

# “Corporate governance disclosure: a study of NIFTY companies”

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## SECTION 3. General issues in management

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### Corporate governance disclosure: a study of NIFTY companies

#### Abstract

Corporate governance (CG) is the acceptance of the inalienable rights of shareholders as the true owners of the corporation and the role of the management is perceived as that of trustees on behalf of the shareholders. It defines the parameters of accountability, scrutinizes the reports and disclosures with the objective of fulfilling the purpose of the corporation's existence in this era of globalization with the aim directed towards the shareholder's welfare. The failure of high profile companies like BCCI, Enron, WorldCom and Parmalat was a clear lesson of the harm bad corporate governance can inflict. For the sake of investors, corporate governance also provides a comprehensive and structured system of disclosure about the company to make better investment decisions. This paper uses companies' annual reports to analyze the disclosures with respect to CG Indian corporations using secondary data of all the 50 companies included in NIFTY. Results reveal that nearly 10 companies can be called model companies which have presented details in a meticulous manner as per Clause 49, while other companies have not provided the same level of disclosure described in the above said clause. Some companies have provided only negligible details regarding this matter. Empirical evidence shows that businesses with superior governance practices generate larger profits, higher returns on equity and larger dividend yields, so all Indian companies should strive for greater CG disclosure to prevent scandals.

**Keywords:** corporate governance, scandals, disclosures, investors, stakeholders, transparency.

**JEL Classification:** G01, G11, G18, G34, G35, G38.

#### Introduction

Corporate citizenship – a commitment to ethical behavior in business policy, operation and tradition – has been on the edge of *corporate governance* and board leadership, related primarily to company's goodwill. Corporations to work effectively and maintain growth, boards must integrate these new dimensions into their core decision-making processes. The global financial crisis has heightened the need for corporate boards of directors to give well-informed strategic direction and work more judiciously. Corporate governance is based on principles such as conducting the business with all integrity and fairness, being transparent with regard to all transactions, making all the necessary disclosures and decisions, complying with all the laws of the land, accountability and responsibility towards the stakeholders and commitment to conducting business in an ethical manner. In other words, corporate governance is about commitment to morals, ethical business conduct, and transparency and makes a difference between personal and corporate funds in the management of a company. Corporate governance (CG) is the interaction between various members (shareholders, board of directors, and corporation's management) in determining corporation's performance. The relationship between the owners and the managers in a business must be healthy and there should be no differences between them. Various definitions are given for corporate governance. For instance, Cadbury Report (UK), 1992 AS, states 'Corporate

governance is the system by which companies are directed and controlled'. Milton Friedman has defined corporate governance as 'the conduct of business in accordance with shareholders desire which generally is to make as much money as possible while conforming to the basic rules of society embodied in law and local customs. Denis & McConnell (2002) defined Corporate Governance as 'an arrangement of a set of internal and external mechanisms designed and adopted to ensure that self interested managers act to maximize the value of the company to its shareholders'. Organization for Economic Cooperation and Development (OECD) defines CG as, 'A set of relationships between a company's management, its board, its shareholders, and other stakeholders. There are different views about CG like 'Corporate Governance is an area where a flexible regulatory regime allowing ample variation across firms is particularly desirable as there is considerable variation in the relation between different governance indices and different measures of performance' (Bhagat, Bolton and Romano, 2008). CG practices have been found to vary across institutions and environments (Gordon & Roe, 2004; Zattoni & Cuomo, 2008), cost of capital is higher in countries with poor corporate governance (Dyck and Zingales, 2004) as well as nations (Aoki, 2001; Gordon & Roe, 2004). The principal characteristics of effective corporate governance are transparency (revelation of related financial and operational information), leadership for efficiency with responsibility, accountability and reporting, good corporate citizenship, protection and enforceability of the rights and privilege of all shareholders and directors.

