Arhtur Anderson Scam

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Contents

- **Introduction**
- **Historical Background**
- **Wrong Steps Taken**
- **New Arthur Anderson**
- **Conclusion**

Historical Background

- Arthur Andersen worked before in Price Waterhouse with Clarence DeLany.
- A 28-year-old accounting professor started his own business in 1913 in Chicago (Andersen, Delany & Co).
- In 1918 DeLany left, and the firm changed its name to Arthur Andersen & Co.
- The company developed a philosophy that focused on building a solid corporate culture among all Andersen employees.
- In the1930s, the federal government adopted new laws to require public companies to submit their financial statements to an independent auditor every year.

- Promotion of “4 cornerstones”:
    - Good service
    - Quality audits
    - Well-managed staff
    - Profits for the firm.

- In 1947 Arthur Andersen died, during that period his firm almost experienced a closed down.

- Leonard Spacek, Andersen’s disciple, convinced the company's partners to remain together despite financial uncertainty, and became the managing partner.
- Arthur Andersen Corporation moved to the top of its profession during Spacek’s term.
- It obtained worldwide growth and opened its first international offices during 1950s.
- In 1950 Josef Glickauf demonstrated that computers can be used to automate bookkeeping.

- In 1954 it launched its new computer consulting business.
- In 1960s a mid-level partner made about $60.000- 160.000 in today's dollars.
- During 1970s its consulting business exploded as the demands for information technology increased.
- By 1979 almost a half of its worldwide fees came from consulting and tax work.

- In 1979 it surpassed 1000 partners and became the world’s biggest business services firm.

- In 1989 it formed a separate consulting practice.

- **Andersen Worldwide= Arthur Andersen + Andersen Consulting**

- In 2000 AC became independent and was renamed (**Accenture**, 2001).

- By 2002 AA had 85000 employees around the world, 2300 clients, $9.3 billion in annual revenues.

Competitors

PwC

KPMG

Deloitte

Ernst
& Young

Wrong steps taken by Arthur Andersen

- After the formation of Arthur Andersen (1989) the company failed to withstand the pressure.

- It leaded to a negative influence on Andersen's corporate culture, which enabled Andersen to be more interested in its own revenue growth through ethical and legal misconducts, such as accounting irregularities and fraud.

- Business was growing very slowly due to increased competition and the large number of mergers in the 1990s.

- Arthur Andersen accountants particularly resented being eclipsed by their consulting counterparts at Andersen Consulting.

- “It was a matter of pride” - Richard Measelle.

- Arthur Andersen adopted a new strategy that focused on generating new business and cutting costs which led to substantially higher revenues and profits per partner ($600.000).

- Arthur Andersen began requiring partners to retire at age 56 years.

- The new policies also led to less experienced auditors and fewer partners overseeing audits.

Boston Chicken

- $50000 audit fee turned into $3 million full service engagement;
- The detailed losses in the financial statements were kept off;
- It moved toward an IPO – rousing success;
- Subsequent collapse and bankruptcy led to legal actions against AA for helping to create a façade of corporate solvency.

Waste Management

- Paid to AA $7.5 million in audit fees, $17.8 million in non-audit fees;

- Signing off on inaccurate financial statements;

- Wrongly written off the value of WM assets;

- As a result, profits were significantly overstated.

AA & AC Separation

- AC (leading subsidiary) 15% of annual profits to be paid to AA which created competition between them.
- AC figured out that AA performed for some of the consulting engagements which violated the internal agreement.
- In 1997 AC partners voted unanimously to split off entirely and filed a formal arbitration claim with the International Chamber of Commerce.

- In 2000 AC was allowed to form a new independent company.

- AA did not receive $14 billion payment expected from AC.

New Arthur Anderson

- In 1998, Samek became a new managing partner.
- New strategy – 2X performance evaluation system: e.g. $2 million a year in auditing fees and an additional $4 million in fees from non-audit services.
- Partners who achieved this standard were rewarded, while others were penalized and in some cases dismissed from the company.

- Changes Andersen's organizational architecture (e.g. dress code, new logo).

- A new service - the entire internal bookkeeping function for their clients and provide internal audit services rather than just handling the once-a-year audit of the public books.

Securities and Exchange Commission (SEC) Proposal

- In 2000, the SEC proposed new regulations that would limit the consulting work at accounting firms.
- In July 2000, Samek called the SEC proposal fatally flawed.
- Intense lobbying by the Big Five accounting firms defeated the SEC proposal.
- The evidence that Andersen's corporate culture contributed to its downfall is some ethical misconducts in the fact that Andersen sold lucrative consulting services to Enron.

Enron & AA

- Enron was one of the biggest clients of AA.
- Enron paid fees to AA for provision of better auditing consequences.
- AA completed the better report by sending untrained auditors to the client’s sides or other unethical methods.
- When Enron came under investigation of federal authorities, AA had a huge “shred” campaign.
- The relationship between Enron and Arthur Andersen was seen as a cozy one which made it easy to maintain the improper accounting practices by both parties.

- They set out to make as much money for themselves as possible.
- These selfish acts led both companies into an eventual downfall in bankruptcy.
- On December 2, 2001 Enron Corporation filed for chapter 11 bankruptcy, which was the largest bankruptcy petition in U.S. history.
- It had cleared out shareholder investments that had once been valued at more than $60 billion.
- Many of Enron's employees had large amounts of Enron stock in the company's retirement savings plans.

Arthur Andersen Collapse

- The federal authorities after the Enron collapse started the overall investigation of other AA clients.
- As a result, WorldCom, Qwest Communications, Global Crossing, Merck and Baptist Foundation of Arizona announced themselves insolvent.
- In the end, Andersen agreed to cease auditing public corporations by the end of August in 2002, essentially marking the end of the ninety-year-old accounting institution.

- All the international offices of AA were bought by the “big four”.
- In 2002, the investigation was finished and AA was found guilty.
- In 2005, the Supreme Court of the US remitted the verdict against Arthur Andersen.
- Nevertheless, the discharge did not help one of the world’s leading auditing companies to come back to work.

Conclusion

- The accounting industry reacted to the Enron case and introduced changes (new regulations) that would improve itself and the economy.
- Ethical misconduct causes loss to the public.
- Accounting ethics is significant not only for everything and everyone in the company but also for the society.
- Placing huge profits ahead of ethics and laws is not a go.

Thank You