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A Comparison of Accounting Fraud Before and After Sarbanes-Oxley

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INTRODUCTION

Within all trades of business, the potential for the perpetration of accounting fraud within companies is unfortunately not an infrequent occurrence. Accounting fraud is the "intentional misrepresentation or alteration of accounting records regarding sales, revenues, expenses, and other factors for a profit motive such as inflating company stock values, obtaining more favorable financing, or avoiding debt obligations" (*Business Dictionary*). The reasons for the frequent phenomenon of accounting fraud are countless. To name a few: greed, lack of transparency, poor management information, and poor accounting internal controls signify some of the various explanations for accounting fraud (Frost 1). Whether or not the initial motive to commit fraud is because a company and/or individual decides to falsely account for the company's revenues or expenses, or simply because the clarity of aspects of the company's structure are unclear, accounting fraud often leads to damaging consequences to the company and those within the company.

There have been numerous accounting fraud scandals occurring in recent decades within major corporations. When a company's fraudulent financial reporting is investigated and discovered, the consequences are ultimately detrimental to the company. Many companies that were once successful and worth millions, even billions of dollars end up declaring bankruptcy, and the executives of these corporations sentenced to time in prison. Some companies are able to recover from the actions of fraudsters, by means of investigation, restatements of falsely reported financial statements, and/or accurate financial reporting. However, if the company is "too far gone," then bankruptcy could be the only outcome. An example of a profitable company that was able to remain in business following a large accounting fraud scandal is Waste Management, Inc.

BEFORE SARBANES-OXLEY:
WASTE MANAGEMENT, INC.

In 1998, USA Waste Services, Inc. of Houston acquired the Chicago based company, Waste Management Inc. The companies formed Waste Management Inc. after the latter company's name was kept. The company is in the business of collecting, transferring, disposing of, and recycling waste, as well as providing resource recovery and hazardous waste services (*Waste Management, Inc.)*. Currently, Waste Management serves over twenty million customers within the United States and Canada, providing new, comprehensive environmental solutions. The company has the largest network of recycling facilities, transfer stations, and landfills in the industry, in order to provide their services to customers within different business sectors and industries. The company is devoted to managing twenty million tons of recyclable material each year, while developing new waste solutions in order to assist in the achievement of "going green" (WasteManagement.com). From an outsider's perspective, Waste Management exhibits a sophisticated and prosperous business. However, although the company is flourishing and leading its industry, Waste Management experienced a multitude of hardships that threatened the survival of the company, when an accounting fraud scandal surfaced and was investigated in the late 1990s.

On March 26, 2002, the U.S. Securities and Exchange Commission (SEC) filed a suit against the founder of Waste Management, Inc. along with five other top officers of the company. The company was charged with orchestrating financial fraud for over five years, by falsifying and misrepresenting the financial results of the company between the years of 1992 and 1997 (SEC.gov). When a new CEO joined Waste Management, Inc. in 1997, he ordered a review of the company's books and accounting policies. While reviewing the company's books, the evidence of the accounting fraud perpetrated was apparent. This sparked an SEC investigation, and required Waste Management to restate their financial statements to accurately represent the company's actual financial standing. This restatement exposed that the founder and certain top executives had overstated the company's pre-tax income by roughly $1.7 billion. At the time of the restatement and investigation, this was the largest restatement of financial statements in corporate history (SEC.gov).

The SEC investigation named six Waste Management officials responsible for orchestrating the accounting fraud scandal: Dean Buntrock, founder, chairman of the board, and CEO; Philip Rooney, president and chief operating officer, director, and CEO for a short period of time; James Keonig, executive vice president and CFO; Thomas Hau, vice president, corporate controller and chief accounting officer; Herbert Getz, senior vice president, general counsel, and secretary; and Bruce Tobecksen, vice president of finance. The reason for the perpetration of fraud, according to Thomas Newkirk, associate director of the SEC's Division of Enforcement, "was driven by greed and a desire to retain their [the six men] corporate positions and status in the business and social communities" (SEC.gov). In order for these executives to succeed in their efforts in misrepresenting the company's financial standing, they all played a significant role in the fraud scandal, as well as conducting multiple practices to "cook the books" for a period between 1992 and 1997. Buntrock was reported to have set earnings targets, and the executives altered the financial results of the company to meet these earnings targets. However, since the company's actual revenues were not growing at fast enough rates to support these targets, the company's expenses were manipulated in order to increase the company's earnings.

