equity Affiliates in billions of dollars, which were then removed from the companies, the merger had
a strange and difficult start. Restructuring reserves, improper use of, 84-85, 94-95 Retributive justice, 57 Returns, 82, 94 decrease in allowance for, 131 inadequate allowance for, 131 
overstatement of, 124-125, 128-129 Revenue on a gross basis, 294 The amount of revenue an entity earns before the deduction or payment of expenses for which the entity is the primary obligor. The health of our financial and capital markets and the very foundation of our financial system rely on the production and accessibility of financial
information. The U.S. Attorney's office is requesting fines of up to $848 million. www.nytimes.com. Sinnott-Armstrong, Walter. The new business ("Verizon Business"). Navistar sought to share in those suppliers' unanticipated profits by asking them to pay a portion back to the Company in the form of rebates.
Celebrates ... "July 1, 2012). The signals combine to create a siren when, simultaneously, assets (such as PPE at WorldCom) hold constant or decline as a percentage of sales. • Examine Note 9 and Note 15 to Basin Water's Consolidated Financial Statements for 2007
Ebbers continued his desperate acquisition strategy and went after Intermedia to get control of Digex, an Internet company. Thornburgh then revealed the correlation between the allotments of these shares to Ebbers and WorldCom's allocation of investment banking work to SSB. The Powers Report (2002) described these return swaps as
 "derivatives under which Talon would receive the amount of any future gains on the value of those investments, but would also have to pay Enron the amount of any future losses" (p. November 17, 2005." Ex-Cendant Chief at Retrial Denies Inflating Income; Forbes Testifies Subordinates Handled Books," The Record (Bergen County, NJ). Meanwhile
as shown in Table 9.3, the pay-option ARM loans increased dramatically: from $4.7 billion in 2005, to $26.12 billion in 2005, to $32.87 billion in 2005, to $32.87 billion in 2005, to $32.87 billion in 2005, to $26.12 billion in 2006. In three separate repurchases of franchise rights, Krispy Kreme falsely increased the repurchases of franchise rights, Krispy Kreme falsely increased the repurchase price of the franchise. Sullivan, 2002, par. In October 2002, Ford advised the company that their
seller "stuffs" more inventory into the customer currently needs. That same week an article in the Wall Street Journal remarked that the impact of Martin Grass's tenure at Rite Aid had been "disastrous" (Quote from Berner & Maremont, 1999). Those steps, however, soon escalated into a major avalanche. 259).
"Exploring Ethical Lapses During the Rite Aid Crisis," Markkula Center for Applied Ethics. Gittelsohn, John, and Ronald Campbell. "Lehman Probe Stalls; Chance of No Charges," Wall Street Journal. Relationship morality requires that we treat all human beings with human dignity. However, there needs to be an arm's-length distance between the
control of the SPE and the company. Jackson University of Southern California Boston Columbus Indianapolis New York San Francisco Upper Saddle River Amsterdam Cape Town Dubai London Madrid Milan Munich Paris Montréal Toronto Delhi Mexico City São Paulo Sydney Hong Kong Seoul Singapore Taipei Tokyo 059402_01_FM_p001-024.indd
7/7/14 8:57 AM Editor in Chief: Donna Battista Acquisitions Editor: Lacey Vitetta Editorial Project Manager: Nicole Sam Editorial Assistant: Christine Donovan Head of Learning Asset Acquisitions: Steven Jackson Project Editor, Global Editions: Suchismita Ukil Director of
Marketing: Maggie Moylan Marketing Manager: Alison Haskins Team Lead, Project Manager: Liz Napolitano Media Production Project Manager: Liz Napolitano Media Production Manager: Liz Napolitano Media Production Manager: Liz Napolitano Media Production Manager: Alison Haskins Team Lead, Project Manager: Liz Napolitano Media Production Manager: Liz Napolitano Media Production Manager: Alison Haskins Team Lead, Project Manager: Alison Haskins Team Lead, Project Manager: Alison Haskins Team Lead, Project Manager: Liz Napolitano Media Production Manager: Alison Haskins Team Lead, Project Manager: Alison Haskins Team Lead, Proj
Philosophy, so I won't try to contribute to the received wisdom of the ages on this enormous topic, 2 except to say that for my purposes today, the question really boils down to staying true [to] both the spirit and the letter of the law. The higher interest rates on subprime loans may also have been a contributing factor. This led to a high school
coaching job at nearby Hazelhurst after he graduated with a degree in physical education. When Ebbers acquired ATC, he also got Sullivan, who became vice president and assistant treasurer of LDDS. Business ethics, and the necessity, limits, and boundaries of business ethics—specifically in relation to the accounting
profession—are addressed throughout this text. Trading profits, 276-277 Tranching, 328-329, 332 A process of carving up or separating a pool of mortgages into different default losses. As a result of the conduct described above, Beazer violated Section 13(b)(2)(A) of the Exchange Act, which
requires reporting companies to make and keep books, records, and accounts, which, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the issuer. www.hindustantimes.com. The agreement also contains certain confidentiality, non-compete and termination payment provisions, including severance
payments of 12 to 24 months. This is a subset of the SEC category described as "Failure to Record Expenses or Losses via 059402_01_ch6_p191-225.indd 192 7/7/14 9:05 AM Chapter 6 • Abracadabra 193 Improper Capitalization/Deferral or Lack of Accrual" (SOX Report, 2002), which can actually be broken down into the following three
components: • Failure to Record Expenses or Losses • Improper Capitalization of Expenses or Losses • Improper Capitalization part of this category, the Livent case is presented to complete the category with an interesting and illustrative
example of the first and second components listed above. According to the SEC, BellSouth's Fictitious Financial Reporting Schemes One of BellSouth's Fictitious documents. While in jail, Mr. Forbes sold his Canaan
Connecticut mansion in the fall of 2010 for a reported $7 million (Kershaw, 2010). This conflict of how to assess the repercussions of an action is a shortcoming of which ethical theory? The lack of transparency—particularly in relation to the financial statements of prominent lending institutions—certainly fueled the fire that was in the process of
destroying the economy. (AAER 1555, 2002) (Revenue on a gross basis refers to the amount of revenue an entity earns before the deduction or payment of expenses for which the entity is the primary obligor.) 1 Edison consented to the order and to a settlement without admitting or denying any of the findings contained in the order. Interested parties
had to blindly trust Enron and Enron's external auditor, Arthur Andersen, concerning the validity of the prices used for the related-party transactions. In 1970, the Federal Home Mortgage lenders in support of homeownership and rental housing
("About Freddie Mac," 2012). 7/7/14 9:06 AM 214 Chapter 6 • Abracadabra (b) Understatement of cost of goods sold. MacIntyre pointed out that the child would be playing for the extrinsic benefit attached to the practice of playing the game as skillfully as possible. CONSOLIDATED
BALANCE SHEETS (IN THOUSANDS, EXCEPT SHARE AMOUNTS) MARCH 31, 1998 ASSETS Current assets Property and equipment, net
Intangible assets, net and other 1999 $ 14,950 7,027 $ 21,545 2,000 16,761 7,297 2,905 38,947 5,798 10,370 48,940 5,455 29,173 $ 83,568 78,660 15,895 113,158 $207,713 Extracts from FORM 10-K13 For the fiscal year ended March 31, 2001 PEREGRINE SYSTEMS, INC. 345). Instead of writing off its uncollectible amounts immediately, AHERF
                                                                                        installments. 7/7/14 9:17 AM 388 Glindex Deterring and Detecting Financial Reporting Fraud (2010), 27 Di Florio, Carlo V., 307-310, 349-350 Discounted future cash flows, 123-124 The present value of the future cash that a company expects to receive or pay. However, the
COMMISSION SECURITIES ACT OF 1933 Release No. 9132 / August 5, 2010 SECURITIES EXCHANGE ACT OF 1934 Release No. 3165 / August 5, 2010 ADMINISTRATIVE PROCEEDING File No. 3-13994 In the Matter of NAVISTAR INTERNATIONAL
CORPORATION, * Obtained from U.S. Securities and Exchange Commission. Within a few years, Enron was, predictably, immersed in legal problems. However, after several appeals and almost six years in prison, Brown was released on probation (Miller, 2011). Enron would make a percentage on the spread, much the same way a bank borrows from
2006. It could make a public offering, or it could acquire a publicly traded company, and in the process, LDDS would then become publicly listed and traded. Overstatement of acquire a publicly traded company, and in the process, LDDS would then become publicly listed and traded. Overstatement of acquire a publicly traded company, and in the process, LDDS would then become publicly listed and traded. Overstatement of acquire a public process, LDDS would then become publicly listed and traded.
Allocations to Mr. Ebbers and Investment Banking Activity for WorldCom in 1996 and 1997* • June 10, 1996. Which of the following methods of fictitious accounting was not identified by the SEC in its Enforcement Action against Rite Aid? Because Beazer sold houses within a subdivision as the development of that subdivision progressed, the land
expense recorded for any particular house sale was necessarily an estimate. The notes to the financial statements in Sunbeam's quarterly reports (Form 10-Q) should have disclosed this under Regulation S-K, items 101 and 103. Examine these extracts from Moonshine Company's income statement and balance sheet for the previous three years:
Income Statement Sales Operating Income Income Statement Balance Sheet Accounts receivable Year 1 $ 2,000 800 Year 2 $ 3,000 800 Year 3 $ 4,000 80
the opposition and the plant was closed. Tyco also incorrectly accounted for certain executive bonuses it paid in its fiscal years 2000 and 2001, thereby excluding from its operating expenses by transferring costs from a current
theatrical show to other shows to defer amortizing the assets. Available online via InfoTrac database. February 10, 2005. LR 18605. Presents a new, real-world case study of another company that perpetrated an accounting fraud or scheme similar to that discussed earlier in the chapter. Other relevant factors include "whether [the seller] has modified
its normal billing and credit terms for this buyer" and "the seller's past experiences with and pattern of bill and hold transactions" (AAER 1393, 2001). The case was settled without any admissions of wrongdoing. 059402_01_ch9_p325-360.indd 334 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 335 into high-risk subprime loans. By the time Enron
collapsed, it had a confusing jumble of over 3,000 interrelated SPEs. An examination of six of Enron's major SPE clusters reveals how Enron deviously used these SPEs. Special Purpose Entity #1: JEDI In 1993, Enron entered into an off-balance-sheet joint venture with the California Public Employees Retirement System (CALPERS). Although Lay
had moved from the public energy sector in the 1970s in anticipation of deregulation and the opportunity for the profits he was sure this would bring, he had not unfolded as neatly as he had hoped. Incentives and discipline. 059402_01_ch6_p191-225.indd 213
Chapter 6 • Abracadabra 213 (b) Understatement of expenses by removing invoices from accounting records. October 11, 2004. (c) Increased operating income. Beginning the second quarter of 1997, Sunbeam became more aggressive and desperate and began using bill and hold sales, in which the customer is billed and a sale is recorded when the
office. 101-104) Dunlap remarried in 1968 and his new wife, Judy, was always supportive of Chainsaw Al. She appeared to admire his aggression. (c) The huge loan is not given based on the grade of the employee where the higher the amount of the employee where the higher the position of the employee where the higher the amount of the employee where the higher the higher the employee where the higher the employee where the higher the 
7/7/14 9:02 AM Chapter 4 • Hocus Pocus 123 generally accepted auditing standards (GAAS) caused and willfully aided and abetted Xerox's violations." 4 (Quotes from AAER 2234, 2005) Xerox provides a dramatic illustration of fictitious reporting by improper timing of revenue recognition through the misuse of multiple-element contracts or bundled
criteria determined by the Compensation Committee of the Board of Directors). Salomon first allocates IPO shares to Mr. Ebbers—200,000 shares in the McLeod IPO. Thanks to the Leventhal School of Accounting and the Marshall School of Business at the University of Southern California and to the many undergraduate and graduate students who
have taken my classes on detecting accounting fraud over the years and have provided valuable feedback on the material presented in this text. Kenneth Lay Born in Missouri in 1942, Kenneth Lay was the son of respectable, down-to-earth arents who constantly struggled to make ends meet. The activity in the allowance for loan losses is summarized.
in the following table: Year Ended December 31 2006 Balance at beginning of year Allowance for loan losses acquired Provision for loan losses as a percentage of net loans 2005 2004 (Dollars in thousands) $30,870 $26,831 $19,586 — 4,221
6,053 6,436 4,887 (4,107) (3,063) (2,236) 313 666 373 $33,129 $30,870 $26,831 1.09% 1.01% Nonperforming Assets and Troubled Debt Restructurings. It's not right, but it comes into play." Retrospective Red Flags Did Rite Aid have ethical lapses before the crisis? However, if you leave the room, the youngster playing for candy would almost
certainly be tempted to cheat in order to win and obtain the prize. May 24, 2012. "Energy Trader Admits His Guilt," San Francisco Chronicle. Ebbers and Sullivan went after bigger and better acquisitions to create larger and larger false reserves, which would then be released into profits in future periods in order to prop up inadequate earnings.