The impetus for this new understanding of board responsibilities can be found in a growing number of global and industry specific initiatives. Chief among these are the Organization for Economic Cooperation and Development (OECD) Principles of Corporate Governance and the United Nations Global Compact. This paper gives insights and a comprehensive view on corporate disclosure practices which will be a useful tool in strategizing actions aiming a closer scrutiny of the governance of corporations and aim at prevention of scandals. This paper is organized as follows. Introduction section gives the meaning and vital details of the corporate scandals. Section 1 gives need and call for corporate governance owing to corporate mismanagement and unethical practices. Section 2 gives comprehensive review of literature. Section 3 explains the data and methodology used. Section 4 contains analysis and interpretation of the data through a variety of tables into which relevant details have been compressed and summarized under appropriate heads and presented in the tables. The final section concludes the paper.

### 1. Call for corporate governance

Corporate governance has become an important matter because of several reasons like fraud and misuse in the corporate world. Nowadays, it is important for almost all people including academicians, policymakers, institutional investors etc. In the Asian financial crises weak investor protection was a key factor in exacerbating stock market declines (Johnson et al., 2000). Another study states that corporate governance is one which facilitates us to know how corporate work, their goals and principles, their reporting lines, to which they are accountable to, the way returns are managed, remunerations paid, etc. (Isaksson and Kirkpatrick, 2009). Bebchuck and Hamdani (2009) indicate that quality of CG and investor protection has direct relationship with the performance of firms as well as the economies. Dyck and Zingales (2004) have found that the cost of capital is higher in countries with poor CG. Firm's value can be reduced by inadequate investor protection. In the macro level, inadequate investor protection may obstruct stock market development and decrease the financial growth.

The Securities Exchange Commission (SEC) came into existence in 1934 due to the corporate mismanagement and unethical practices which were the main cause of Great Depression of 1930s in the overall market. After the establishment of the SEC, corporate ownership and control were redefined in a different way. In 1970s there were many business scams found in US Corporations due to unveiling and pervasive unethical business practices in the economy. Illegal contracting practices, insider trading, deceptive advertising and savings and loan

scandals were investigated in a BIG way and they were controlled by SEC to a lot extent. As per a survey, hundreds of US Companies and Business Houses accepted the corporate misconduct and after that more transparency was observed everywhere in the market. Due to the governance failures which were the major reason for investors' dissatisfaction, the public in general was forced to take necessary action so as to improve the governance of corporations. It resulted in the demand for mandatory disclosure and compliance by corporations which activated a movement from 'soft law' practice to 'hard law' requirement of mandatory disclosures and compliance with standardized governance practices strictly supervised by the regulators. It gave birth to the number of investors associations, powerful committees, exchanges, effective commissions etc. To improve the poor governance of the economy, various initiatives were taken by these committees and commissions like Tread way Commission and the SEC Blue Ribbon Commission in the USA, the Cadbury Committee in the UK, the Vienot Committee in France, and the Peters Report in the Netherlands. All these committees and commissions had a common goal that is a sound governance requires transparency, investor protection etc. During the early 2000s, major scams like WorldCom, TYCO, Qwest, Enron, etc., have failed the laws that were passed to address the responsibilities relating to competent performance and levels of disclosure for corporations. It is found that unethical accounting practices were committed by exaggerating profits by the book partnerships, by playing with the profit figures to the extent of billions of dollars etc. It was all because of self-indulgence, arrogance and ignorance for law, at the cost of investor confidence and shareholders. As per the report of NCAER- Growth Trade and Economic Management-2009, "the loss in global capital inflow by 2009 is estimated to be more than \$7 trillion in the capital market. The Satyam scam is one worth considering knowing how the shareholders lost their confidence because of irregularities in the accounting disclosures in India. Satyam's balance sheet of 2008 reflected inflated figures for cash and bank balances of Rs. 5,040 crores as against Rs. 5,361 crore reflected in the books. The mismanagement in the disclosures reveals a non-existent accrued interest to the extent of Rs. 376 crores, an understated liability of Rs. 1,230 crores on account of funds, and an overstated debtors' position of Rs.490 crores. It must be noted that Satyam was the 2008 winner of the popular Golden Peacock Award for Corporate Governance (World Council for Corporate Governance – UK). It was stripped from them in the aftermath of the scandal, under Risk Management and Compliance Issues.