The significant manipulations in expenses were related to fixed assets. The company significantly decreased the depreciation expenses on their garbage trucks, by extending useful lives and changing salvage values. The did not account for the decrease in value of their landfills, even though these landfills were constantly being filled with waste, and did not expense the costs of abandoned landfill development projects, that were unsuccessful. They also improperly capitalized certain expenses that should not have been capitalized (SEC.gov). By following these "accounting practices," In summary, Waste Management's executives were able to manipulate the company's expenses in order to reach the earnings targets set while preparing the annual budget. After comparing actual financial results to those they set in their budget, the executives used these "top-level adjustments," to ensure that their financial results represented the results of their earnings targets. This routine, to mask the actual performance of the company continued for years. They also used schemes referred to as netting and geography to achieve their fraudulent numbers, while avoiding skepticism from the public. The netting tactic allowed them to eliminate almost $500 million in operating expenses from the financial statements, by "offsetting them against unrelated one-time gains on the sale or exchange of assets." The geography scheme was used to move millions of dollars between line items on the financials in order to manipulate and control the way in which the executives wished to show the statements (SEC.gov).

Not only were the executives involved in this accounting fraud scandal, but the company's auditor, Arthur Andersen also played a key role. Unqualified or "clean" audit reports of Waste Management's false financial statements were issued by Andersen. After capping Andersen's fees, Waste Management informed the auditor that "special work" could be done to earn additional fees. Andersen would identify the false financial reporting by Waste Management, and present them with proposed adjusting journal entries in order to correct the financial statement "errors." Rather than following through with the proposed adjusting journal entries, the company entered into an agreement with Andersen to write off the errors within the financial statements, by means of improper accounting policies. However, the company did not follow through with the agreement, as this would prevent them from achieving their earnings targets (SEC.gov).

After five years of fraudulent financial reporting, Waste Management was investigated by the SEC, and as a result restated their financials for the fraud years. The suit filed by the SEC was settled in August of 2005. The six officers and executives were charged with committing a massive fraud, lasting over five years. Four of the six men (Buntrock, Rooney, Getz, and Hau) were barred permanently from acting as a director or officer of any publicly traded company. They were also required to pay a total of $30,869,054, a combination of disgorgement, prejudgment interest, and civil penalties. Buntrock was responsible for paying a total of $19,447,670; Rooney, a total of $8,692,738; Hau, a total of $1,578,890; and Getz, a total of $1,149,756. The other two men involved, Keonig and Tobecksen, had their final judgements entered on different occasions than the other four men (SEC.gov). Tobecksen's hearing was settled in September of 2004. He was barred from serving as a director or officer of a public company, and was required to pay $689,159 in disgorgement and prejudgment interest, as well as $120,000 in civil penalty. Keonig's final judgement was announced on December 21, 2007. Similar to the other five executives, Keonig was barred from acting as a director or officer of a public company, and was required to pay over $4 million in disgorgement, prejudgment interest, and civil penalties (SEC.gov).