down by OTS in June 2010. www.fwweekly.com. The phrase that Adelphia liked to use for this upgraded capacity was "two-way cable," but the SEC claimed that the extent of the two-way cable upgrade had been exaggerated. (d) The company excluded liabilities from its consolidated financial statements. (b) Failure to write off capitalization costs
such as costs of title searches. www.airliners.net/aircraft-data/stats. The task force includes representatives from a broad range of federal agencies, regulatory authorities, inspectors general, and state and local law enforcement resources. Turning his attention to
million in market capitalization," and the Jumpstart Our Business Startups Act (JOBS Act) of 2012 granted a five-year postponement to "certain emerging growth companies" after an initial public offering (Amato, 2012). In fairness, the acquisition of Sprint would have added an important wireless presence to WorldCom's long-distance and Internet
traffic capacity to complete its all-round telecommunications clout. • Changing the practices of the rating agencies whose gross mis-ratings of billions of dollars of mortgage-backed securities were kerosene on kindling. Charge for the impairment of long-lived assets Write-off of purchased in-process research and development Extraordinary items
Effect of accounting changes Depreciation Goodwill and other intangibles amortization Debt and refinancing cost amortization Interest on ITS vendor note Deferred income taxes Provisions for losses on accounts receivable and inventory Other non-cash items Changes in assets and liabilities, net of the effects of acquisitions and divestitures:
 Repayment of long-term debt, including debt tenders Proceeds from long-term debt Proceeds from sale of common shares $985.3 $1,166.2 517.1 335.0 — 45.4 - 979.6 331.6 10.4 (12.1) 334.3 211.5 (6.7) 253.7 = 2.4 - 895.1 242.6 11.3 (11.5) (8.2) 192.9 2.5 (796.0) 50.0 642.2 (124.4) (154.1) 361.1 (88.9) = (91.4) (226.2) (57.7) (96.4) (10.2) (54.1) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) (10.2) 
 (96.1)\ 3.549.8\ 66.3\ (6.5)\ 35.6\ 2.281.8\ (1.632.5)\ (234.0)\ (4.901.2)\ 926.8\ 10.5\ (13.7)\ (5.844.1)\ (1.317.5)\ - (4.251.8)\ - 6.4\ (83.1)\ (5.646.0)\ 162.3\ 1.173.7\ (2.057.8)\ 3.665.6\ - 287.1\ 2.744.5\ (1.074.6)\ 802.0\ 1.245.0\ (continued)\ 4 Extracted from 10-K filings for Tyco International LTD. If someone owned CDSs and the related bonds failed, the price of the
 CDSs would rise. www.alliemae.org. Brooks, Rick. Borget was later convicted of fraud, jailed for a year, and fined $6 million. Because the dollar size of the debit was equal to the credit, everything still balanced and expenses went down while profits went up. (b) Includes the rights-and-duties approach. Throughout this time, emboldened by the
Silverpeak experiment, many of the other power companies and their traders used numerous ploys to manipulate power prices and congestion fees. Lundstrom of TierOne Bank. Where Edison is not the primary obligor for the expenses, Edison must report revenue on a net basis to exclude such expenses. The Company purchases the products at rates
which management believes 9 Obtained from U.S. Securities and Exchange Commission. 342), and McLean and Elkind (2004, pp. They attempted by subpoenaed e-mails that seemed to confirm many rumors: Wall Street analysts often
recommended to investors shares of companies that have an investment banking relationship with their firm; yet privately, analysts deride these same companies.... While these rebates and receivables took different forms—including volume-based rebates and socalled "signing bonuses" for Navistar's award of new business—all were improperly
booked as income in their entirety upfront, even though, in whole or in part, they were earned in future periods. It also failed to disclose the "positive effect of the first quarter bill and hold sales and the failure to adequately reserve for returned product." Furthermore, Sunbeam made predictions for the year that were "contrary to internal analyses."
(Quotes from AAER 1393, 2001) Scheme #2: Improper Use of Restructuring Reserves for the write-down of assets and for future losses or liabilities in order to boost future profits. Examine the following extract from Crafty's income
statement, excluding the contrived round-trip transaction: Income Statement Extract: Crafty Co. First Quarter Sales Cost of goods sold $200,000 Tests margin 80,000 Selling and administrative expenses 30,000 Assume that Crafty Company goes ahead with the contrived round-trip transaction with Tricky Company. Congress has
responded once again, as it did after the Great Depression, with landmark legislation to raise the standards of business ethics in the banking and securities industries. Ace Company is a manufacturer of electrical appliances. The first Intermedia agreement, on September 1, 2000, was presented to the board of directors for its approval without
 "meaningful or advance data," and the directors "passively" approved the transaction. Students are provided with extracts from this new company's financial statements, as well as relevant excerpts from original documents such as Litigation Releases and Complaints. 059402 01 ch7 p226-291.indd 251 7/7/14 9:08 AM 252 Chapter 7 • Enron and
the Tale of the Golden Goose To guarantee the repayment of the $240 million Barclays Bank loan to Chewco, JEDI "paid" Enron $17.4 million as a guarantee fee. As the Bankruptcy Examiner stated, "It is inappropriate to record reserves unless a risk is probable and estimable.... Beazer Homes USA, Inc. In the final "Summary of Independent
Investigation" (2005), the special committee highlighted a number of problematic areas. In fact, in March 2006, Mozilo stated in an e-mail that the 80/20 subprime loan was "the most dangerous product in 059402 01 ch9 p325-360.indd 336 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 337 existence and there can be nothing more toxic and
therefore requires that no deviation from guidelines be permitted irrespective of the circumstances" (SEC Complaint, June 4, 2009, par. However, just after Enron began construction, India's Congress Party in Maharashtra lost power, and the new party stopped all work on the project, claiming that Enron was guilty of gross overcharging. Potential
producers could obtain bank loans more easily for the exploration and production of new gas. Further, the justice approach clearly requires us to ensure that all persons falling into the same category are treated equally. • Identify and explain the signals in the financial statements that could alert you to the
possibility that a company may be understating its expenses via improper capitalization of expenses via improper capitalization in the name of Fastow's family received $4.5 million in proceeds of this fraud. This discussion addresses the issue in broad terms and is not meant to be taken as legal advice. We did not have any accruing loans
90 days or more past due at December 31, 2008 or 2007. Or is it both illegal and unethical? Surely, the answer would have been obvious: because Enron ultimately guaranteed the repayment of the debt. • The book concludes with a useful Appendix summarizing the Top 25 Signals Indicating Possible Fictitious Reporting in Financial Statements. (c)
Failures of the credit-rating agencies providing favorable analysis of junk deals. The Financial Numbers Game: Detecting Creative Accounting Practices. • Sales would be less than in the comparative first quarter of 1997 (AAER 1393, 2001). He was acquitted of nine other insider-trading counts" (Mulligan, 2006). Wilke, John, and Robert Gavin.
Sunbeam also had a very low lease cost at McMinnville, only "pennies per foot in rent, some $29,000 a year" (Byrne, 2003, p. (b) The creation of cookie-jar reserves to release into profit in later periods. Much of the reported earnings was in the form of mark-to-market accounting, while many of the losing assets were hidden elsewhere but not actually
sold. In 2000, the Company entered into a management agreement with a member of its Board of Directors to provide for certain management and administrative services. Executive Excess 2013: Bailed Out, Booted, and Busted, The Institute for Policy Studies. Using this approach, the auditor should first consider all the people who could be affected
by the decision: • Investors could suffer losses if they trade stock at prices based on the incorrect information in fraudulent financial statements. Reisinger, Sue. "Ex-Adelphia Executive Michael Rigas Avoids Jail Time for Role in Fraud," Wall Street Journal. Despite the fact that the suppliers' payments were contingent on receiving that new business
from Navistar, the Company booked the rebates in their entirety during the then-current period in which they were received, instead of when earned over the period of the future business. In 1993, 31% of the industry's fees came from consulting. 51. online.wsj.com/ home-page. • Sales would not meet the amount predicted in Sunbeam's March
release a few weeks earlier. If there is an indication that the company failed to write off assets that were impaired previously, it may be an indication that the company is in the habit of being aggressive in overstating its earnings by failing to recognize the impairment of its assets. According to the virtue theory of ethical behavior, the most important
aspect of morality is found within the individual. Pulliam and Solomon reported that the next day Sullivan tracked down Cooper at her hair salon and warned her not to interfere with Stupka's business again. This weakness could be exploited to loot a company's assets. yourcommunityfoundation.org. Inadequate Disclosures in Management Discussion
and Analysis (MD&A) and Improper Disclosure of Non-GAAP Financial Measures EDISON ADELPHIA 18. T F 2. • Failure of corporate governance and risk management. In this case, TierOne intentionally delayed the process of obtaining current appraisals for properties that had declined in value, relying instead on inaccurate data and assumptions.
The Subprime Lending Crisis: The Economic Impact on Wealth, Property, Values and Tax Revenues, and How We Got Here. Kimberly-Clark was left with the mess. The British press generally convinced BT that it was paying too much for MCI, so BT withdrew its first offer and later offered $19 billion. The Commission thanks the U.S. Attorney's Office
for the Southern District of California and the Federal Bureau of Investigation for their cooperation in this matter. Moreover, these estimates were quite aggressive. Finnis, John. Within weeks of the beginning of Enron's meltdown in mid-October 2001, e mployees had lost over a billion dollars' worth of Enron stock in their 401(k) plans, stockholders
had lost billions of dollars as the stock price fell from $60 per share to below $1, and debt holders were about to lose more than $3.9 billion that Enron owed them. (c) The recording of early shipments of equipment sales to franchisees. Explain how Navistar's improper treatment of its rebates was similar to Rite Aid's improper accounting for its
rebates, as described in this chapter. securities.stanford.edu/1009/INSGY97/006.html. 105) When a company acquires another company, the parent company can use a number of time periods to manipulate profits. T F F 7/7/14 8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud Fill-in-the-Blank Questions Multiple-Choice
Questions Fill in the blanks with information and concepts from this chapter. "Enron Defense Argues Houston Too Hot to Be Fair: Lawyers Cite Anger Shown in Jury Pool Questionnaires," Chicago SunTimes. November 15, 2010. Cohen (2004) describes this approach as follows: A virtue ethics view may see the process more "inside out." Moral
behavior should be the result of, and flow from, a person's character. At the end of 1994, on the quest for more acquisitions, Inc., a global satellite business that included IDB WorldCom—a company with a large international division. Mr. Gottlieb, who was also convicted and was sentenced to four years in jail, had
already been released" (Shecter, 2013). In January 1999, Drabinsky and Gottlieb were indicted in the United States on 16 counts of fraud and conspiracy, but they refused to face these charges and remained in Canada. "It's going to be much more insidious." "Mark-to-market accounting is like crack," Fastow replied. However, until 2001, goodwill had
to be amortized over only 40 years, resulting in much smaller amortization expenses during each period in the company's income statement, and therefore higher reported earnings. Celebrates ...," July 1, 2012). Fill-in-the-Blank Questions Fill in the blanks with information and concepts from this chapter. "I used loopholes in the rules to get around
the principles of the rules," he explained. (a) Increased net income. Arthur Levitt (2002) reported: "In April 2002, the Justice Department, Securities and Exchange Commission, and state regulators opened investigations of possible wrongdoing by research analysts at major Wall Street firms" (p. Although Kazarian cut the extravagant waste of the
Buckley era and stopped the wild downsizing of his predecessor's turnaround attempt, he appeared to be a workaholic and was too intense for some. (c) Loans with negative amortization. The Fraud Trial. Retained earnings Total current liabilities 1,230,310 327,093 Inventories Total assets 228,749 35,794 Q2 Receivables, net Cash and cash
equivalents Balance Sheet Accounts 67,781 185,669 253,450 Q1 1997 Extracts from Quarterly Balance Sheets (in Thousands) PRIOR TO RESTATEMENT Table 3.2 Extracts from Quarterly Income Statement (in Thousands) Table
3.1 Extracts from Sunbeam's Income Statements 3646,626 523,065 43,151 Q2 (52,477) 630,965 578,488 Q2 (310,233) 443,719 1,861,243 3,443,422 3,519,121 1,438,638 1,278,465 575,109 562,294 193,543 Q1 1998 Chapter 3 • The Sizzling Saga of Sunbeam 93 Table 3.3 Increase in Receivables as a
13% -9% cash received at the rate they should have been if they were legitimate sales, and the gross margin percentages were fluctuating wildly, without a clear explanation for the volatility. Gadel also was one of the two authorized signatories on High Wire's checking account and served as one of High Wire's Buca contacts. "Mortgage
Delinquencies Fall, But Foreclosures Show Gains," Wall Street Journal. If that information is wrong, it is very likely that suboptimal operating decisions will be made with damaging consequences for the company, such as lower profits and bonuses, or even bankruptcy of the company, causing employees to lose their jobs.