The main principle of CG is transparency and investor protection. Corporations with strong corporate governance structure and procedure are most likely to disclose more information in comparison to poor corporate governance. According to Rahman (1998) and Johnson, Boone, Breach, & Friedman (2000) “lack of transparency of corporate financial reporting is the root cause of the East Asian financial crisis that happened in the mid nineties”. Mitton (2002) states on the need for disclosure in corporate governance that satisfactory disclosure is its essential element. “Due to the failures and weaknesses in corporate governance arrangement, the current financial crisis could be recognized”, as per OECD (2009). All these factors point out towards the requirement of CG in the current scenario.

## 2. Review of literature

Various studies describe the ‘agency problem’ which means the separation of ownership (by shareholders) and control (by managers) which gives rise to conflict of interests within a firm. According to Bhagat, Bolton & Romano (2008) “the shareholders are not the managers who are in control”. Core et al. (1999) suggest that firms with weaker governance structure have greater agency problems; that firms with greater agency problems allow managers to extract greater private benefits; and that firms with greater agency problems perform worse. Specifically in Asia, it has been shown that both before (Joh, 2003) and after (Mitton, 2002) the Asian financial crisis in 1997, firms that paid attention to good corporate governance practices fared better and provided greater protection to shareholders, especially the minority shareholders. Ho, Tower & Barako (2008) indicate that this agency theory has directed to an issue of ‘information asymmetry’ between the shareholders and managers. In this abnormal relationship, management who act as the agents acquires information about the present and the future performance of the firm, which may be far more superior to the information acquired by shareholders who are the principals. As such there is all possibility that the management may take unnecessary advantage so as to employ in activities that may improve their personal goals. An in depth study of corporate governance by Cohen, Krishnamurthy & Wright have emphasized on Resource Dependence, Managerial Hegemony, Institutional Theory which can be explained as follows. *Resource Dependence* focuses on the role of governance procedures as a tool to help a corporation to achieve its strategic goals. *Managerial Hegemony* is based on the strategy literature and in comparison to the agency theory, it shows the board and its attendant committees as being under the control of management. On-

ly regulatory needs are fulfilled through this theory. *Institutional Theory* indicates that it is essential to understand the matter of the interactions between different governance parties and how these parties use at times symbolic gestures and activities to maintain their form to all relevant parties.

In India the Securities and Exchange Board of India (SEBI) has framed certain rules and regulations for corporate governance by the listed companies, through the listing agreement. In the year 2000, SEBI introduced Clause 49 (provided as Annexure) after conducting a meeting of many large firms, and consequent to a governance code being planned by a leading industry group. These parameters now apply to all the listed public companies in India. The present study has compared the disclosures in the Annual Report of the 50 NIFTY companies for the year 2010-12 with the standard clause 49 of listing agreement.

## 3. Data and methodology

The study is based on secondary data which is collected from reports, journals and websites to examine the position of CG and its disclosure among Indian companies. In the present study a comparison was made with respect to the disclosures regarding CG of all the 50 companies included in the NIFTY. The study used the Annual Reports pertaining to the year 2010-11 of the 50 companies listed in NIFTY. The disclosures regarding CG in the Annual Reports were compared with the Clause 49 of Listing Agreement of Stock Exchanges introduced by SEBI which was taken as a benchmark for this analytical evaluation. The underlying principles behind using the NIFTY companies for the study are the following; NSE is the third largest Stock Exchange in the world in terms of the number of trades in equities. It is the second fastest growing stock exchange in the world with a recorded growth of 16.6%. It is the 9th largest stock exchange in the world by market capitalization and the largest in India by daily turnover and number of trades, for both equities and derivative trading. The turnover of NSE during 2010-2011 was Rs. 1916843.98 crores. In addition, NSE has played a catalytic role in reorganizing the Indian securities market in terms of microstructure, market practices and trading volumes. NSE has a market capitalization of around US\$1.59 trillion and over 1,552 listings as of December 2010.

## 4. Analysis and interpretation

Table 1 presents, the analysis and the details relating to the disclosures of CG as against the Clause 49 of Listing Agreement of Stock Exchanges. Some interesting pattern has been discovered from the analysis concerning the disclosures of CG. The data at present is given under the respective sub-headings.

