

WHY ACCOUNTANCY FRAUD THRIVES IN AMERICA

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Corporate crime is booming once again in America. America has always been its natural home. In 2005 a long line of American ‘whiz kid’ CEOs went to jail with life or near life sentences—Dennis Kozlowski and Mark Swartz of Tyco, John and Timothy Rags of Adelphia, Andrew Fastow of Enron, Martin Glass of Rite Aid, Jamie Oles of Dynegy Sam Wicksal of ImClone and of course Bernie Ebbers of WorldCom. By persecuting individuals and sparing companies—Enron, WorldCom, Arthur Andersen, Tyco and Rite Aid continue to survive and often, thrive—American judges have shown their awareness of the link between burgeoning corporate crime and impending capitalist crises.

The American justice system’s commitment to capitalism has been graphically demonstrated by its treatment of Arthur Andersen and KPMG—two of the global accounting industry’s “final four”. Both Andersen and KPMG have admitted to serious fraud and both have been spared by the American Supreme Court and the American Justice Department: Arthur Andersen settled out of court with WorldCom investors in April 2005 and in May the American Supreme Court overturned its 2002 conviction. The judgment amounted to exonerating Arthur Andersen.

The American Department of Justice has been extremely reluctant to bring legal action against KPMG. European Union regulators (after intensive lobbying by Arthur Andersen) have warned it that bringing KPMG to the courts would destabilize the global accountancy industry. KPMG’s corruption is well known. An American senate committee report issued in May 2005 exposed the fraudulent and highly lucrative tax avoidance business run by KPMG for years and in July 2005 KPMG admitted “full responsibility for unlawful conduct” with respect to what the US Senate described as “abusive tax practices”. Abusive tax practices are of course not confined to KPMG. Deloitte Touche has moved swiftly to avoid action with regard to misconduct of its associated firms in a case filed by investors. The Senate Report hinted at similar business deals involving Price Waterhouse Coopers and Ernst and Young. The American Justice Department is however bending all the rules unscrupulously to avoid the collapse of

another 'Final Four' accountancy firm and to prevent it from following in Arthur Andersen's footsteps. A decision not to punish KPMG severely has been interpreted as a license for continuing frauds. Other accountancy firms throughout the world will feel that it is lucrative and beneficial to take the sort of risks that KPMG took when it advised clients on how to undertake tax frauds.

The "easy" alternative of punishing CEOs while exonerating corporations is also becoming unpalatable. CEOs have expressed reservations about the "chilling effects" of enhanced conceptions of individual legal responsibility for corporate transactions. As long as corporate America's corrupt godfather Dick Cheney continues to call the shots at the White House it will be impossible to dismantle the protective barriers which shield most American corrupt CEOs. Accounting fraud will continue to flourish in America.

Accounting fraud is increasingly common throughout America. In 2005 major accounting frauds have been discovered at General Electric and the AIG and the Standard and Poor downgrades of GM and Ford shares in mid 2005 was also partly fuelled by accounts related suspicions: With the explosive growth of "fair value" accounting—and its official endorsement by American regulators in 2005—the scope for accounting fraud has expanded enormously. A 2005 study by Glass Lewis found that investors lost almost \$ 1 trillion during 1999-2004 due to accountancy related frauds.

"Fair Value" accounting allows firms, in connivance with their auditors, to declare what profits suit them—"fair value" is unfair value in this precise sense. "Fair Value" accounting allows accountants to assign imagined estimated value to items such as bank loans and buildings. A 2004 study by Bergstesser and Rauh has shown that such estimates are usually widely of the mark and very easy to manipulate. They found robust evidence of deliberate tampering of statistics to influence M and A, new issues and stock option deals. Further evidence of fraud is presented by the Lev, Li and Sougiamis' 2005 study which shows that "fair value" accounts estimates are worthless as indicators of a company's future performance, because they are in the main fraudulently estimated. Federal Reserve based records show that bond and loan "fair value" estimates are so volatile that they are practically worthless.