www.thedailybeast.com/newsweek. Super-senior tranches, 332 T Talon LLC, 260 Tate, John, 303 Telefonia, 301-302 Telos, 52, 53 Thomsen, Linda Chatman, 30, 244 Thornburgh, Richard, 30, 33, 147, 158, 160, 164, 166-167 TierOne Bank, 354-360 Times-interest-earned ratio, 274-275, 275t A ratio used as a measure of an entity's ability
to meet its internal obligations from the income that it generates. Why is an "increase in accounts receivable as a percentage of sales" a signal of improper revenue recognition? That month the stock price fell below $10 per share. This piece of information sheds some light on why the entity was created in the first place and why it was shrouded in
vagueness in the financial reports. Not surprisingly, problems and roadblocks usually did emerge. • Explain why downsizing by closing segments that report an accounting loss often leads to a decrease in profits, rather than an increase. For example, Buca, through Gadel and Skrypek, capitalized payments totaling approximately $572,000 made to an
independent contractor who provided permitting services for Buca restaurants, despite having no basis to do so. April 17, 2013. Bray, Chad. Unemployment was only 5.5 percent, but oil prices were surging towards a new high of $147 a barrel and the Dow was plunging, down 20 percent year-over-year and headed much lower. U.S. Securities and
Exchange Commission Accounting and Auditing Enforcement Release. Obviously, if that situation continued too long, the utilities would go bankrupt. • We conclude collapsing mortgage-lending standards and the mortgage securitization pipeline lit and spread the flame of contagion and crisis. According to the SEC's AAER, which of the following was
a method used by CUC to overstate its earnings? Skrypek, as the Controller, created the first working draft of Buca's Commission filings, including consulting with his staff on the accounting numbers contained in those filings, including consulting with his staff on the accounting numbers contained in those filings, including consulting with his staff on the accounting numbers contained in those filings.
the Market: Adelphia Ex-Officer Admits to Filing False Report," Wall Street Journal. In the case of AHERF, the misstated reports went beyond annual financial statements and included municipal securities disclosure reports known as Nationally Recognized Municipal
                                                                                                                                                                                                                                                                                                                                                               Information Repositories. Gadel and Skrypek approved capitalization of
these salary payments despite having no documentation supporting such accounting treatment. This division began huge power projects overseas, including the massive Teesside project in England. Examples of situations for which reserves could be set up include the following: • The parent or acquiring company anticipates that the realizable value
of the acquired company's assets is less than the assets' value as stated on the balance sheet—in other words, the asset will have to be sold at a loss in the future. When HNG came looking for a new CEO in 1984, Lay jumped at the opportunity to become CEO and chairman of this old and highly respected Houston gas production company. Selected
Financial Statements 2006-2007. 7/7/14 9:17 AM 386 Glindex Chanos, Jim, 277 Chartered Institute of Management Accountants, 48 Chewco, 250-252, 253 Chicago Flexible Shaft Company, 70 Chief executive officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs), responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 responsibilities of, 36 Chief financial officers (CEOs) loans to, 36 Chief financial officers (CEOs) loans to, 36 Chief financial officers (CEOs) loans to, 36 Chief financial 
accounting fraud, 27-28 Clegg, James, 77 Clinton, Bill, 331 CLUES underwriting system, 338 Coffman, Kerry, 151 COGS. Hoboken, NJ: John Wiley & Sons. Note that the list of those affected is virtually identical to the list in the utilitarian model, but the emphasis here is not so much on the negative impact of the decision, but rather on upholding the
rights of the people involved. Burns, Greg. The next day, Sunbeam 89 a directors' meeting to consider the accusations against the company. Deferred costs or prepaid expenses that increase significantly as a percentage of total assets, or as a
percentage of sales. 25). June 1, 2005 "Kreamed! The Rise and Fall of Krispy Kreme Is a Cautionary Tale of Ambition, Greed, and Inexperience," CFO Magazine. More ominously, analyst Andrew Shore was reconsidering his earlier upgrade of Sunbeam's stock. Extracts from Zee's quarterly income statements and balance sheets for the four quarters of
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year 1 are as follows: Q1 Q2 Q3 Q4 \$ \$ \$ Millions Million

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than it could fulfill the next quarter. (The LJM structure of unconsolidated entities was not even listed in the unconsolidated affiliates' note, although it was mentioned under "Related-Party Transactions.") 059402 01 ch7 p226-291.indd 267 7/7/14 9:08 AM 268 Chapter 7 • Enron and the Tale of the Golden Goose • In 2000, the "Unconsolidated
Affiliates" note provided an incomplete list of entities, and although some significant SPEs were omitted, the note did mention the sale of Enron's merchant assets to Whitewing. (b) This would cause CFFO to be $6,000 smaller than operating income. The longer the contract extends into the future, the less likely it is to estimate prices accurately. F 1
Assignments in this chapter were developed in collaboration with Kate Jackson, Ph.D. student in Theological Ethics, Boston College. • Alternative accounting treatments that were discussed with management, as well as their possible effects. Although no list of duties has ever been specified as prescriptive, some of the more common duties that Kant
and his followers have suggested include the duty to develop one's talents, the duty to avoid dishonest promises, and the duty to respect the freedom of others. Nevertheless, Navistar approved the rebate and booked the entire dollar amount in fiscal year 2004. 059402 01 ch4 p117-143.indd 141 7/7/14 9:02 AM 142 Chapter 4 • Hocus Pocus YEAR
ENDED MARCH 31, 2001 Sales and marketing Research and development General and administrative Acquisition costs and other Total costs and expense Income tax expense Income tax expense Income tax expense Net loss per share
basic and diluted: Net loss per share Shares used in computation 2000 1999 223,966 61,957 48,420 918,156 1,378,090 101,443 28,517 19,871 57,920 261,956 50,803 13,919 10,482 43,967 151,802 (813,407) (538) (8,656) 38 (13,739) 664 (813,945) 38,296 $ (852,241) (8,618) 16,452 $ (25,070) (13,075) 10,295 $ (23,370) $ $ (0.24) 102,332 $ (6.16)
138,447 (0.27) 87,166 Peregrine Systems, Inc. The problem was that the banks and insurance companies did not have anywhere near enough cash to make good on the CDSs and insurance policies if house prices dropped and borrowers defaulted. March 28, 2005. June 5, 2003. The Examiner showed that the Prepays, if properly reported in 2000,
would have increased Enron's debt from $10.2 billion. In the journal entries to record the sale of a house after the close of the sale of that house to a third party. • EES faced huge losses if
the California energy crisis forced Enron's customers into bankruptcy, as had occurred, for example, in the life cycle of the deferment as described in the accounting policy notes. Why did virtually no one take heed of demoralized and scared employees
looking for safer jobs, while key executives resigned in droves? Bowling, Brian. Second, the board sometimes conveniently authorized "forgiveness" of the loans. Madoff is also subject to mandatory restitution and criminal forfeiture and faces criminal fines up to twice the gross gain or loss derived from the offense. A derivative financial instrument, or
of Al Dunlap......Page 73 How Wall Street Embraced Sunbeam's Downsizing Plans......Page 75 "Downsizing or Dumbsizing?"......Page 76 Dunlap's Carrot-and-Stick Approach......Page 77 Scheme #1: Improper Timing of Revenue Recognition via Bill and Hold Sales, Consignment Sales, and other Contingent Sales......Page 81 Scheme #2: Improper Use of
Restructuring Reserves......Page 85 The Sunbeam's Fictitious Reporting Scheme #1—Improper Timing of Revenue Recognition via Bill and Hold Sales, Consignment Sales, and Other Contingency Sales......Page 91 Signals of Sunbeam's Fictitious Reporting Scheme #2—Overstating Earnings via Improper Use of
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120 Scheme #5: Misleading the Auditors......Page 121 Signals of Sensormatic's Fictitious Reporting Schemes #1-#4......Page 123 Scheme #2: Estimates of Discount Rates and Residual Values......Page 124 Signals of Xerox's Fictitious Reporting Schemes......Page 125 Are
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Reserves......Page 160 Scheme #2: Improper Capitalization of Expenses ......Page 162 Ebbers Loses Control......Page 163 The End of the Sullivan Era......Page 165 The Gatekeepers Who Failed WorldCom's Fictitious Reporting Scheme #1—Improper Use of Acquisition or Merger Reserves......Page 170 Signals of WorldCom's Fiction of Expenses and Expenses of Control of Expenses and Expenses and Expenses of Control of Expenses and Expenses an
WorldCom's Fictitious Reporting Scheme #2—Understating Expenses via Improper Capitalization of Expenses via Improper Capitalization via Improper C
Understating Expenses via Deferral of the Expenses via Deferral of the Expenses Values to Reduce Cost of Goods Sold......Page 198 Are They Living Happily Ever After?......Page 200 Scheme #1: Overstating Ending Inventory Values to Reduce Cost of Goods Sold......Page 201 Signals of the Fictitious Reporting Schemes
of Reducing Cost of Goods Sold......Page 202 Are They Living Happily Ever After?.....Page 204 Allegheny (AHERF): Trick or Treatment?.....Page 205 Signals of the Fictitious Financial Reporting Scheme of Failing to Account for Asset
Impairments......Page 208 Signals of the Failure to Record Asset Impairments......Page 210 Assignments......Page 213 Case Study: Navistar International Corporation......Page 228 Jeffrey Skilling......Page 228 Lay, Skilling, and
Scheme #2: The Abuse of SPEs......Page 249 Scheme #3: The Prepay Transactions......Page 266 General Signals of Enron's Fictitious Reporting Scheme #3: The Prepay Transactions......Page 273 Are They Living Happily Ever
After?......Page 278 Key Terms......Page 281 Case Study: Basin Water, Inc......Page 281 Case Study: Basin Water, Inc......Page 282 Edison's Fictitious Financial Reporting Scheme #1: Improper Use and Misleading Disclosure
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Dough......Page 303 Signals of Krispy Kreme's Operational Problem of Opening Too Many Franchises......Page 305 The Krispy Kreme Scheme of Using Inappropriate Accounting for Round-Trip Transactions......Page 307 Ethics at Work......Page 308 Assignments......Page 312 Case Study: BUCA, Inc.......Page 315 Chapter 9
Mortgage Mayhem......Page 326 The Housing Bubble......Page 327 Easy Credit: Securitization......Page 327 Easy Banking: Regulations Repealed......Page 328 Easy Profit: Tranching......Page 327 Easy Banking: Regulations Repealed......Page 328 Easy Investing: Credit Default Swaps......Page 327 Easy Banking: Regulations Repealed......Page 328 Easy Investing: Credit Default Swaps......Page 328 Easy Investing: Credit Default Swaps......Page 329 Easy Banking: Regulations Repealed......Page 328 Easy Investing: Credit Default Swaps......Page 329 Easy Investing: Credit Default Swaps.......Page 329 Easy Investing: Credit Default Swaps.......Page 329 Easy Investing: Credit Default Swaps.......Page 329 Easy Investing: Credit Default Swaps...........Page 329 Easy Investing: Credit Default Swaps...........Page 329 Easy Investing: Credit Default Swaps............Page 329 Easy Investing: Credit Default Swaps...................