**4.1. Board of directors.** It is viewed that, of the four aspects given under this heading, details have been supplied in the Report on CG by all the 50 companies only in the first two aspects. In the other two aspects, i.e. information regarding 'Other provisions as to Board and Committees' and 'Code of Conduct', three and six companies respectively has not given adequate information in depth as required.

**4.2. Audit Committee.** Analysis reveals that disclosures were offered by 47 companies each in the first two aspects only, i.e. 'Qualified & independent Audit Committee' and 'Meeting of Audit Committee' respectively, out of the five aspects given under this head in the guidelines. On the other hand, 3 companies made only negligible particulars about these aspects in their report on CG. Further it was observed that only 38 of the companies provided particulars in the Report, under the head 'Power of Audit Committee' where 8 companies did not give any particulars and 4 gave only negligible details. While full details were presented by 39 companies in the aspect 'Role of Audit Committee', 7 did not provide any mention about this, and four of them presented least particulars. At the same time as 42 companies have given particulars under this aspect 'Review of Information by Audit Committee', it was considered better than the above two. Negligible information was provided by 3 companies and 5 companies did not present any information at all. Menon (2009) while, mentioning the example of Satyam episode has clarified that auditor independence is a matter of concern, and is a problem in any big audit failures. The distressing issue is auditor independence, which has confirmed to be a problem in any big audit failures. By performing an in depth analysis of the major steps taken recently he states that 'if an auditor is not independent from the client, then he/she may fail to exercise adequate effort to detect a problem, or even after having revealed a problem, may be unsuccessful to report it'. The Birla Committee (2009), had accepted the significance of audit committees and made many definite recommendations regarding the role and constitution of board audit committees. These suggestions have been supplied with a thought of having transparency in operations and for giving the required information to the shareholders. In the case of the 50 NIFTY companies studied not all companies have given the appropriate information related to the Audit Committee in their CG Reports, which do not bode well for CG.

**4.3. Subsidiary companies.** It was established here in this study that only 33 of the companies provided full details about their subsidiary companies. Whereas one company made available negligible data it

was observed that 16 companies did not give any data at all regarding their particular subsidiary companies.

**4.4. Disclosures.** There are seven different aspects, under the head 'Disclosures'. Based on the suggestions of various committees, all these aspects have been provided here so that there is transparency in all the matters made available to the shareholders (Afsharipour, 2009). In the present study, the analysis of the facts presented a mixed bag with many of the companies disregard this aspect. For instance, though as many as 23 companies did not make any declaration regarding proceeds from public/rights/preferential issues, etc.; four supplied only insignificant data. Likewise, only 29 companies made disclosure about accounting treatment with six of them supplying insufficient data. On the top of it, 46 companies supplied full data relating to the remuneration to Directors, with two each not providing any data or negligible data. Based on the facts available to us, the 50 companies studied here are considered as the leading players in the Indian Corporate world, and the table presented above present's diverse results seems to give not so better a picture about Corporate Disclosures.

**4.5. Non-mandatory requirements.** The study of facts relating to non-mandatory requirements also provided a picture worth studying in detail. 'Training of Board Members' and Mechanism for Evaluating Non-Executive Board Members' are the two main aspects relating to the Board provided under this head. It was amazing to note that only less than 50 per cent of the companies have provided details in their CG Report about these two aspects. Moreover, only 30 of the companies under consideration were having a 'Whistle Blower Policy'. According to Afsharipour (2009), the Narayana Murthy Committee had given special reference about this and had even affirmed that whistle blowers must have access to the audit committee even without telling their supervisors initially and that companies should yearly state that they have not denied access to the audit committee or unjustly treated whistle-blowers generally. It is significant to note that although 14 of the companies were not at all having a policy; six companies were either formless or provided only negligible data regarding this aspect. It appears as if, in general, the non-mandatory requirements have been treated by Indian companies in a 'non-mandatory' way.