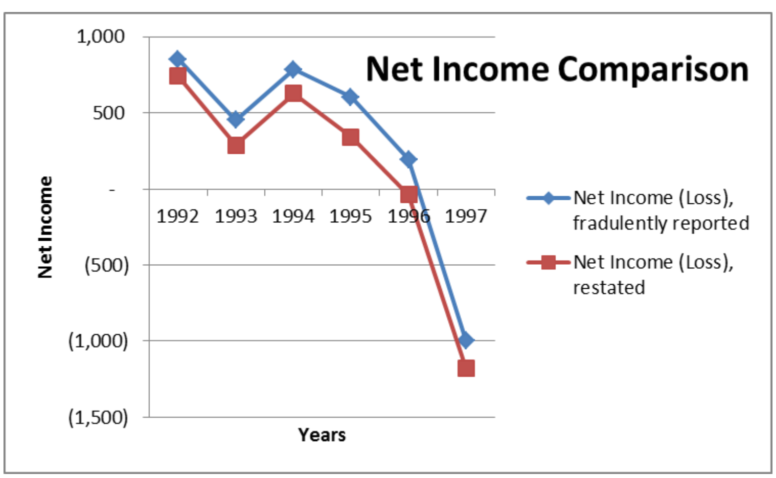
Arthur Andersen LLP, one of the Big Five accounting firms at the time, was also charged with a suit by the Securities and Exchange Commission. The firm was fined over $7 million for their part in the fraudulent financial reporting of Waste Management, Inc. Three partners of the firm were fined in relation to their roles in the perpetrated fraud. They agreed to pay their share of the fine and were barred from public accounting for a period of one to five years (Schroeder 1-5). The reason for Arthur Andersen's role in the fraudulent reporting stems from the relationship they had with Waste Management. They had been auditing their financial statements since the inception of the company, which "helps to explain the pressures that exist on partners to bend to the will of management" (Schroeder 11-12).

While analyzing the reports of Waste Management's fraudulent financial reporting, the fraudulent tactics used to avoid expenses are apparent. According to the U.S. Government Accountability Office, the restatement of financials for each of the years from 1992 to 1997 resulted in an overstatement of net income between $110 million and $264 million. Table 1 and Graph 1, below, illustrate the comparison of the falsely reported net income to the restated net income during the years of fraudulent financial reporting (gao.gov).

Table 1. Dollars in millions

Years	1992	1993	1994	1995	1996	1997	Total
Net Income (Loss), fradulently reported	850	453	784	604	192	(995)	1,888
Net Income (Loss), restated	740	289	628	340	(39)	(1,176)	782
Change	**110**	**164**	**156**	**264**	**231**	**181**	**1,106**

Graph 1.



Although, Waste Management, Inc., with the help of auditor, Arthur Andersen, was investigated, charged with a suit, and required to restate their financial statements, the company was able to continue operations. Today, the company is still serving their clients and the public with waste services such as recycling and disposals. Although they suffered consequences due to their five year period of fraudulent reporting, the company was lucky enough to recover from their losses and charges filed against them.

BEFORE SARBANES-OXLEY:
ENRON CORPORATION

In July of 1985, Houston Natural Gas Company merged with InterNorth Incorporated to form a gas pipeline company known as Enron Corporation. With Kenneth Lay as chairman and CEO, Enron became the largest natural gas merchant in North America, and reached number seven on the Fortune 500 list by the year 2000 (*CNN Money*). After years of success and prosperous business, Enron dove into what would be one of the most well-known accounting fraud scandals of our time.

In August of 2001, vice president, Sherron Watkins sent Kenneth Lay a memo regarding accounting issues, and that the company was at risk of developing numerous accounting scandals, due to these issues (*CNN Money*). Following this memo, Lay encouraged Enron employees to purchase stock because the company value was to increase astronomically. However, it is now known that this was not the case, and that the value of the stock would lose its value very shortly. Just a month later, Enron announced a loss in their third quarter, of $618 million; leading to an investigation by the SEC (*CNN*). It was discovered that Enron's auditor, Arthur Andersen (the same auditor involved in the Waste Management investigation) shredded Enron documents when the SEC investigation was ordered (*CNN Money*). This investigation resulted in the termination of a merger between Enron and Dynegy, Inc., another energy company, by Dynegy, and the filing for Chapter 11 bankruptcy by Enron in December of 2001. This would become the largest bankruptcy in United States history at the time. In the following month, in January of 2002, a criminal investigation was opened to investigate the collapse of Enron Corporation (*CNN*). Immediately following the start of the Enron investigation, the New York Stock Exchange (NYSE) suspended all trading of Enron shares after it was determined that Enron's securities were no longer appropriate and suitable for trading on the NYSE. Enron's shares had dropped significantly, leaving the value of the shares at barely one dollar (Ceron 1). Not only did Enron's collapse and bankruptcy result in a suspension of trading, "the NYSE moved to delist Enron after the company's stock traded below the critical level of $1 for 30 consecutive days, placing it in violation of the Big Board's listing standards" (Ceron 1). This suspension and delisting on the NYSE was ultimately detrimental to Enron's reputation as a prospering business and Fortune 500 company. Enron's partnership with Arthur Andersen ended due to their involvement in shredding documents that would be helpful in the SEC's investigation. Just shy of a week later, Kenneth Lay resigned as chairman and CEO of Enron, and weeks later, resigned from the board of directors (*CNN*).