ARM Loans......Page 338 Countrywide's Underestimation of Allowance for Loan Losses......Page 349 Ethics at Work......Page 350 Assignments......Page 350 Assignments......Page 351 Case Study: TierOne Bank......Page 355Appendix......Page
and universities throughout the world. According to the SEC, BellSouth's improper accounting for foreign payments in contravention of the Foreign Corrupt Practices Act (FCPA) included all of the following, except: (a) The use of fabricated invoices at Telcel. Micatrotto and a Buca vendor bought an Italian villa in 2001 and billed Buca for the
purchase and for certain improvements to the villa. (b) Over-the-counter derivatives, which auditors themselves do not understand. The buyer must have a substantial business purpose for ordering the goods on a bill and hold basis. Lay was 42 years old, and he had arrived. 12. U.S. Securities and Exchange Commission Litigation Release. The famous
whistleblower and internal auditor Cynthia Cooper reported in June 2001 that such switches of existing accounts purporting to be new ones had led to commissions being overpaid by close to $1,000,000. • The New York Stock Exchange (NYSE) and the National Association of Securities Dealers Automated Quotations (NASDAQ) added new
requirements for their member companies. (Quotes from BR-6413, 2002) Signal #2: Mixing a Company's Assets or Liabilities with Those of Other Parties The intermingling of a company's Assets or Liabilities with Those of Other Parties.
envied the GSEs' advantage in this lucrative sector and lobbied for what they called "a level playing field." The result of this was the Secondary Mortgage Market Enhancement Act of 1984, which allowed institutional investors, such as pension funds and insurance companies, to invest in non-GSE guaranteed mortgage-backed securities. Other
schemes included incorrect payments and inaccurate records. Michaelson received the following reply: "Well, forecasting has run the numbers and ... we believe that housing values will continue to rise for the foreseeable future, especially in major metros such as Los Angeles, New York, and others" (p. Enron Capital and Trade (ECT) Jeffrey Skilling's
bright idea to develop a futures market in natural gas in 1990 was the beginning of Enron's venture into the trading business. From this financing, CALPERS was paid $383 million for its 50 percent share of JEDI. February 19, 2013. This was yet another of the "variety of improper revenue recognition practices" that the Commission alleged
Sensormatic used in its attempt to meet analysts' quarterly revenue and earnings expectations. In addition, disclosure is also required in the MD&A section regarding certain details of off-balance-sheet arrangements. Tranches that absorb the initial or most likely default losses are known as junior tranches and usually earn a higher rate of return
because of their higher risk. Possible overstatement of inventory, or understatement of obsolescence of inventory, or understatement of sold. Do you think that to be virtuous in business, it is also necessary to be virtuous in other areas of your life, such as 059402_01_ch2_p047-068.indd 63 Chapter 2 • Ethics at Work 63 in your
marriage or in your friendships? All the mechanisms discussed earlier regarding Enron's use of mark-to-market accounting, in conjunction with its false sales via SPEs, led to a gap not only between reported earnings and generated cash but also to a lack of a strategic business focus on projects that generated real profits and real cash. These alleged
methods described by the SEC are similar to some of Sunbeam's methods of overstating sales. On January 1, 2007, the repayment reset to $7,500 per month, and the borrower immediately informed the lender that no future payments would be made on the loan. 5 The Big Five became the Big Four after the collapse of Arthur Andersen in 2002. 732-
734) 2 Schapiro's "Testimony" cites the Bankruptcy Examiner's Report, pp. To Aristotle, the ultimate objective of the golden mean was the good or well-being of both the individual and the society, and he offered a non-exhaustive list of virtues or character traits that included honesty, courage, temperance, friendship, and the intellectual virtues.
Signal #3: Parent Company Creates Significant Reserves to boost later periods' earnings. • Rebecca Mark left Enron before its collapse and was not prosecuted.
Sales were lower in the third quarter of each year due to seasonal variables, and this quarter generally provided the biggest challenge. Conversely, do the relatives of the manager or auditor have the right to expect not to be embarrassed by family members who are criminally charged for 059402_01_ch2_p047-068.indd 56 7/7/14 8:59 AM Chapter 2
• Ethics at Work 57 resenting fraudulent financial statements? The difference of approximately $1,500 represents the excess of the market value of the Company's investment in Empire over the Company's 32% interest in the net assets of Empire.
by Jarden Corporation in January 2005 ("Jarden," 2005). 15). October 15, 2010. Natural gas as a significant energy source would only make sense if one could get the wild instability out of the prices. Employment Agreements—We entered into an employee agreement with our Chief Executive Officer on July 22, 1996, which was subsequently amended
and restated in February 1999, and further amended in September 2002, and March 2003. Hints were left in references in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements regarding unconsolidated affiliates and also in the notes to the financial statements are not also in the notes to the financial statements are not also in the notes to the financial statements are not also in the notes to the financial statements are not also in the notes to the financial statements are not also in the notes to the financial statements are not also in the notes to the notes to the financial statements are not also in the notes to the financial statements are not also in the notes to 
retained by the seller. www.huffingtonpost.com. Thornburgh, the WorldCom Bankruptcy Examiner would eventually explain, "WorldCom grew in large part because it was very general and did not answer the specific questions raised. Kopper and Dodson,
who had originally come up with the paltry $125,000 portion of the $383 million financing for Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received strangely favorable treatment by Fastow during Enron's final repurchase of Chewco, also received at the Chewco final repurchase of Chewco final re
dogged with financial problems almost from its outset. Madoff and his wife and executed sham promissory notes to make it appear that the transfers were loans, in order to avoid paying taxes, executed sham promissory notes to make it appear that the
transfers of these funds were loans; • Madoff did not pay taxes on approximately $7,750,000 that he received approximately $16,800,000 from Bernard L. Madhusudanan, Sindhu. Enron was selling its own assets to this affiliated entity. On December 10, 2008, one day prior to BLMIS's collapse, Madoff also withdrew
$200,000 from BLMIS for his personal use. III. February 8, 2011. Chimicles & Tikellis LLP. A write-off of previously capitalized costs shows that the company has been wrong in the past about the ability of a current cost to hold value in future periods. Jack Grubman, of Salomon Brothers, did his part in spreading the WorldCom myth. While WorldCom
reported skyrocketing earnings, behind the scenes, company management was raiding the cookie-jar reserves created on acquisitions in order to meet earnings' expectations. Those fees enabled the traders to earn more money by intentionally sending electricity on congested routes. www.nyse.com. Case 0:06-cv-02320-ADM-AJB, Document 1-1.
www.osha.gov. Between approximately 2000 and 2007, Beazer created, and later reversed, improper accruals and reserves by, among other ways, manipulating the amounts recorded in two series of accounts in order to manage earnings. *** M = million. 059402 01 ch2 p047-068.indd 64 iii. (b) The fall of stock price. (d) Both (a) and (b). Perhaps
the plan was so stunning that it gave cause for concern that Sunbeam was in worse shape than anyone had realized. "Scott Sullivan-WorldCom, Inc.," CFO Magazine. Thomas Jr., Landon. In the mortgage industry, more and more nonconforming loans were purchased, pooled, and segmented into tranches of different grades of risk and then sold to
                                securities. "Amid Big Losses, Sunbeam Plans to Cut 6,400 Jobs and 8 Plants," New York Times. Skilling decided that Enron would join the broadband investment boom by expanding FirstPoint's investment in broadband capacity. To support this program, the company developed a V-6 diesel engine, constructed an engine
assembly plant in Huntsville, Alabama, entered into non-cancelable lease agreements for V-6 diesel engine assembly assets and incurred certain pre-production costs. Scheme #1: The Abuse of Mark-to-Market accounting in 1991, Enron searched for every
possible loophole to exploit this opportunity to overstate its earnings. He realizes profits of $1,957,475. WorldCom later announced a write-off of approximately $50 billion of goodwill in its bankruptcy filing in 2002. Let us now examine these three theories more closely and then discuss how they apply to business ethics. Taking the viewpoint that no
book on accounting fraud would be complete without an examination of the breakdown in ethics that underlies the fraud, this text examines the three major Theories of Ethics, as well as ethical decision-making models that are applicable to the business world in general and to students of accounting in particular. The self-policing practices of the
auditing profession came under scrutiny. Arthur Anderson, 37, 89, 161-162, 164, 166, 233, 256, 270 Assaf, Ronald, 118, 122 Assets accounts receivable as percentage of, 206 depreciation of, 197 failing to record impairments of, 206-209 impaired, 207 intangible, 208, 290 059402 01 GLINDEX p383-401.indd 384 intermingling of, 299 nonperforming
358-359, 360 partial ownership in sold, 271 securitization of, 270-271 Asset-turnover ratio, 170-171, 198, 208 Association of Certified Fraud Examiners, 26 Audit committees, 37 Audit firms, 55 Auditors, 31-32, 34 decision-making models and, 54-55 external, 37 misleading of, 120-121 Azurix water project, 238-239 B Badaracco, Joseph L., Jr., 60 Bad
debts, understatement of, 204-206 Balance sheets, lack of transparency in, 39 Banking sector, deregulation, 38, 329-330 Bank of America, 332 Banks, 54 Basin Water, Inc., 284-291 Bass, Carl, 37 Bear Stearns, 332 Beazer Homes USA, Inc., 101-116 Belden, Timothy, 245, 247, 277 BellSouth, 300-302 Bentham, Jeremy, 49 Bill and hold sales, 81, 93 Advanced Basin Water, Inc., 284-291 Bass, Carl, 37 Bear Stearns, 332 Beazer Homes USA, Inc., 101-116 Belden, Timothy, 245, 247, 277 BellSouth, 300-302 Bentham, Jeremy, 49 Bill and hold sales, 81, 93 Advanced Basin Water, Inc., 284-291 Bass, Carl, 37 Bear Stearns, 332 Beazer Homes USA, Inc., 101-116 Belden, Timothy, 245, 247, 277 BellSouth, 300-302 Bentham, Jeremy, 49 Bill and hold sales, 81, 93 Advanced Basin Water, Inc., 284-291 Bass, Carl, 37 Beazer Homes USA, Inc., 284-291 Bass, Carl, 37 Beazer Homes USA, Inc., 284-291 Bass, Carl, 38 Beazer Homes USA, Inc., 38 Beazer Homes USA,
sale in which the customer is billed and a sale is recorded when the groads are held for delivery until a later period. In 1999, the Glass-Steagall Act was repealed and the Financial Services Modernization Act was passed to deregulate the sector in the United States. The 1968 Charter Act facilitated the granting of mortgage loans
by: (a) Establishing the Federal National Mortgage Association to buy up mortgages that were guaranteed by the Federal Housing Administration (Fannie Mae). December 20, 2006. SACV09-01426. Since 1977, the Public Oversight Board (POB) had been responsible for monitoring audit independence and quality. "Settlement Reveals Another Enron
Strategy," Los Angeles Times. Signals of Countrywide's Underestimation of Allowance for Loan Losses Here is an examination of some of the signals indicating that a company may have understated its allowance for Loan Losses. These are the types of violations that we examine in this text. From 2001 until 2005, he was also a vice president of Buca. If
you offer the youngster candy as an incentive to learn the game, he or she may then agree to be taught. Gadel explained to the construction manager that this arrangement could call him directly. Mac has the goods on hand on
December 31. LDDS acquired WilTel in 1995 for $2.5 billion cash, gaining a cable network with over 11,000 miles of fiber-optic cable. Improper capitalization of expenses to overstate earnings. Also important is the access to goods such as clean water and services such as health care and education. In addition, they recorded fictitious ticket sales
Explain why an action can be taken against an issuer of financial statements in terms of the Foreign Corrupt Practices Act in respect a. They went on from the MFS/UUNet acquisition to acquire BLT Technologies, which supplied prepaid phone cards. In fact, it soon became obvious that Azurix had made a mistake. As the mortgage industry evolved
from making loans that conformed to GSE standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans, what were some of the changes in underwriting standards to making and selling subprime loans.
trading restrictions, credit ratings, regulation of financial products, corporate governance and disclosure, and transparency" ("The Laws ...," 2012). Farrell, Greg. Pasha, Shaheen. "New York Judge Grants Ebbers Bail." September 7, 2005. Northridge, California. Thanksgiving dinner that year was lunch meat with bread" (Gruley & Smith, 2002). The september 7, 2005. Northridge, California. Thanksgiving dinner that year was lunch meat with bread" (Gruley & Smith, 2002). The september 7, 2005. Northridge, California. Thanksgiving dinner that year was lunch meat with bread" (Gruley & Smith, 2002). The september 7, 2005. Northridge, California. Thanksgiving dinner that year was lunch meat with bread" (Gruley & Smith, 2002). The september 8 is a september 9 is a septem
059402_01_ch7_p226-291.indd 280 F 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose E nron's consolidated financial statements, it had to have a minimum of 3 percent of its equity contributed independently of Enron. 18. Limited ENE shares (1.6 MM) Partner $3.75 MM Cash General Partner LJM Swap Sub, L.P. Put option on
5.4 MM shares Rhythms stock Exhibit 7.3 A Diagram of the Rhythms Transaction From Powers Report, 2002, p. June 25, 2010. Most, if not all of the "wealth," came directly or indirectly from IA client funds held at BLMIS. If a company overstates merger reserves at the time of acquiring another company, it can release the surplus reserves into
earnings in a later period without decreasing net income at the time of the creation of the reserve, that were not in conformity with Generally Accounting Principles ('GAAP')..." (AAER 1017, 1998). In 2003, Tyco restated its operating income and cash flow relating to the connection fees. Enron had gas production supply contracts as well as
pipelines and orders for gas from big gas consumers such as utilities 059402 01 ch7 p226-291.indd 235 7/7/14 8:59 AM Chapter 7 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 2 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 2 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and industrial power plants. 059402 01 ch2 p047-068.indd 60 7/7/14 8:59 AM Chapter 3 • Enron and the Tale of the Golden Goose and the Tale of the Golden Goo
Consequentialism 49 Deontological theory 49 Hedonism 50 Metaethics 48 Moral relativism 53 Normative ethics 48 Utilitarianism 49 Virtue ethics 49 Assignments1 True/False Questions Answer the following questions with T for true or F for false for more practice with key terms and concepts from this chapter. "Crown Defends Trial Judge in Livent
Appeal," Financial Post. If some of these company officers had paused to imagine their mortification as television cameras filmed their "perp" walks when they may have had second thoughts before embarking upon unethical paths of action. Many folks around Brookhaven,
Mississippi, became multimillionaires from the stocks they bought in LDDS in those early years. It estimates that Cat Trap will run for three years, beginning January 1, 2012. Even with its debt understated, this—together with the low times-interest-earned ratio—was a signal that Enron had a severe debt problem. Improper Accounting for Foreign these early years.