### Conclusions and recommendations

CG is often expressed as one that has come up as an outcome of separation of ownership and control of the companies. This is of vast significance in the current corporate set-up as good CG is being valued

as a sound business strategy. Additionally, it works as an important catalyst to tap the domestic as well as international capital. India has a lot to do in the area of CG as it has the fastest growing economy. The present study attempts to determine the current patterns of CG among Indian corporate. With respect to the 50 NIFTY companies studied, the disclosures regarding CG in the Annual Report for the year 2010-11 were compared with the Clause 49 of Listing Agreement of Stock Exchanges introduced by SEBI which was taken as a benchmark for this evaluation. The scrutiny of the Reports on CG discovered that certain companies have not given due significance and focus to the features provided in Clause 49. Some of them have given only small details about this matter, and gives the impression to have dealt with this subject in an informal manner whereas some of them have done in a comprehensive way. In view of the fact that numerous international studies have established positive relationship between CG and corporate performance (Fernando, 2006), in terms of increase in share price, profitability, etc., Indian companies should also attempt to attain or even surpass the international standards. The current study determined that Indian companies have to go a long way to meet the international standards of CG because of many weaknesses in the disclosures as per standards. This study attempts to find out only whether the disclosure has been made with respect to Clause 49, so that issues of non disclosures can be highlighted and can be strategized for future course of action for compliance of Clause 49 and meet international standards, but the value of the disclosure has not been analyzed in this study and can be the scope for future research. Good governance is not something theoretical, and it does not happen as a consequence of mishap or unexpected outburst of humanity. It occurs only when the leaders lead with honesty, when directors really direct and when key organizations are held to the highest standards of responsibility by cautious stakeholders and learned individuals. Nowadays more strict standards for financial disclosures, committee and board nominations and audit policies have been created in the USA by the Sarbanes-Oxley Act (SOX), the revised NYSE and NASDAQ listing rules.

The use of SOX 404 tests in a company entails the company's CEO to yearly review internal controls and sign written reports, accepting accountability in maintaining control over financial reporting. Heavy penalties including imprisonment and fines up to \$30 million can be imposed if there is any violation and false declaration made. SOX attention is more on matter than appearance which continue; shift from rule based accounting to the setting up of objective

oriented accounting standards; and reporting based on business prospects, risks, policies and strategies; evaluation of quality sustainability and unpredictability of companies cash flows and funds flow and earnings (including compensation comparison of CEO) through elucidated reporting of audit committee.

The Conference Board published its FDI Confidence Index in which it suggests that India must persist to get better its CG and financial infrastructure to really understand its huge potential. Superior governance calls for a state of mind within the company, which mixes the corporate moral code into the daily activities of its managers and employees. To have quality CG and to evade scandals in the years to come, the company can have improved shareholder's observation and try the following:

- ◆ For board positions learned people with truthfulness and freedom of mind should be chosen.
- ◆ Enough focus should be given to the board governance training, including self-regulating directors, with normal evaluation of their performance.
- ◆ The selection committee should do appraisal of each member of the board, where the chair person of the board discuss their troubles and recommends remedies to them.
- ◆ The main independent director should hold the chair person's performance evaluation.
- ◆ International standards for director independence should be accepted by the board, which reveals whether each independent director pursue GAAP and IAS and meet up the set standards.
- ◆ Executives should be regularly contacted by the board members to be aware of the operational concerns.
- ◆ Audit committee should establish procedures for the treatment of complaints received through anonymous submission by employees or whistle blowers who must be protected.
- ◆ Earlier consent of Audit Committee, the full board and the stakeholders is necessary if any allied party transaction is to be carried out.
- ◆ The performance of the company's CEO, the internal directors and the higher management should be at times evaluated by the independent board members.
- ◆ The board should fix on the higher management's compensation which is reasonable to all stakeholders as well.
- ◆ Independent assessment of financial statements should be done by effective and self-governing Audit Committee, preferably consisting of independent directors to ensure they are free of material misstatement.

- ◆ The guide audit partner and the audit partner responsible for evaluating the company's audit must be changed once in every three to five years.
  - ◆ If intentionally and purposely false certifications made by the CEO & CFO then they should be subject to strict criminal penalties including fines and imprisonment.
  - ◆ To speed up the disclosure of insider trading necessary steps should be taken.
  - ◆ A reasonable, careful, clear and responsible role should be played by State for the regulation of free markets.
- Good companies can do bad things but by applying good corporate governance the bad things can be reduced. A more effective system of CG in India would then have to move beyond shareholder interests to consider the entire value system the company operates in.