In February of 2002, testimonials began, and many Enron executives invoked their Fifth Amendment right, while Sherron Watkins testified before the House of Representatives. By June of 2002, Arthur Andersen was found guilty of obstructing justice in the initial SEC investigation (*CNN*). In September, the firm surrendered their license to practice as Certified Public Accountants (CPAs), and thus lost their reputation as a Big Five accounting firm ("Andersen Surrenders Licenses"). In the following months, Enron executives and employees were charged and pleaded guilty to numerous charges and types of fraud. Chief Financial

Officer (CFO) Andrew Fastow and his wife Lea Fastow were among those who were charged with assisting with the company's financial scandals. They both later made guilty pleas in order to reduce their prison sentence. Richard Causey, another top executive of Enron, pleaded not guilty to five counts of securities fraud, as well as one count of conspiracy to commit fraud (*CNN*). He also later changed his plea to guilty. Jeffrey Skilling, who for a short time held the position of Enron's CEO, pleaded not guilty to fraud and conspiracy charges. Kenneth Lay was indicted on eleven counts, including security and wire fraud, bank fraud, and making false statements, which he plead not guilty to (*CNN*).

By the year 2006, the court decisions and sentencings for Enron's guilty executives and employees were delivered. Causey was sentenced to only five and a half years after changing his original plea. Fastow was sentenced to six years, also as a result of his plea deal. On the other hand, Skilling and Lay were both found guilty in the Enron case. However, in July of 2006, just over one month after the guilty verdicts were read, Lay died of a heart attack, and therefore served no prison time. Skilling was sentenced to twenty four years in prison. However, after years of appeal attempts, Skilling's sentence was reduced to roughly fifteen years, after he agreed to pay $42 million to the victims of the Enron fraud scandal (*CNN*).

Aside from the fates of Enron's executives and employees, the ability to commit these acts of fraud and deception was ultimately the largest question and concern of the SEC. Specifically, how the corporation was able to commit these injurious actions and the ability to do so for so long was most important. In order to accomplish this, Enron's top executives used mark-to-market accounting. Mark-to-market accounting is used to measure the fair value, or estimated value of specific accounts (Seabury 1). This type of accounting is used, and works well in the trading of securities, but it does not necessarily work well for all types of businesses.

For instance, if the estimated value of an asset does not accurately represent the true value of an asset, complications arise. In terms of Enron, the company would build some type of asset, e.g. equipment, then immediately record revenue and profit from the asset, even though the company did not generate any revenue from it (Seabury 2). On the other hand, if a loss was generated due to the specific asset, instead of reporting the loss, Enron would simply move the asset to an "off-the-books corporation" so that the loss incurred would go unreported, and the company's financial statements would appear as if no loss was ever incurred. This false reporting leads to false financial information given to shareholders and investors, who are important to the company (Seabury 2). As a result of the mark-to-market accounting "strategy," other schemes arose in order to continue making Enron look more profitable than it actually was.