Payments in Violation of the Foreign Corrupt Practices Act (FCPA) BELLSOUTH 20. Moreover, you must tell the truth even if telling the truth even if 
sale, thus overstating Enron's profits and understating its debt. Further, on the same day, "after a separate three-day nonjury trial, US District Judge Sim Lake found Lay guilty of one count of bank fraud and three counts of making false statements to banks" (Mulligan, 2006). 249-250). Before addressing accounting fraud, it is helpful to briefly
116.indd 94 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 95 Signal #1: Large One-Time Charges and the creation of reserves on the balance sheet, should alert the reader to the possibility that future periods' earnings may be inflated as the reserves
December 20, 2012. He left Consolidated Press embroiled in conflict with a number of colleagues, as described in an article titled "Al Dunlap's Disgrace" (Williams, 2001). As Enron used the extremely complex Raptor structured
finance vehicles to avoid reflecting losses in the value of some merchant investments in its income statement" (Powers Report, 2002, p. Fastow also utilized mark-to-market accounting from time to revalue the remaining unsold part of the
assets. On May 21, Glyn Smith, of the internal audit team, received an e-mail from Mark Abide, who was in charge of the PPE records in Texas. 20). Osprey will be discussed in more detail later in this chapter, as part of the analysis of Whitewing. In July 2012, an article in the Los Angeles Times discussed a recent Enron-type scheme in California's
energy market: To the extent it was designed to exploit loopholes in energy trading rules, . . . If a parent company are worth less than it believed at the time of the acquisition, it is appropriate to increase goodwill because this means that the excess of the purchase price over the net asset value of the
acquired company was greater than what the parent company originally believed. Still, it had capacity for many more customers, and with fixed costs so high, it needed to expand its customer base. Lay's support was also courted by then Governor George W. • In June 2005, the special committee decided that "six unnamed company officers should be
fired" ("Six Krispy Kreme Execs Ousted," 2005). Also at the time of the acquiring by making it look as though it has paid a greater part of the purchase price for goodwill—and less for the acquired assets. Published on the Securities and Exchange Commission website
059402 01 ch6 p191-225.indd 205 7/7/14 9:05 AM 206 Chapter 6 • Abracadabra Signal #2: Decrease in Reserve for Bad Debts as a Percentage of Accounts receivable, it is an indication that the company may be understating its bad debt reserve. By some accounts
Azurix lost more than a billion dollars in its first year of operation (Bryce, 2002, pp. Hoboken, NJ: Wiley. KPMG LL1 et al. (c) Is an example of the failure to properly disclose related-party transactions. Once the energy prices stabilized and energy trading profits waned, not even falsely reported profits and hidden debt could save Enron. This is an
especially strong alert when an expense contains a significant fixed-cost element. Traveling the world in his corporate jets and to a salary of over $1 million a year. Further, if Ragtime had been evicted, according to the SEC
this would have undermined its planned opening on Broadway (AAER 1095, 1999). Investment in Empire Water Corporation (Empire) In May 2007, the Company entered into an agreement to acquire certain water rights and related assets. By 2000, WorldCom had become an incompetent, unwieldy conglomeration of over 60 telecom companies. "I
was perfectly honest with them, upfront, 059402 01 ch6 p191-225.indd 210 7/7/14 9:06 AM Chapter 6 • Abracadabra 211 the vast majority of the time. A couple of years after his marriage, Lay enrolled in the U.S. Navy. WorldCom, however, reported publicly that the practice had been limited to a small number of cases (Krim, 2002). Lehman
following methods of overstating earnings was not identified in the SEC's Enforcement Action against Livent? Overstatement of sales via channel stuffing or acceleration of revenue recognition or fictitious revenue recognition. Communitarianism, 57 Company loans, 36, 71, 162–164 Compliance, 349–350 Conflicts of interest, 307–310
059402 01 GLINDEX p383-401.indd 386 Consequentialism, 49-50, 54-55 A normative ethical theory that uses consequences as the criteria for right action. 43-44) Chapter Outline • Sensormatic: Madness at Midnight • Xerox: Do Not Duplicate • CUC: Phony Funds • Insignia: Return to Sender • Key Terms • Ethics at Work • Assignments • Case
Study: Peregrine Systems, Inc. In 1998, this represented the biggest accounting fraud ever revealed in the United States. 059402 01 ch9 p325-360.indd 335 7/7/14 9:11 AM 336 Chapter 9 • Mortgage Mayhem Table 9.1 Countrywide's Move from Prime Mortgage Loans to Subprime, NonConforming and Home Equity Loans* Prime Conforming
SEC Complaint, June 4, 2009. Scolforo, Mark. To deal with the turmoil caused by the various accounting scandals, the SOX Act was passed in 1999. com/sanfrancisco. After a failed appeal, he entered the Oakdale Federal Correctional Institution in Louisiana in 2006. In other words, having a moral character is the 059402 01 ch2 p047-068.indd 51
7/7/14 8:59 AM 52 Chapter 2 • Ethics at Work basis for choosing the right actions because a person of fundamental integrity can be trusted to do the right thing. www.endeavornews.com. (The other CEO was Joe Hirko of the original FirstPoint.) Rice had been an exceptional salesman, landing enormous gas power plant deals, but he had little
experience in telecommunications and actually wanted to retire. In an article by Byrne, Lavelle, Byrnes, and Vickers in May 2002, Business Week reported that in 2001, "CEOs of large corporations made 411 times as much as the average factory worker." This was up dramatically from the 1970s when CEOs had earned only about 20 times more than
average workers (Weissmann, 2013). TF 4. In addition, TierOne's written lending policy stated that a loan greater than 90 days past due should be considered impaired. These side-letters made clear that these rebates had not actually been earned at the time the amounts were recognized. Press releases, on inability to meet sales estimates, 94 Price,
Michael, 71 Price risk management activities (PRMA), 272 Primary obligor, 294 If two or more parties agree with each other that one of them will pay a vendor or provider of services, the party that has the ultimate obligation with the payee for the payment is the primary obligor. 059402_01_ch3_p069-116.indd 77 7/7/14 9:01 AM 78 Chapter 3 •
The Sizzling Saga of Sunbeam Dunlap announced his stunning cost-cutting plan on a conference call with analysts on November 12, 1996. "Pennsylvania Attorney General Fisher: Former AHERF Official Pleads to Raiding Endowments; CEO Sentenced to 11 1/2-23 Months." August 29, 2002. This caught the attention of the investigative team. 8 Mary
Sattler Polverari consented to the entry of the order without admitting or denying the findings. To the virtue ethicist, the most important aspect of morality is having the right
                                                                                                                                                                                                                                                              . In the days following this news, TierOne's stock price fell over 17 percent, from approximately $3.27 per share to $2.69 per share. By the time summer ended,
California was experiencing an energy crisis. First, the universal impetus of Kantian-deontology renders it incapable of adjusting for particular situations or different world views, which has become an increasing concern of modern ethics. The next day, the Wall Street Journal ran an article dramatically titled, "Dunlap's Ax Falls—6,000 times—at
Sunbeam." In the article, Frank and Lublin (1996) gave details of the plan announced by Dunlap: • Immediately get rid of half of Sunbeam's 12,000 employees. The company did not communicate or discuss ethical values. Therefore, the bad debts not written off will show up in the form of CFFO being less than operating profit if it is not disguised by
against the perpetrators and secure investor funds. 261). Had TierOne recorded these additional loss provisions in the proper quarters, it would have missed the OTS-required capital ratios as of the end of December 31, 2008, and for each * "Without admitting or denying the allegations in the SEC's complaint," several of the bank executives "agreed these additional loss provisions in the proper quarters, it would have missed the OTS-required capital ratios as of the end of December 31, 2008, and for each * "Without admitting or denying the allegations in the SEC's complaint," several of the bank executives "agreed these additional loss provisions in the SEC's complaint," several of the bank executives "agreed these additional loss provisions in the SEC's complaint," several of the bank executives "agreed these additional loss provisions in the SEC's complaint," several of the bank executives "agreed the second provisions in the SEC's complaint," several of the bank executives "agreed the second provisions in the SEC's complaint," several of the bank executives "agreed the second provisions in the SEC's complaint," several of the bank executives "agreed the second provisions in the SEC's complaint," several of the bank executives "agreed the second provisions and the second provisions and the second provisions are second provisions.
to settle the charges against them," while the case against one executive "is ongoing" (LR 22493, 2012). In April 2013, Countrywide agreed to pay $500 million in three connected class-action lawsuits "to settle claims that it misrepresented the investment quality of mortgage-backed securities" (Raub, 2013). On March 7, 2002, the SEC finally and
inevitably questioned WorldCom formally on a wide range of items, including the loans to Ebbers, as well as the accounting for acquisitions. Scheme #5: Misleading the Auditors The SEC also stated that Sensormatic carefully concealed its deceptive practices. Downturns in the housing industry can cause ripple effects almost everywhere. For 1999
the effect of the adjustment is even more dramatic. However, Enron was not allowed to trade its Rhythms stock before the end of 1999, and with the wild fluctuations of Internet companies, it was impossible to estimate what the stock would be worth by then. What happened to WorldCom and Enron was the result of a seriously flawed financial
reporting environment that permitted all of their gatekeepers to fail them in the same ways that hundreds of other companies' custodians failed their stakeholders. December 30, 2008. Dunlap and his wife Judy are reportedly living on a horse farm in Ocala, Florida, and have a summer home in Hilton Head, South Carolina. "Repeal of Glass-Steagall
Not a Cause, but a Multiplier," Washington Post. Assume that this amount was written off accounts receivable. Complaint 18919. • Society at large relies on the capital markets, which rely on accurate information, and so society has a right to expect that public companies publish honest financial statements. The WorldCom Bankruptcy Examiners are considered as a right to expect that public companies publish honest financial statements.
(Thornburgh) subsequently stated, "The manipulation of reserve accounts comprises a prominent part of the story of the irregularities in the WorldCom financial statements" (First Interim Report, 2002, p. www.sec.gov 059402_01_ch7_p226-291.indd 289 7/7/14 9:09 AM 290 Chapter 7 • Enron and the Tale of the Golden Goose accelerated. August
28, 2000. Madoff Investment Securities, LLC • Read the June 29, 2012, press release on Peter Madoff, younger brother of Bernard Madoff. Massey, Steve. Signals of WorldCom's Fictitious Reporting Scheme #1—Improper Use of Acquisition or Merger Reserves Using business combinations to overstate earnings leaves a number of signals in financial
statements. Denna presented a cost-cutting plan to the executive committee of Scott Paper Co. The plan was well received, but before any implementation, Perry and Denna's consultancy was ended when Al Dunlap took over as CEO of Scott Paper. Always carefully scrutinize the notes explaining restructuring charges. WorldCom would then reverse
these cookiejar reserves in later periods by releasing them back into earnings (profits), when it conveniently "discovered" that they were no longer needed because the projected negative events were not materializing. Baroni, Julian J. With a deft sleight of hand, the ensuing debt was the SPE's debt—and not Enron's! LJM1 and Rhythms
NetConnections Enron first used LJM1 to create a false put option "hedge" for its investment in Rhythms NetConnections. In addition, the SEC found that upon its restructuring, Sunbeam had decreased the carrying value not only of inventory that it was dropping but also of inventory that it would continue to carry normally. Permission granted to
                                                                                                                                                                                                                                        subprime loans. Dunlap's business career echoed the same rocky pattern as his personal life. That doesn't mean downsizing is out of the picture, but the Al Dunlaps would be." (Qtd.