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## Appendix

Table 1. Detailed item – Wise disclosure regarding CG of the NIFTY 50 companies

S. no	Main dimension	Sub dimension	No. of firms			
			Yes	No	Negligible details	Disclosure %
1	Board of directors	Composition of Board	50	0	0	100
		Non Executive Director's Compensation & disclosures	50	0	0	100
		Other provisions as to Board & Committees	47	3	0	94
		Code of Conduct	44	6	0	88
2	Audit Committee	Qualified and independent Audit Committee	47	3	0	94
		Meeting of Audit Committee	47	3	0	94
		Power of Audit Committee	38	8	4	76
		Role of Audit Committee	39	7	4	78
		Review of Information	42	5	3	84
3	Subsidiary companies	Subsidiary Companies	33	16	1	66
4	Disclosures	Basis of related party transactions	41	5	4	82
		Disclosure of Accounting Treatment	29	15	6	58
		Board Disclosures – Risk Management	39	7	4	78
		Proceeds from public, rights issues, etc.	23	23	4	46
		Remuneration of Directors	46	2	2	92
		Management	34	12	4	68
		Shareholders	41	5	4	82
5	CEO/CFO certification	CEO/CFO Certification	46	4	0	92
6	Report on corporate governance	Report on Corporate Governance	38	12	0	76
7	Compliance	Compliance	44	6	0	88
8	Non-mandatory requirements	The Board	33	10	7	66
		Remuneration Committee	38	5	7	76
		Shareholders Rights	33	10	7	66
		Audit qualifications	35	6	7	70
		Training of Board Members	21	22	7	42
		Mechanism for evaluating non-executive Board Members	20	23	7	40
		Whistle Blower Policy	30	14	6	60

Table 2. Corporate scandal sheet\*

Company	When scandal went public	Allegations	Investigating agencies	Latest developments	Company comment
Adelphia Communications (otc: ADELA – news – people)	Apr-02	Founding Rigas family collected \$3.1 billion in off-balance-sheet loans backed by Adelphia; overstated results by inflating capital expenses and hiding debt.	SEC; Pennsylvania and New York federal grand juries	Three Rigas family members and two other ex-executives have been arrested for fraud. The company is suing the entire Rigas family for \$1 billion for breach of fiduciary duties, among other things.	Did not return repeated calls for comment.
AOL Time Warner (nyse: AOL – news – people)	Jul-02	As the ad market faltered and AOL's purchase of Time Warner loomed, AOL inflated sales by booking barter deals and ads it sold on behalf of others as revenue to keep its growth rate up and seal the deal. AOL also boosted sales via "round-trip" deals with advertisers and suppliers.	SEC; DOJ	Fears about the inquiry intensified when the DOJ ordered the company to preserve its documents. AOL said it may have overstated revenue by \$49 million. New concerns are afoot that the company may take another goodwill writedown, after it took a \$54 billion charge in April.	No comment.
Arthur Andersen	Nov-01	Shredding documents related to audit client Enron after the SEC launched an inquiry into Enron.	SEC; DOJ	Andersen was convicted of obstruction of justice in June and will cease auditing public firms by Aug. 31. Andersen lost hundreds of clients and has seen massive employee defections.	Did not return repeated calls for comment.
Bristol-Myers Squibb (nyse: BMY – news – people)	Jul-02	Inflated its 2001 revenue by \$1.5 billion by "channel stuffing," or forcing wholesalers to accept more inventory than they can sell to get it off the manufacturer's books.	SEC	Efforts to get inventory back to acceptable size will reduce earnings by 61 cents per share through 2003.	Bristol will continue to cooperate fully with the SEC. We believe that the accounting treatment of the domestic wholesaler inventory buildup has been completely appropriate.