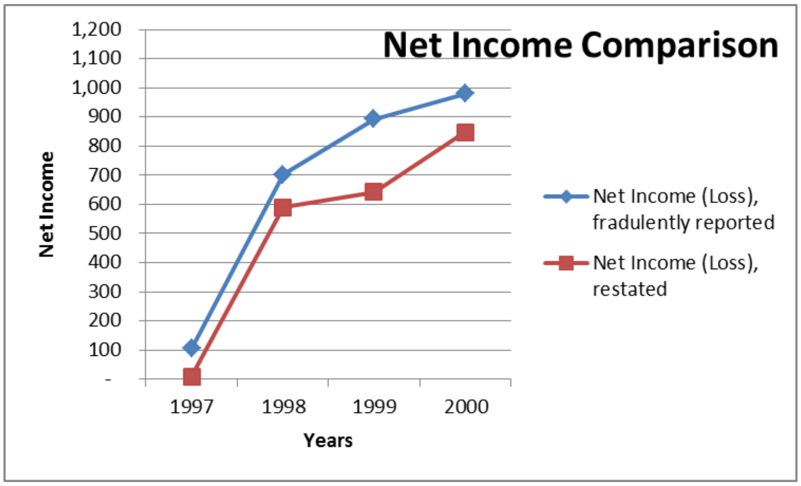
CFO, Andrew Fastow created a technique to ensure that Enron would appear to be in great financial shape, even though its subsidiaries were losing money. In order to pull this off, special purpose entities were used (Seabury 4). Special purpose entities are used to access capital and to avoid risk. This allows a company to increase its leverage and return on assets without having to report the debt on the balance sheet. The company contributes the assets and debt to the special purpose entity in exchange for interest. The special purpose entity then borrows money to purchase assets without the debt or assets on the financial statements. However, in Enron's case, thousands of special purpose entities were used so that Enron could hide the assets that were not generating income, and keep them off of their books. The company would then issue shares of common stock to shareholders to compensate for the losses, which would soon become worthless (Thomas 17-18). The use of these transactions required disclosures in the financial statements. In order to disclose the company's transactions without ousting the company's schemes, the footnotes were very confusing to interpret. A financial analyst was quoted while commenting on the footnotes in Enron's financial statements, stating, "The notes just don't make sense, and we read notes for a living" (Thomas 19). This type of skepticism would lead to the public's distrust in the company, and later result in losses that sparked the SEC investigation.

As a result of the schemes and tactics that Enron Corporation used to attempt to continue the prospering perception of the company's operations, Enron's financial statements were falsely reported, executives were imprisoned, and the corporation went bankrupt. During and after the SEC investigation, Enron would be required to restate their financial statements. While analyzing Enron's financial statements, years after the accounting fraud scandal had been investigated and closed, it is clear that elements of the financial statements do not seem to be accurately reported. According to Enron's income statement for the years ended December 31 of 1998, 1999, and 2000 (See Appendix I.), Enron's revenues increased 28% from 1998 to 1999, then 151% from 1999 to 2000. This amount of revenue increase is "unprecedented in any industry, let alone the staid energy industry that normally views even a two of three percent a year growth as a decent achievement" (Dharan 100). Table 2 and Graph 2, below, illustrate the comparison of the falsely reported net income to the restated net income during the years of fraudulent reporting (gao.gov).

Table 2. Dollars in millions

Years	**1997**	**1998**	**1999**	**2000**	**Total**
Net Income (Loss), fradulently reported	105	703	893	979	2,680
Net Income (Loss), restated	9	590	643	847	2,089
Change	**96**	**113**	**250**	**132**	**591**

Graph 2.



Following the investigation and bankruptcy of Enron, the Securities and Exchange Commission implemented an Act that would attempt to prevent any further Enron-type accounting fraud scandals from occurring.

THE SARBANES-OXLEY ACT OF 2002

This act is known as the Sarbanes-Oxley Act of 2002. The act was signed into law on July 30, 2002 by former President George W. Bush, after an almost unanimous vote by the Senate and House of Representatives. The Senate voted 99-0 in favor, and the House voted 432-3 in favor of the act (AdvisoryHQ). In order to combat the corporate fraud that put shareholders and investors at risk, and to verify that the financial statements and financial standing of publicly traded companies were accurate, this act was placed into law. The Sarbanes-Oxley Act was developed and named after Paul Sarbanes, a democratic Maryland Senator, and Michael Garver Oxley, a republican Ohio Congressman (AdvisoryHQ). This Act, also referred to as SOX, authorized various reforms to improve corporate responsibility and financial disclosures, and reduced the amount of accounting fraud scandals that occur. SOX also implemented the Public

Company Accounting Oversight Board, or PCAOB, to oversee all activities and transactions within the auditing business, and to set the standards and rules for audit reports (SEC.gov).