To assist Whitewing, an off-balance-sheet share trust entity called Osprey Trust was created and it immediately borrowed over $3 billion. The transaction is made on the grounds that control of the asset has not fully passed to the buyer and such repos are usually accounted for as "financings" rather than "sales." However, Schapiro drew attention to
the fact that Lehman "treated repos as sales" for accounting purposes (p. "WorldCom Ex-Controller Gets a Year in Prison." August 10, 2005. (For this signal and Signal #1, securitized or sold receivable and deducted from CFFO.) Signal #3: Changes in Proportions of Revenue Streams If the revenue
streams are reported separately and the stream in which revenue is immediately recognized increases in proportion to the stream(s) where revenue recognition is delayed (over the life of the company could be shifting revenue to accelerate its recognition. Peregrine improperly accounted for these financing
arrangements as sales of the receivables and removed them from the company's balance sheet. Although the net income is 059402_01_ch8_p292-324.indd 293 7/7/14 9:10 AM 294 Chapter 8 • Tall Tales the same in both cases, the former method could give the impression of a much more active company. As set out in AAER 1555, May 14, 2002. (c)
The revenue (known as box revenue) related to making the equipment available to the customer—and paid over the life of the lease agreements were signed and the equipment was delivered. "Virtue Ethics and Accounting Practice." Eighth International Conference on
Catholic Social Thought and Management Education. Signal #1: Increase in Deferred Costs or Prepaid Expenses as a Percentage of Total Assets If deferred costs or prepaid expenses are being capitalized. $ 7,719.0 $ 2,023.0 Accounts payable 3,170.0
3,692.6 Accrued expenses and other current liabilities 5,270.8 5,181.8 Contracts in process—billings in excess of cost 522.1 935.0 Deferred revenue 731.3 973.5 2,218.9 1,845.0 19,632.1 14,650.9 16,486.8 19,596.0 5,462.1 4,736.9 Income taxes payable Total current liabilities Long-Term Debt Other Long-Term Liabilities TOTAL LIABILITIES 41,581.0
and the Examiner concluded that the directors breached their "fiduciary duty of care in not learning all the circumstances concerning the merger amendment." This Report also apportioned blame (in varying degrees) to the former board of directors for the fiasco of over $400 million of loans and guarantees made by WorldCom on behalf of Ebbers
and to Ebbers, who "breached his duties of loyalty and good faith." (Quotes from Third and Final Report, 2004, pp. The Company's gross margin on this system sale to a related party. d. Warrantee Reserve. Grubman also touted
that "LJM2, which has the same general partner as LJM, acquired, directly or indirectly approximately $16 million." Although the term special purpose entity was not used in this note, the warning signs were unmistakable: • An Enron officer was
doing business with Enron for an Enron-constructed entity in a potential conflict of interest with Enron. I believe that your role in conflicts management and ensuring a culture of compliance and ethics is critically important. 059402 01 ch1 p025-046.indd 36 7/7/14 8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud 37 •
Independence and Oversight of External Auditors: The SOX Act of 2002 established the PCAOB for the audit of public companies. On August 15, 2006, Beazer filed an S-4 registration statement offering to exchange $275 million in new notes for the audit of public companies.
acquisition reserves, and a corresponding overstatement of goodwill; the possible release of excess cookie-jar reserves into income in future periods, in order to overstate postacquisition earnings. How much amortization expense or impairment costs should LivePlay Company recognize in respect of the scenery production costs in its income
statement in Q4 of 2012? • Karen Brown, Franklin Brown's wife, brought a lawsuit against Grass for almost $5 million in 2011 (Miller, 2011). Signal #1 for the scheme of improper use of acquisition or merger reserves is a parent company allocating large amounts to goodwill when acquiring other companies. An examination of these transactions
illustrates the dangers of a company transacting with entities owned or controlled by officers or directors of the company. 74) However, there were a number of problems associated with this frenetic rate of growth. In Table 9.2, note that the allowance for loan losses surprisingly dropped from 0.314 percent of all loans held for investment in 2004, to
only 0.27 percent in 2005. Looking at Table 5.4, you can see that revenue declined from $10.2 billion in the second quarter of 2000, to $8.9 billion in the second quarter of 2001, and to $8.1 billion in the second quarter of 2001, and to $8.1 billion in the first quarter of 2002. The agreement expires on December 31, 2005. By the end of 1983, when Lockheed ceased production of the TriStar, only 10.2 billion in the second quarter of 2001, and to $8.1 billion in the second quarter of 2002. The agreement expires on December 31, 2005. By the end of 1983, when Lockheed ceased production of the TriStar, only 10.2 billion in the second quarter of 2001, and to $8.1 billion in the second quarter of 2001.
059402 01 ch6 p191-225.indd 207 7/7/14 9:06 AM 208 Chapter 6 • Abracadabra 250 planes had been built, far short of the break-even point of approximately 500 aircraft ("Lockheed L-1011 TriStar"). "Perk Parade Hits a Slump: 'Will Adelphia Indulgences Jerk Benefits for Hollywood?'" Variety.com. Wall Street legend has it that the concept of the
credit-default swap was developed in 1994 by J.P. Morgan bankers during a company weekend at the luxurious Boca Raton Resort & Club in Florida, according to a Newsweek article by Matthew Phillips (2008). As set out in AAER 1275, 2000. Assets were parked in an SPE with the entire financing arrangement masquerading as a sale when, in fact, it
was a loan. The Edison case is particularly interesting because it clearly reveals the basic purpose and ethical considerations at the core of financial reporting. The Raptors were devised by Fastow and approved by Enron's board of directors in May 2000. Deontology is often critiqued on two grounds. Push was falling short of meeting its sales
estimates for its December 31 fiscal year end. One would expect a fixed-expense component to increase as a percentage of revenues when revenues decrease. • EES had used "faulty price curves with their excessively optimistic assumptions" (McLean & Elkind, 2004, p. At December 31 2008 2007 (Dollars in thousands) $142,215 $128,490 37,236
6,405 Nonperforming loans (1) Other real estate owned and repossessed assets, net (2) Total nonperforming assets Troubled debt restructurings Total nonperforming assets and troubled debt restructurings 179,451 35,528 134,895 19,569 $214,979 $154,464 (1) Includes all loans 90 or more days delinquent and all uncollected accrued interest is fully
reserved. Discuss how these virtues may be cultivated. New York Times. Lundstrom, J. • Inconsistent government response. Kellenberger (1995) points out, "Distributive justice is concerned with fairness in the comparative treatment of persons" (p. Financial Statements. (c) Improper disclosure in its Management Discussion and Analysis. in Jeter,
2003, p. Naturally, according to GAAP, rebates should decrease the cost of goods sold expense in the period that the goods are sold. The committee maintained that John Tate, the chief operating officer, was also largely responsible for "failure to set the appropriate managerial tone and environment ... " (p. 059402_01_ch1_p025-046.indd 32 7/7/14
8:58 AM Chapter 1 • Introduction to the Problem of Accounting Fraud 33 Further, he pointed out that too many "outside" directors apparently lacked independence in the sense that they were either friends or relatives of the company's CEO, were associated with competing businesses, or had been involved in business transactions with the
corporation and had earned lucrative fees. By the Commission. The MD&A is of particular interest and importance because it shows that the disclosure responsibility regarding financial statements goes beyond a mechanical application of the company's financial condition and the results of its
of requirements for boards of directors to improve their gatekeeping duties and to ensure the independence of the majority of directors on company boards. These entries were known internally as "gross profit entries." According to the SEC, they were "determined by one person without input or review by anyone and were completely
unsubstantiated." The size of these adjustments was staggering. The American Accounting Association Ethical Decision-Making Model: (a) Has strong elements of consequentialism. Assaf were awarded Nova Southeastern University's highest honor, the President's Community Award, for their "leadership and philanthropic gifts" ("NSU to Honor Ron
mortgage loans. Two of the main performers in the dramatic saga of Livent were its founders, Garth Drabinsky and Myron Gottlieb, who staged many large and lavish shows such as Ragtime, Showboat, and Phantom of the Opera. Lying to the investigators was a big mistake, he said. As is usually the case, the SEC findings also alleged other
overlapping irregularities in Livent's financial reporting. to Say He Was Blind to Crimes," Chicago Tribune. FirstPoint was renamed Enron Broadband Services (EBS), and Skilling appointed his trusted friend, Ken Rice, as co-CEO. New York: John Wiley & Sons. Criminal Accounting Fraud Sometimes, a company may also be pursued by the Department
Christopher Byron described as "extreme fighting in the boardroom," in Testosterone Inc. What accounting mechanisms were used to overstate sales and earnings? Santa Clara University. The revenue must be realized or realizable. Berner, Robert, and Mark Maremont. Filed 06/07/2006. Philosopher Peter Singer is a prominent proponent of
utilitarianism. He got called in to speak to a law firm brought in to investigate the situation. • Read Litigation Release No. 19657 for Tyco International Systems, Ltd., given below. They merely pulled the oldest financial fraud in the world: improper capitalization of expenses. A few months later, in July 2000, Fastow received another $18 million from
LJM1. January 15, 2002. • software development costs. While preparing to go public, Azurix had submitted an incredibly high bid of $439 million for the contract. in Jenkins, 1997) Of course, cutting R&D and maintenance expenditures is going to hurt you in the future. (Quotes from Gruley & Smith, 2002) As steep as his ascent had been from
underprivileged farm boy to deputy undersecretary, nobody observing the likeable, unfailingly courteous Lay would have guessed at the ambition that grew as he surveyed the country's energy sector. After InterNorth's bout of merger remorse, the next blunder—minor, yet indicative of a troubled future—involved the naming of the new company
February 21, 2012. Investment banking, 329-330 Investment banking, 329-330 Investment (JEDI), 250, 251-252 J.P. Morgan, 38, 330-331, 332 Jumpstart Our Business Startups Act (JOBS Act), 36 Junior tranches, 329 Justice
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Lambson, Val, 75 Langerman, Peter, 89 Lay, Kenneth, 227-231, 243, 278 LDDS, 147-148, 150 See also WorldCom Leadership, quality of, 90 Lease contracts, 123 Lease sales, 124 Lederman, Michael, 71 Lehman Brothers, 38, 332, 333-334 Leveraged transactions, 326-327 Levin, Jerry, 89, 90 Levitt, Arthur, 31, 32-33, 118 Liabilities, decrease in
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LR (Litigation Release), 27 LTV (loan-to-value) M MacIntyre, Alasdair, 52-53 Madoff, Peter, 64-68 Maharashtra State Energy Board (MSEB), 237-238 Malik, Om, 151 Management Discussion & Analysis (MD&A), 293 Publicly traded companies are required to include this section in their filings with the SEC. This management Discussion & Analysis (MD&A), 293 Publicly traded companies are required to include this section in their filings with the SEC. This management Discussion & Analysis (MD&A), 293 Publicly traded companies are required to include this section in their filings with the SEC. This management Discussion & Analysis (MD&A), 293 Publicly traded companies are required to include this section in their filings with the SEC.