Mathematical model based calculations of "fair values" of financial assets are nothing but fraud. This is because market values of all assets are speculatively determined in capitalist

order—without reference to any objectively determined foundation—and as chaos theory shows there are no rational grounds underlying speculation. "Rational" expectations are a myth. A 2005 much awaited Ernst and Young report admits this when it recognizes that estimated "fair value" for intangible assets, unquoted securities, derivatives, pension costs and share based payments appear in company accounts at a hypothetical market price based on management's assumption about the future and using a valuation model. We consider that it is inappropriate to refer to such estimated value as fair value "Fair Value" ' accounting has deliberately been made increasingly incomprehensible to conceal fraud.

What are American regulators doing to deal with all this? Paradoxically, they are watering down the implementation of the Sarberne-Oxley Act (SOX) to facilitate accountancy fraud. SOX was a panic reaction to the mega accountancy frauds of 2002. Today the imperialist press – the Financial Times, the Economist, the Wall Street Journal—is full of demands to roll back SOX. It requires management boards to waste a “huge proportion of time on reporting procedures”. SOX is accused of “addressing symptoms not causes” and “costs significantly exceed benefits “In May 2005 the American Public Company Accounting Board (PCAOB)—a body established under SOX—chided management for being “overly cautious and mechanical” in interpreting SOX. The American Securities and Exchange Commission has also called for greater management discretion. Section 204 of SOX—requiring management to maintain “an adequate internal control structure and procedures for financial reporting” has come in for heavy criticism. This is said to cost companies in America about \$ 1.4 trillion and according to Deloitte 700,000 additional man hours. It is also said to be leading to a further concentration of the accountancy industry. The “final four”—Deloitte, Ernst and Young, KPMG and PwC—are said to hog 98 percent of the SOX related business. SOX, it is said, discourages risk taking. There is virtually no evidence to show that SOX has reduced fraud..

William Donaldson’s replacement by Christopher Cox as American Security and Exchange Commission Chairman in June 2005 has led to a “lighter application of SOX” according to the Financial Times. The American business press is urging on Mr. COX “to scrap Article 204 of SOX. No doubt he will do so but you eat an apple bite by bite.

That accountancy fraud thrives in America is hardly surprising. Corruption is the American way of life. A 2001 Dept of Justice study found that 43 percent of all income in America is in some form connected to the booming national crimes industry. Moreover, corruption has deep historical and cultural roots. Thirty five million Red Indians were methodically slaughtered and an entire continent looted and plundered for over two and a half centuries through political and financial fraud and corruption. Today the American government is inextricably involved in similar action in Iraq, Afghanistan and much of Latin America. America is the natural home of fraud and its global capital.

But America is also the sole surviving capitalist hegemony and capitalism is a system not a Habermasian life world. Objectively (i.e from an Islamic perspective) finance is fraud, and capitalist property is theft but capitalist order structures finance and capitalist property so that they flourish as normal social praxes. Historically this has required a reconciliation of the practices legitimized by welfare (consumption) maximization with those required by the need for profit (surplus) maximization. Capitalist fraud is action which (a) either prevents a corporation from maximizing profit or (b) enables it to maximize profit in a manner considered illegal because it inhibits welfare (consumption) maximization by the political representatives of free citizens. Global / neo liberal capitalism shies away from recognizing that the capitalist state must be empowered to prevent both types of capitalist fraud. It subscribes to the mistaken (but time honored) belief that markets can be self regulating – i.e that shareholders can discipline (in a Foucaultian sense) managers and that profit maximizing behavior of

antecedently individuated (corporate) persons will automatically un-intentionally lead to the maximization of social consumption (welfare).

Global capitalism has shown both assumptions to be untenable. Managers cannot be disciplined by shareholders in ways which do not inhibit accumulation. Efficient markets do not maximize social consumption. Moreover dominant political forces, specially in America are systematically obstructing the search for viable institutional restructuring to address the agency problem and the problem of increased market un-governability. Social democracy is dead in America and America is killing it in Europe, Japan, China and India. Those working for the overthrow of capitalist order may therefore live in hope.