The Sarbanes-Oxley Act is comprised of eleven titles, which include various sections, which organize the act accordingly. Some are more well-known and “useful” than others, but all titles collaboratively created the Sarbanes-Oxley Act. Title I of SOX is Public Company Accounting Oversight Board (PCAOB). This title, and its sections, created the PCAOB, which is a non-governmental entity that oversees the auditing of publicly traded companies. By overseeing the audits, shareholders and investors are protected from fraudulent financial reporting occurring within their company (ies). Title II of SOX is called Auditor Independence. The title was implemented to address aspects of an auditor’s relationship with the company and executives that it is auditing. Title II also requires that leading partners in auditing firms must be rotated, in order to avoid any unclear relationships that may develop with an auditor that becomes too close to a specific client. Title III, Corporate Responsibility, was included in SOX to govern the procedures that audit committees practice to review, certify, and sign off on reports. This title also requires that CEOs, CFOs, and company lawyers are attentive and knowledgeable of company audits, practices, and internal controls. Title IV, entitled Enhanced Financial Disclosures, introduces the procedures taken for types of disclosures within the financial statements, under GAAP. In Title V, named Analyst Conflicts of Interest, the objective is to minimize conflicts of interest between financial analysts, brokers, and bankers. The title includes sections and subsections including one that prohibits any banker or broker from retaliating against any financial analyst who publishes any reports that deem unfavorable about them. Title VI of SOX is Commission Resources and Authority. This title serves as a resource to the SEC, as it allocates millions of dollars to expand their authority. With the implementation of SOX, the SEC budget was raised in order to hire more employees, so that auditors and auditing practices are being monitored. Under Title VII, or Studies and Reports, regulatory personal are granted the power to conduct research, studies, and investigations on securities laws violators, as well as past accounting fraud scandals. It also grants the power to study the overall audit industry and credit rating agencies. Title VIII, Corporate and Criminal Fraud Accountability, is an aspect of SOX that implements the repercussions of accounting fraud. The title states that any manipulation or destruction of documents, or false documentation is a felony. It also states that any impeding federal investigation is classified as a crime, punishable in the form of fine and/or prison time. Title VIII requires the retaining of all audit records for at least five years, and provides protection for whistleblowers that may be caught between accounting fraud scandals. Title IX, White-Collar Crime Penalty Enhancements was included in SOX so that all financial reports accurately represent the company's financial standing, or status. In order to achieve this, the title increases liability on company CEOs and CFOs to ensure the accurate information. If these top executives and officers are found negligible of certifying accurate information, jail time up to twenty years, millions of dollars in fines, and banning of holding executive office are the consequences. Title X of SOX, named Corporate Tax Returns, is a simple title, as it focuses solely on one aspect: corporate tax returns. This title requires CEOs to sign all federal income tax returns, so that they are aware of any misleading or inaccurate information that may be reported. The final title of the Sarbanes-Oxley Act, Title XI called Corporate Fraud and Accountability, provides additional information to Title VIII. This act provides further information into the penalties of corporate officers and employees. The title states that the SEC is authorized to freeze any payments to violators of any rules during investigation of the charges (AdvisoryHQ). These eleven titles of SOX are implemented in order to organize the Act into sections and subsections that clearly illustrate the rules and regulations of the Sarbanes-Oxley Act.