Table 2 (cont.). Corporate scandal sheet\*

Company	When scandal went public	Allegations	Investigating agencies	Latest developments	Company comment
CMS Energy (nyse: CMS – news – people)	May-02	Executing “round-trip” trades to artificially boost energy trading volume.	SEC; CFTC; Houston U.S. attorney’s office; U.S. Attorney’s Office for the Southern District of New York	Appointed Thomas J. Webb, a former Kellogg’s CFO, as its new chief financial officer, effective in August.	No comment.
Duke Energy (nyse: DUK – news – people)	Jul-02	Engaged in 23 “round-trip” trades to boost trading volumes and revenue.	SEC; CFTC; Houston U.S. Attorney’s office; Federal Energy Regulatory Commission	The company says an internal investigation concluded that its round-trip trades had “no material impact on current or prior” financial periods.	Although the effect [of these trades] on the company’s financial statements was immaterial, we consider improper trades in conflict with the company’s policies. To address this we have made changes to our organization, personnel and procedures.
Dynegy (nyse: DYN – news – people)	May-02	Executing “round-trip” trades to artificially boost energy trading volume and cash flow.	SEC; CFTC; Houston U.S. Attorney’s Office	Currently conducting a re-audit. Standard & Poor’s cut its credit rating to “junk,” and the company said it expects to fall as much as \$400 million short of the \$1 billion in cash flow it originally projected for 2002.	Dynegy believes that it has not executed any simultaneous buy-and-sell trades for the purpose of artificially increasing its trading volume or revenue.
El Paso (nyse: EP – news – people)	May-02	Executing “round-trip” trades to artificially boost energy trading volume.	SEC; Houston U.S. Attorney’s Office	Oscar Wyatt, a major shareholder and renowned wildcatter, may be engineering a management shakeup.	There have been no allegations or accusations, only requests for information. The company has confirmed in multiple affidavits that it did not engage in “round-trip” trades to artificially inflate volume or revenue.
Enron (otc: ENRNQ – news – people)	Oct-01	Boosted profits and hid debts totaling over \$1 billion by improperly using off-the-books partnerships; manipulated the Texas power market; bribed foreign governments to win contracts abroad; manipulated California energy market.	DOJ; SEC; FERC; various congressional committees; Public Utility Commission of Texas	Ex-Enron executive Michael Kopper pled guilty to two felony charges; acting CEO Stephen Cooper said Enron may face \$100 billion in claims and liabilities; company filed Chapter 11; its auditor Andersen was convicted of obstruction of justice for destroying Enron documents.	No comment.
Global Crossing (otc: GBLXQ – news – people)	Feb-02	Engaged in network capacity “swaps” with other carriers to inflate revenue; shredded documents related to accounting practices.	DOJ; SEC; various congressional committees	Company filed Chapter 11; Hutchison Telecommunications Limited and Singapore Technologies Telemedia will pay \$250 million for a 61.5% majority interest in the firm when it emerges from bankruptcy; Congress is examining the role that company’s accounting firms played in its bankruptcy.	No comment.
Halliburton (nyse: HAL – news – people)	May-02	Improperly booked \$100 million in annual construction cost overruns before customers agreed to pay for them.	SEC	Legal watchdog group Judicial Watch filed an accounting fraud lawsuit against Halliburton and its former CEO, Vice President Dick Cheney, among others.	Halliburton follows the guidelines set by experts, including GAAP (generally accepted accounting principles).
Homestore.com (nasdaq: HOMS – news – people)	Jan-02	Inflating sales by booking barter transactions as revenue.	SEC	The California State Teachers’ Retirement pension fund, which lost \$9 million on a Homestore investment, has filed suit against the company.	No comment.
Kmart (nyse: KM – news – people)	Jan-02	Anonymous letters from people claiming to be Kmart employees allege that the company’s accounting practices intended to mislead investors about its financial health.	SEC; House Energy and Commerce Committee; U.S. Attorney for the Eastern District of Michigan	The company, which is in bankruptcy, said the “stewardship review” it promised to complete by Labor Day won’t be done until the end of the year.	Did not return repeated calls for comment.