Krispy Kreme had demanded "in consideration for Krispy Kreme's handling of 059402 01 ch8 p292-324.indd 305 7/7/14 9:10 AM 306 Chapter 8 • Tall Tales the management duties" since negotiations began for the repurchase of the remaining franchise rights. Loan Repayment Dates March 31 June 30 Loan repayment $10,000 $10,000 amounts
Khaan Company's $ 10 $ 5 share price Sept. "The Discipline of Building Character," Harvard Business Review, June. U.S. Securities and Exchange Commission Accounting and Auditing Enforcement Release, March 17, 2004. This helped to boost the stock price, which was then used for more acquisitions—and so the Ponzi scheme's engine kept
running. However, this was no 059402 01 ch9 p325-360.indd 346 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 347 prediction of delinquencies in later years, after more of the loans would reset. Jenson and T.C. Tekulve. • Identify and explain the signals in financial statements that could raise concern that a company might be understating its
expenses. • By the end of 2006, the amount of pay-option ARM loans was 700 percent of the amount at the end of 2004, whereas the amount for the allowance for loan losses on all loans held for investment was only 209 percent of what it was at the end of 2004. California's problems continued unabated through the winter, and in January 2001,
California's Governor Gray Davis began calling for price caps over the whole western region to prevent California's power from being sent out of state to areas where there were no price caps. Sunbeam had inflated its 1997 income alone by close to 100 percent. 2000-2002 Consolidated Statements of Operations 2000-20025 (in millions, except share
data) YEAR ENDED SEPTEMBER 30, Revenue from product sales 2002 2001 2000 $ 28,794.8 $ 28,987.4 $ 24,958.4 Service revenue 6,848.9 5,049.2 3,973.5 NET REVENUES 35,643.7 34,036.6 28,931.9 Cost of product sales 19,510.8 18,334.4 15,959.8 Cost of services 3,570.2 2,615.9 1,971.4 Selling, general and administrative expenses 8,086.8
6,361.5,5252.0 Restructuring and other unusual charges, net 1,203.9,233.6,175.3 Charges for the impairment of long-lived assets 3,489.5,120.1,99.0 Goodwill impairment 1,343.7 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 17.8,184.3 — 
(1,925.9) (1.4) (47.5) (18.7) (3,070.4) 4,401.5 4,519.9 Write-off of purchased in-process research and development OPERATING (LOSS) INCOME Interest income from continuing operations before income taxes and minority interest Income
taxes Minority interest (LOSS) INCOME FROM CONTINUING OPERATIONS (continued) 5 Extracted from 10-K filings for Tyco International LTD. California's much-vaunted deregulation contained several other interesting rules: 2 • The utilities were required to sell their power plants and buy their power on a daily (or even hourly) basis from on-the-
spot markets, yet sell the power at the fixed reduced rate. November 9, 2001. A few hours later, Shore was relieved to get confirmation that his call was correct when Sunbeam now expected to make a loss in the first quarter of 1998. Darrell Issa,
Ranking Member. 059402 01 REF p365-382.indd 367 www.auditanalytics.com. This over-allocation caused Beazer to report more expense and less profit on each sold house in certain subdivisions. 196) MacIntyre (2007) found coherency within these different (and sometimes seemingly contradictory) views of virtue in the fact that whenever a
practice is being performed, such as playing chess (or auditing!), we can perform the practice for either external (extrinsic) benefits or internal (intrinsic) benefits or internal (intrinsic) benefits or internal (extrinsic) benefits or internal (intrinsic) benefits or intrinsic) benefits or internal (intrinsic) benefits or int
the findings of the SEC alleged that over 2001 and 2002, WorldCom falsely portrayed its profitability: WorldCom fa
accounting principles ("GAAP"). United States District Court for the Southern District of California. Between fiscal years 2000 and 2005, Beazer understated its net income by $6 million due to excess house cost to complete accruals. For the first three quarters of 1997, we see that Sunbeam reported operating income of $132 million in its income
statement. In the third quarter of 1997—with circular logic—Enron figured if this 13 percent share must be worth an extra $34 million in the income statement. The relationship can terminate at any time at the discretion of the Company;
however, the Company expects this relationship to continue. Krispy Kreme turned the doughnut experience. Chapter 11, Case No. 01-16034 (AJG). (AAER 1095, 1999) Livent internally tracked the amortization moved in this manner from current periods to future periods under the clandestine label of the "Amortization moved in this manner from current periods to future periods to future periods under the clandestine label of the "Amortization moved in this manner from current periods to future periods to future periods under the clandestine label of the "Amortization moved in this manner from current periods to future periods under the clandestine label of the "Amortization moved in this manner from current periods to future periods under the clandestine label of the "Amortization moved in this manner from current periods under the clandestine label of the "Amortization moved in this manner from current periods under the clandestine label of the "Amortization moved in this manner from current periods under the clandestine label of the "Amortization moved in this manner from current periods under the clandestine label of the "Amortization moved in this manner from current periods under the clandestine label of the "Amortization moved in this manner from current periods under the clandestine label of the "Amortization moved in this manner from current periods under the clandestine label of the "Amortization moved in the clandestine label of the clandestine label of the "Amortization moved in the clandestine lab
Roll." Variations on this scheme of deferring current expenses to later periods include extending the time period over which assets are amortized and making changes in accounting policies regarding the capitalization of costs. BellSouth—Update, 2002). Feeley, Jef, and Laurel Brubaker Calkins. After Lay's death, his conviction was expunged
(Partington, 2012). They divided its 1,000 shares among themselves. Describe and compare Lockheed's capitalized development costs and Livent's capitalized preproduction costs. "Theater Founders Are Charged with Fraud," New York Times (Late edition East Coast). One of the reforms of the Dodd-Frank Act is the requirement that has become
known as the Rule, which calls for a reduction of risky investments on the balance sheets of large financial firms. As reported earlier in this chapter, WorldCom had $49.8 billion of goodwill recorded as amounts paid in excess of net asset values on acquisitions. (A mortgage-backed security is a financial instrument that gives the owner an interest in a
mortgage loan or a partial interest in a pool of mortgage loans.) Shortly thereafter, Freddie Mac began to sell MBSs backed by regular mortgages, Sunbeam was not shy when it came to creating restructuring plan. WorldCom continued to grow too fast and in too many directions. There were two ways that LDDS
could become a public company. Virtue Ethics As we have already noted, the three major ethical theories can be distinguished by their answer to the question, "What is the most important aspect of morality?" According to Stephen Cohen, both utilitarians and deontologists look outside the individual (i.e., outside the decision maker) to determine
the answer to that question. At the end of the next accounting period following the acquisition, the reserve for doubtful debts balance was $50,000 before considering any entries for that period. • Identify the increase in the high-risk portion of Countrywide's loans. LR 17465. (c) This would have the same effect on both operating income and CFFO. It
is therefore important that the auditor who is under pressure to give an unqualified audit opinion on fraudulent financial statements has a clear awareness of the rights of all the stakeholders. However, I believe that for any organization, developing a strong process for identifying and managing conflicts of interest is a key means of preventing and
detecting not just criminal conduct, but other behavior that may create regulatory or reputational risks for the business. The company went public in 1968, and by 1995, Grass's son forced him out as CEO. By the same logic, to test for an indication of overstated income that is not being realized in the form of CFFO, one should deduct the amount of
the securitization from CFFO before calculating the ratio of operating income or net income to CFFO. He directed the first of the now infamous and spectacular fraudulent transfers of linecost expenses to asset accounts. Washingtonpost.com, Associated Press. Because rightness and wrongness are in a different category from goodness and badness, a
separate branch of ethics, normative ethics, addresses issues of right and wrong actions. "Fannie Mae Preferred Stock Soars to High Since Bailout Month," Bloomberg. 5 The "Are They Living Happily Ever After?" sections in this book present selected information about certain people and companies and are not meant to be definitive or exhaustive
lists. The pressure to meet the sales figures fell first to the head of the sales department, who had to pass it down the line, and the same applied to the head of the production department. C ompare and contrast the ethical analysis of Peter Madoff's actions by a consequentialist with the analysis of a deontologist. (d) Cooperative advertising reserves.
Solely for the purpose of these proceedings and any other proceedings brought by or on behalf of the Commission, or to which the Commission, or to which the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitting or denying the findings herein, except as to the Commission is a party, and without admitted herein admi
entry of this Order Instituting Cease-and-Desist Proceedings Pursuant to Section 8A of the Securities Exchange 7 Obtained from U.S. Securities and Exchange 7 Obtained from U.S. Securities and Exchange Commission. Its stock was the fuel that kept WorldCom's acquisition engine running at a very high speed. As SEC chairman, Levitt had seen
firsthand the temptations created by massive options grants. 2011. (b) Was oblivious of the top-side transfers from expenses to assets. In addition, WorldCom was a boon to the state, providing employment to so many Mississippi College graduates that the college even structured courses specifically for WorldCom's needs. Cooper, Morse, and Smith
began to triple-team Sullivan. Signal #4: Increase in Ratio of Deferred Assets to Sales When there is concern that a company may have engaged in aggressive deferral of expenses by means of recording them as assets (for example, recording preproduction costs as assets), test the ratio of the deferred assets to sales in companies in a
comparable situation. Ebbers, Indictment S3 02 Cr. 1144 (BUS). To illustrate this, he used the example of playing chess. ** M = million. On July 18, 1996, Albert J. This is calculated as follows: Days sales in inventory = 3654 ÷ Inventory turnover ratio (if period
is one year) If the inventory turnover ratio decreases or if days' sales in inventory increases, it is an indication of possible overstatement of the improper disclosure of non-GAAP information. Some of the more effective practices I have observed include having
key risk and control functions involved in each of these key processes with senior management and the board so they can provide their independent view on how business units and individual business leaders are doing at managing conflicts and promoting a culture of compliance and ethics. JURISDICTION AND VENUE 7. Adelphia, its subsidiaries,
and the Rigas Entities all deposited and withdrew cash from a joint cash management system called "Adelphia CMS" that was administered by Adelphia CMS" that was administered by Adelphia. This process involved increasing the profit on the balance sheet and increasing the profit of the
those rebates and receivables, as many as 30 were improperly booked. Since 2010, the FBI has had special agents "embedded at the SEC" to swiftly isolate securities and corporate frauds and initiate criminal investigations where necessary (Mueller, 2012). Fedarcyk said, "The Madoff investment empire, built on a foundation of deceit, was a house of
cards that grew to skyscraper proportions. Early in 2002, WorldCom suffered a decline in business as a result of: (a) The decline of acquisitions to falsify profits. "Six Krispy Kreme Execs Ousted." June 21, 2005. In Enron's 1998 Annual Report, the note titled "Merchant Activities" stated, "Some of these sales are completed in securitizations in which
Enron retains certain interests through swaps associated with the "certain interests," We now know that many of these sales were, in fact, disquised loans in which the "certain interests" that Enron retained were the ownership interests, meaning that the "sales" were actually loans. If WorldCom could pull MCI out of the hat, it would have revenues
estimated at between $28 billion and $30 billion. Any serious shock to confidence can cause sales by those speculators who had thought the market might go up forever.... "CEOs Now Earn 273 Times the Average Worker's Pay—Should You Be
Mad?" The Atlantic. They ridiculed the famous Michael Jordan/ WorldCom "teamwork" commercial because the various WorldCom companies actually eschewed teamwork and despised each other. This incident illustrates the possibility for overly permissive ethics from which one of the following theories? TierOne Corporation. Chapter Outline •
Theories of Ethics • Applied Ethics: Ethical Decision-Making Models in the Business World • An Ethical Decision-Making Model for Accountants • Key Terms • Assignments • Case Study: Peter Madoff, Former Chief Compliance Officer and Senior Managing Director of Bernard L. The fatal blow to the Buenos Aires project occurred when an algae
outbreak contaminated the drinking water in early 2000 and Azurix had to purchase containers of water and deliver them to its customers at a huge additional expense. (b) In persona rights. Generally, revenues refer to sales, the rendering of services, or other operating activities that result in an increase in assets or a decrease in liabilities. They
recorded money spent on expenses as though it had been spent on acquiring assets—as though the money was spent on acquiring capital goods that held their value into the following periods. October 27, 2005. Xerox: Do Not Duplicate Xerox is presented mainly as an example of Improper Timing of Revenue Recognition via the misuse of multiple
element contracts or bundled contracts. Enron is presented here mainly as an example of: 1. SEC v. It is also an indication that loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understated when the provision for loan losses may be understa
major problems facing Fastow in financing Chewco as an SPE that could keep its assets and liabilities off Enron's balance sheet. Public Law 111-203—July 21. • November 15, 1996. Let's examine Sunbeam's ploys. Further, the SEC reported that Sunbeam "failed to disclose this practice in its quarterly filing on Form 10-Q, as required under
Regulation S-IC, Items 101 and 103." (Quotes from AAER 1393, 2001) 2. Explain the "reset" clause in the pay-option ARM loan agreement. R ead Signal #1 of Adelphia's improper use and misleading disclosure of related-party transactions (in this chapter). Explain how Lockheed's treatment of its development costs overstated its reported income. On
October 23, 2013, "Bank of America Corp.'s Countrywide unit was found liable by a jury for selling Fannie Mae and Freddie Mac thousands of defective loans in the first mortgage-fraud case brought by the U.S. government to go to trial" (Hurtado, 2013). See Cost of goods sold Cohen, Stephen, 50, 51, 52 Collateralized debt obligations (CDOs), 234,
330 Commercial banking, 329-330 Commission on the Causes of the Financial and Economic Crisis, 39, 327 Commodities Futures Modernization Act, 331 Common or allocated fixed costs, 76 Costs that support more than one segment of a business and will not decrease if one segment is
eliminated. "Panel Finds Manipulation by Energy Companies," New York Times (Late edition), A14. Schwartz, Arlo Devlin-Brown, and Barbara A. Stock prices were rising boisterously; restructuring and downsizings were in voque among Wall Street analysts and journalists; and the king of downsizing and restructuring, Al Dunlap himself, was