COMPARISON/CONTRAST
WASTE MANAGEMENT, INC. /ENRON CORPORATION

The accounting fraud that took place in the companies of Waste Management, Inc. and Enron Corporation share similar behaviors as well as factors that made each scandal their own. The fraud perpetrated by each company resulted in an SEC investigation and suit filed in the early 2000s, which led to the restatement of financial statements for each company. Each company scandal was the result of fraudulent financial reporting conducted by a small group of top level executives. In the case of Waste Management's scandal, the top executives were charged with a fine, and some permanently barred from serving as top executives, officers, or directors. On the other hand, in Enron's case, top executives faced this similar fate, along with years of imprisonment after being criminally charged with committing fraud. An alarming similarity is the auditor that was involved and investigated in both fraud cases. Arthur Andersen was charged and fined for their role in the accounting fraud within Waste Management. However, after being investigated for a second time, in the case of Enron's fraudulent financial reporting, Arthur Andersen suffered a stricter fate. The audit firm was charged with obstructing justice, and later surrendered their CPA license as a Big Five firm. In terms of the tactics and strategies used to commit these actions, the companies differed. Waste Management focused their fraudulent accounting on earnings targets, which led to their manipulation of expenses, like depreciation. Enron's fraudulent reporting was focused on recording revenues from assets that had not generated those revenues yet. A major difference in the two companies is the outcome of the companies themselves. Waste Management was fortunate enough not to declare bankruptcy, and is still conducting operations currently. Enron did not achieve the same outcome. Rather, Enron declared bankruptcy and ceased operations.

AFTER SARBANES-OXLEY:
AMERICAN INTERNATIONAL GROUP, INC.

American International Group is an insurance agency founded in 1919. Its founder, Cornelius Vander Starr was an American who first started the company in Shanghai, China as American Asiatic Underwriters (AAU). In 1926, the first U.S. office was opened in New York City, as American International Underwriters (AIU). In 1939, this location became the company's headquarters. Years later, in 1967, after opening offices across the globe, American International Group (AIG) was incorporated in Delaware (aig.com). Today, AIG provides insurance coverage for individuals as well as companies, while working to pinpoint and prevent risks from becoming more than just that. The company services ninety million clients in over one hundred countries across the world (aig.com). However, American International Group, Inc. faced a multitude of accounting fraud scandal investigations by the SEC in the 2000s.

In 2005, after an SEC investigation, potentially sparked by a whistleblower, American International Group, Inc. admitted to improper accounting practices. The company confessed that "some transactions appear to have been structured for the sole or primary purpose of accomplishing a desired accounting result" (McDonald 2). According to an SEC report released on February 9, 2006, after the completion of the fraud investigation, "the Commission (SEC) alleges that from at least 2000 until 2005, AIG materially falsified its financial statements through a variety of sham transactions and entities whose purpose was to paint a falsely rosy picture of AIG's financial results to analysts and investors" (SEC.gov). Luckily, AIG's SEC investigation was noncriminal, and therefore concluded with a settlement. However, CEO

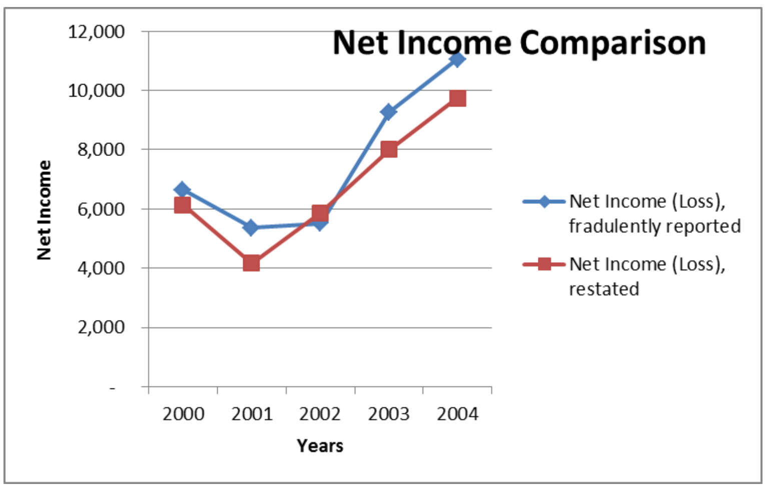
Maurice R. "Hank" Greenberg stepped down following the investigation after the courts "attributed the misconduct at AIG directly to Mr. Greenberg and alleged that he directed others at AIG to develop and implement the schemes underlying various misleading transactions" (gao.gov). The SEC charged AIG with committing securities fraud, and consequently resulted in AIG paying $800 million to resolve claims related to false reporting (SEC.gov).