Table 2 (cont.). Corporate scandal sheet\*

Company	When scandal went public	Allegations	Investigating agencies	Latest developments	Company comment
Merck (nyse: MRK – news – people)	Jul-02	Recorded \$12.4 billion in consumer-to-pharmacy co-payments that Merck never collected.	None	The SEC approved Medco's IPO registration, including its sales accounting. The company has since withdrawn the registration for the IPO, which was expected to raise \$1 billion.	Our accounting practices accurately reflect the results of Medco's business and are in accordance with GAAP. Recognizing retail co-payments has no impact on Merck's net income or earnings per share.
Mirant (nyse: MIR – news – people)	Jul-02	The company said it may have overstated various assets and liabilities.	SEC	An internal review revealed errors that may have inflated revenue by \$1.1 billion.	This is an informal inquiry, and we will cooperate fully with this request for information.
Nicor Energy, LLC, a joint venture between Nicor (nyse: GAS – news – people) and Dynege (nyse: DYN – news – people)	Jul-02	Independent audit uncovered accounting problems that boosted revenue and underestimated expenses.	None	Nicor restated results to reflect proper accounting in the first half of this year.	Our focus now is to stabilize this venture and put some certainty to its financial results. The company is evaluating its continued involvement in this venture.
Peregrine Systems (nadaq: PRGNE – news – people)	May-02	Overstated \$100 million in sales by improperly recognizing revenue from third-party resellers.	SEC; various congressional committees	Said it will restate results dating back to 2000; slashed nearly 50% of its workforce to cut costs; is on its third auditor in three months and has yet to file its 2001 10-K and so, consequently, is in danger of being delisted from the Nasdaq.	We have been and will continue to cooperate with the SEC and the Congressional committee.
Qwest Communications International (nyse: Q – news – people)	Feb-02	Inflated revenue using network capacity "swaps" and improper accounting for long-term deals.	DOJ; SEC; FBI; Denver U.S. Attorney's Office	Qwest admitted that an internal review found that it incorrectly accounted for \$1.16 billion in sales. It will restate results for 2000, 2001 and 2002. To raise funds, Qwest says it is selling its phone-directory unit for \$7.05 billion.	We are continuing to cooperate fully with the investigations.
Reliant Energy (nyse: REI – news – people)	May-02	Engaging in "round-trip" trades to boost trading volumes and revenue.	SEC; CFTC	Recently replaced Chief Financial Officer Steve Naeve with Mark M. Jacobs, a managing director of Goldman Sachs and a Reliant adviser.	We're cooperating with the investigations.
Tyco (nyse: TYC – news – people)	May-02	Ex-CEO L. Dennis Kozlowski indicted for tax evasion. SEC investigating whether the company was aware of his actions, possible improper use of company funds and related-party transactions, as well as improper merger accounting practices.	Manhattan district attorney; SEC	Said it will not certify its financial results until after an internal investigation is completed. The Bermuda-based company is not required to meet the SEC's Aug. 14 deadline. Investors looking to unseat all board members who served under Kozlowski may launch a proxy fight to do so.	The company is conducting an internal investigation and we cannot comment on its specifics, but we will file an 8-K on the initial results around Sept. 15.
WorldCom (nasdaq: WCOEQ – news – people)	Mar-02	Overstated cash flow by booking \$3.8 billion in operating expenses as capital expenses; gave founder Bernard Ebbers \$400 million in off-the-books loans.	DOJ; SEC; U.S. Attorney's Office for the Southern District of New York; various congressional committees	The company stunned the Street when it found another \$3.3 billion in improperly booked funds, which will bring its total restatement up to \$7.2 billion, and that it may have to take a goodwill charge of \$50 billion. Former CFO Scott Sullivan and ex-controller David Myers have been arrested and criminally charged, while rumors of Bernie Ebbers' impending indictment persist.	WorldCom is continuing to cooperate with all ongoing investigations.
Xerox (nyse: XRX – news – people)	Jun-00	Falsifying financial results for five years, boosting income by \$1.5 billion.	SEC	Xerox agreed to pay a \$10 million and to restate its financials dating back to 1997.	We chose to settle with the SEC in April so we can put the matter behind us. We have restated our financials and certified our financials for the new SEC requirements.

Note: \* Compiled by SEC: Securities and Exchange Commission. CFTC: Commodity Futures Trading Commission. DOJ: U.S. Department of Justice.