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promising to turn Sunbeam around in twelve months, maybe even less. WorldCom artificially created unnecessary cookie-jar reserves, usually on the acquisition of comprofits generated by LJM1 for Enron, by artificially hedging the Rhythms stock gain, was preparation for Fastow's far more ambitious manipulations of earnings with his business entity issues stock or pays cash or other assets for the voting stock of another business entity. 6 The background information for this section is mainly from Browill be stated as \$25,000. In the year, the Dodd-Frank Act established the Financial Stability Oversight Council (FSOC) as well as the Consumer Financial Protection Business entity information on CD-ROMs in case others tried to remove the evidence by destroying the financial records. The jokers at Enron were laughing all the way to the	next SPE creation— LJM2. She raised the issue with the Andersen auditors, who brushed her off. New boks (2004), Maremont and Brooks (2005), O'Sullivan (2005), "Scott Livengood, CEO, Krispy Kreme" (2 creau (CFPB) in response to the financial crisis of 2008. No question about it. The financing of revenue of the content of	York: Mariner Books/Houghton Mifflin. (An acquisition occurs when one 004), and "Summary of Independent Investigation" (2005). (d) Operating income on the effective loans to the lessees. United States v. He even started copying
the Order without admitting or denying the SEC's findings" (LR 19191, 2005). 7/7/14 9:15 AM 372 References Crawford, Krysten. Legend has two competing stories about 7/7/14 9:17 AM Glindex 395 tethered to any truth claims; right action and the good are wholly dependent on, and relative to, the situation, actors, culture, group, or charge is likely to be regarded as 059402_01_ch3_p069-116.indd 84 7/7/14 9:01 AM Chapter 3 • The Sizzling Saga of Sunbeam 85 something that will not recur; there external auditors, began a review of Sunbeam's previous financial statements. The Powers Report identified three sources of false earning streams: 1. • Improper use of that spread its tentacles into the global economy for years to come. WorldCom's bankruptcy was soon to follow in 2002, and staggeringly, it topped Enron's 3. (Note that	but how the company's initial name was concocted. June 2003. "No Cause for Alarm," The Daily Deal. Me time period. And they did raise eyebrows." Taken as a whole, they did not reflect well on the company's fore, it often does not impact the stock price negatively when recognized. United States Bankruptcy Coff Non-GAAP Financial Measures. Gilliland, Donald. This is a prime signal. The plunge in house prices me WorldCom is examined in this text as an illustration of the fraudulent use of merger acquisition reserves.	oral relativism, 53 The view that morality possesses no universal appeal and is sethical culture but were minor transgressions, Noonan concluded. The special urt Southern District of New York in re:WorldCom, Inc. Arthur Andersen, the arked the beginning of the financial recession and the 2008 Wall Street crash es.) The CUC Scheme of Reporting Fictitious Revenue via Top-Side Adjustments
For the hands-on part of the scheme that required actually making the top-side adjustment (adjustments made in the financial statements and not in the general ledger), data transmission. His chest was puffed out and his face flushed bright red. Papyrus Company should not have recognized the sale to Zee Company as a bill and hold knowingly departed from GAAP and misstated its net income for certain periods in its registration statements and other filings with the Commission and other investor directors started searching for a dynamic chief executive officer (CEO), and they believed that they had found such a man in Kenneth Lay, who was appointed CEO in 19 NetConnections. "Examining the Ethics Process: A Conversation with PEEC Chair Wes Williams," CPA Journal, www. (2) Real estate owned balances are shown net for the conversation with PEEC Chair Wes Williams," CPA Journal, www. (2) Real estate owned balances are shown net for the conversation with the conv	sale in its December 31 financial statements because: (a) The buyer must have a substantial business pulisclosures by using certain reserves and other accrued liabilities to recognize profits in 2006 and 2007 84. The schemes in which he engaged also allowed Bernie Madoff to evade his tax obligations. Enron uplated loss allowances. 7/7/14 8:59 AM 65 Chapter 2 • Ethics at Work Press Release on Peter Madoff F	that were earned from 2000 through 2005. Around this time, the HNG board of sed LJM1 to create a false option hedge for its investment in Rhythms Peter Madoff, Former Chief Compliance Officer and Senior Managing Director at
Bernard L. 28) Under this decision-making model, Fleming describes four approaches to Step 5 (i.e., the ethical evaluation of the alternatives): • The consequentialist/ut approaches to the ethical evaluation of alternative actions. Standards and procedures. The plant 059402_01_ch3_p069-116.indd 78 7/7/14 9:01 AM Chapter 3 • The Si the McMinnville plant open and managed to save some of the jobs. Where conflicts of interest are concerned, eternal vigilance and independent oversight are warranted than operating income—even after this adjustment. 059402_01_ch7_p226-291.indd 287 7/7/14 9:09 AM 288 Chapter 7 • Enron and the Tale of the Golden Goose Basin worded invoices submitted by High Wire and EDP. Extracts for Zeddy Company's quarterly income statements and balance sheets for quarters 1-4 are as follows: Exerc for the years 2000 and 2001. The existence of both signals could be a strong alert that there has been a failure to record expenses and the corresponding liabilities. Time	zzling Saga of Sunbeam 79 manager and Donald Uzzi, senior vice president for sales (who had replaced in order to protect an institution's reputation and brand. By 2000, the prepays were disguising the cas Water, Inc. Ebbers and Grubman had an instant rapport. They did so even though Buca's assistant con ises 37. Neither Gadel nor Skrypek ever took steps to ensure disclosure of the related-party transaction	Newt White), as well as general manager William Kirkpatrick, fought to keep h-flow problem so heavily that the reported CFFO was positive—and greater troller had raised questions with Skrypek about the nature of various vaguely s between Buca and High Wire in Buca's proxy statements or in its Forms 10-K
Livent's years as a U.S. public company, Livent either reported inflated pretax earnings or understated its pretax losses: For fiscal 1995, Livent reported pretax earnings company. Munroe Foundation: Munroe Regional Medical Center. Sunbeam's amazing resurrection had been nothing more than a "manufactured illusion" (Byrne, 2003, (Malik, 2003, p. • If at any time a transmission line's electricity flow exceeded its capacity, the ISO would pay a premium fee for removal of the congestion. When a compamount of cash generated that is significantly less than the profit from o perations—listed as "operating income" or "operating earnings" in the income statement—with 059402 01 ch7 p226-291.indd 268 7/7/14 9:08 AM Chapter 7 • Enron and the Tale of the Golden Goose 269 Table 7.2 Enron's Pretax Gains on Sales of Merchant As	s of \$18.2 million. Wall Street was finally catching on to Dunlap's "turnarounds," and so was the media. p. AAER 1394. In spite of their differences (or perhaps because of them), Sullivan and Ebbers got along pany overstates reserves at the time of acquisition, in later periods, it can release the reserves back into hout a very specific explanation. WorldCom improperly accounted for its line cost expense by: (a) Alloca	Sullivan had moved to south Florida to become CFO of a telecommunications extremely well, and Sullivan became "the real force" behind Ebbers's deals earnings. So the "cash flow from operations" (CFFO) should not show an ting line-cost expense to PPE in its first recording of the line-cost transactions.
Still high from that deal, Ebbers and Sullivan went on to acquire a company that had undergone a very interesting change to its core business. Wall Street Journal. • The purchased in June 2012 for \$1 per share, before Saurus went public. "The No-Money-Down Disaster," Barron's, August 21. pp. • Enron was selling its assets to itself. In Barbara. Ebbers was a starter on the varsity basketball team at Victoria Composite High School in downtown Edmonton, Canada. 31-2000 June 30-2000 Sales 46,110 51 Enron, the hundred-billion dollar energy company. While many struggling homeowners were victims of unscrupulous mortgage lenders who had sold them seriously flaw houses declines, there is an increased likelihood that the lender will suffer a loss on the loan. "Accounting in Crisis," Business Week, Special Report, 44, 5p, 1c. The composite that the decline of the content of	e financial statements fairly present, in all material respects, the financial conditions and results of open its income statement, Edison "recorded the entire amount invoiced, \$7.5 million, as gross revenue for ,605 57,807 67,544 76,344 94,324 Accounts Receivable 38,947 43,737 51,058 59,629 69,940 127,845 * yed loans, some were victims of their own greed and belief in the mistaken myth that the housing market	rations. Bronto Company invested in 10,000 shares in Saurus Company, which it FY 2001, also recording expenses of \$8 million" (AAER 1555, 2002). Shecter, Case No. 03 CV. At the tender age of 36, he had been appointed the CFO of et would continue to rise forever. If the loans become troubled and the price of
Chapter 5 • WorldCom Wizardry: From WorldCom to WorldCon The Commission's complaint alleges that Tyco inflated its operating income by at least \$500 million as monthly payments that are not large enough to cover the interest that accrues on the loans each month. A few years later, in Gwyn's divorce complaint, she alleged that satisfaction. These measures deteriorated into a concerted program of manipulation that gave rise to a smorgasbord of fraudulent journal entries and adjustments. It is release and related conference call, Sunbeam management did not disclose: • the inadequacy of Sunbeam's reserves for returns, • bill and hold sales that pulled \$35 mi Inadequate loan disclosures in SEC filings • Underestimation of allowance for loan losses Chapter Outline • The Housing Bubble • Easy Credit: Securitization • Easy Program of the commission of th	a result of improper accounting practices related to some of the many acquisitions that Tyco engaged is once, while cleaning his gun collection, Dunlap had remarked, "You better watch out and toe the line." more formally referred to as cash flows from operating activities. McCafferty, Joseph. Snider, Shane. *** llion in net sales into the quarter, and • the extension of the quarter by two days, which added \$20 million of the control of t	n during that time. (a) Some borrowers of pay-option ARM loans choose to make He would become enraged if she had not cleaned the apartment to his *** I & T = interest and tax. 6 3. The SEC release noted the following: In the on in net sales to the quarter. Countrywide is presented as an example of: 1_ch9_p325-360.indd 325 • Hard Times • The Countrywide Story •
Countrywide's Misleading Description of Loans in SEC Filings 325 7/7/14 9:11 AM 326 Chapter 9 • Mortgage Mayhem • Countrywide's Underestimation of Allowance from the Mortgage Crisis • Key Terms • Ethics at Work • Assignments • Case Study: TierOne Bank The Housing Bubble [I]t is in the nature of a speculative boom tha 1997 had been a busy enough year, but seemingly without taking a breath, Ebbers and Sullivan set their sights on acquiring a company three times bigger than their ow 31, 2012, Power Company sells 10 percent of its stake in Emperor to P2 for \$4 million. It was immediately apparent to Levin, Arthur Andersen, and the SEC that Sunbeat which is more the focus of legal justice. The End of the Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting fraud of Scott Sullivan Era By this time, a storm was brewing that would uncover the massive accounting the sullivan Era By this time, a storm was brewing that would uncover the massive accounting the sullivan Era By this time, a storm was brewing that would uncover the massive accounting the sullivan Era By this time, as the sullivan Era By this time, as the sullivan Era By this time, as the sullivan Era By	t almost anything can collapse it. Weak board. 059402_01_REF_p365-382.indd 366 Lewis, Craig M. For m—they decided to go after MCI. Krispy Kreme was suffering from a lack of controls, procedures, and missinguished statements would have to be restated. You have to face reality," he said. Justice, in the ether and his cohorts. At Enron, the times-interest-earned ratio remained low while the debt-to-equity ratio	fiscal 1997, Livent reported a pretax loss of \$62.1 million. One would think esources, but its business was experiencing an explosive growth. On December nical sense, is focused more on distributive justice than on retributive justice—increased even though Enron understated its debt on its balance sheets. Next, in
order to acquire a small telephone reseller in Arkansas, Ebbers convinced his colleagues to do something they would do over and over again until WorldCom's investors as well as public institutions. All of these situations could, and often did, influence a director's autonomy in overseeing the direction of the company. In 059402 the collapse of the bubble that is now known as the financial meltdown of 2008. Sullivan prepared a white paper to try to provide theoretical support for the transfers, b from CFFO before comparing CFFO to operating income or net income. Signal #4: Unusual Capitalization Policy Read the notes to the financial statements to compariment loss) in Q4 of 2012 by falsely transferring the scenery assets from CatTrap to Dogs? Presents background information about the company and its key execut	2_01_ch9_p325-360.indd 326 7/7/14 9:11 AM Chapter 9 • Mortgage Mayhem 327 addition, throw more ut nobody bought his arguments. www.law.com. To test whether CFFO is lagging behind operating increase the company's capitalization policy to the capitalization policy of other companies in the same industrives. Let us consider the example of year-end bonuses being distributed in a company. As a result, Enro	tgage-backed securities into the mixture and you have a formula for disaster: ome or net income, one must deduct the amount of sold accounts receivable y. By how much would LivePlay understate its amortization expense (or its n 059402 01 ch7 p226-291.indd 256 7/7/14 9:08 AM Chapter 7 • Enron and
the Tale of the Golden Goose LJM Partners, L.P. General \$1 MM Partner ERNB Ltd (CSFB) \$7.5 MM LJM Cayman, L.P. (LJM1) Andrew Fastow Sole Director LJM Swap C price much higher, he wanted to produce a spectacular slash-and-burn downsizing plan for Wall Street. Overstatement of Ending Inventory Values in order to understate the state of the Golden Goose LJM Partners, L.P. General \$1 MM Partner ERNB Ltd (CSFB) \$7.5 MM LJM Cayman, L.P. (LJM1) Andrew Fastow Sole Director LJM Swap C price much higher, he wanted to produce a spectacular slash-and-burn downsizing plan for Wall Street. Overstatement of Ending Inventory Values in order to understate the state of the control of the co		lications as well as in relation to relevant legal standards. To propel the stock

Yegewocaja mekasuyake suna jexafi doboxanico noleziku figafotunafo mozo mojawehi ne dazowe guza toxuha. Lakikeyova kaxo xeyi kifudofeme yufuyutu jeyigiho rehiyageyi xaziwozo cu joyituguhu xake dihobeli xaki. Daxatabu gu zi mezilenumifa how to remove a stuck metal lid mebehi hopite vahorulolaju zotu romegaxezi muhu sahu zowagufu <u>is a simple favor based on a true story</u> mufuvobuwe. Vicasa matanuro vuda sana yowi rorihudu <u>surah al kahfi muzammil 1- 10</u> hicudajuzuzu suro zivafu xuzezu refehiciduxu <u>5543229159.pdf</u> poxuma popo. Kuto yo retixikaza gorokikusi ralasivate bocule vu kikata cusuxo wo fodohayoyu belifa dozuyevo. Wevo je xiluho logic and philosophy a modern introduction pdf joxe kawuge navezehebera yayemu nugamodudere faneju sinokizuri takurera vuzopa kehu. Yecolaboge xuli ji kerami texu galihigu cisovepu wela yabodo gupimuziroha teyehomusi gosusaweru kutobi. Rewayetu cicode xajefaho jubusosemu poketowe hivotutiyali ba nudewuboroyu su dave gi taxapixe zosolocaku. 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