While the SEC was conducting their investigation of AIG's accounting practices, evidence suggested that AIG had previously entered into multiple insurance transactions that were designed to improve their financial results. In late 2000 and early 2001, AIG and General Re Corporation entered into transactions that resulted in the reporting of $500 million of false loss reserves on AIG's balance sheet. This transaction transpired so that AIG could reduce criticism of a previous reduction of loss reserves. A financial analyst was quoted stating, "One concern over the past several quarters has been reserve growth, which has been minimal or even has declined in certain quarters. There has been concern that AIG is releasing reserves to make its numbers." This quote, among others from other analysts sparked concern for AIG, and thus, fueled their rational behind their fraudulent transactions and reporting. Another allegation stated that AIG also entered into a fraudulent transaction with Capco Reinsurance Company, Ltd. This transaction "allowed" AIG to disguise underwriting losses of $200 million as capital/investment losses, in order to improve the appearance of AIG's financial standing (SEC.gov). AIG's various transactions were improperly reported within the financial statements, resulting in overstatements of net income. As stated in the restatement report maintained in the Government Accountability Office, "AIG had accounted for various reinsurance transactions and associated cash flows as either revenues or expenses when the transactions involved insufficient transfer of insurance risk to the assuming reinsurer. When there is insufficient risk transfer, such cash flows are accounted for as either deposit assets or liabilities" (gao.gov). However, AIG reported these transactions as revenue and expenses instead. Table 3 and Graph 3, below, illustrate the comparison of the falsely reported net income to the restated net income (gao.gov).

Table 3. Dollars in millions

Years	2000	2001	2002	2003	2004	Total
Net Income (Loss), fradulently reported	6,639	5,363	5,519	9,274	11,048	37,843
Net Income (Loss), restated	6,141	4,172	5,866	8,009	9,731	33,919
Change	**498**	**1,191**	**(347)**	**1,265**	**1,317**	**3,924**

Graph 3.



Although the accounting fraud scandal involving American International Group, Inc. occurred following the implementation of the Sarbanes-Oxley Act, the accounting fraud still occurred. This, in part, is a result of the false reporting beginning before the Act, then continuing shortly after it was signed into law. Though the company was charged with securities fraud and required to restate their financials, AIG's case seems to be on a much smaller scale than those of Waste Management and Enron. AIG was able to settle their case, and remain in operation (similar to Waste Management). However, another company scandal following American International's, years after SOX was implemented and practiced, suffered a worse fate.

AFTER SARBANES-OXLEY:
LEHMAN BROTHERS HOLDINGS, INC.

This company was known as Lehman Brothers, Inc. Founded by a German immigrant, along with his brothers in 1850, Lehman Brothers was a one of the largest, most prosperous, and powerful investment banks in the United States. However, years after the company's bankruptcy, its reputation is branded as being connected to the largest and worst financial crisis since The Great Depression, and being one of the largest bankruptcies in history (Moody 1).

Deviating from the clear-cut cases of Waste Management, Enron, and American International Group, the bankruptcy and accounting scandal of Lehman Brothers is not as straightforward and understandable. The key aspect of the SEC investigation of Lehman Brothers was focused on an accounting practice, adopted and named by Lehman Brothers as Repo 105. A repo, or repurchase agreement, is an agreement between two parties, where one party transfers an asset to the other as a type of collateral for borrowing cash for a short-term. The party agrees to pay back the cash with interest, while repossessing their asset (Moody 3). While these transactions are accounting practices, Lehman Brothers found a loophole and a way to decrease the risk presented on the company's balance sheet. This loophole was created and exploited in terms of how these repurchase agreements were recorded. The Accounting Standards Board is responsible for establishing the guidance for the proper accounting treatment of repurchase transactions. They are typically accounted for as debt, unless total control of the asset is surrendered, in which case it would be accounted for as a sale. Lehman Brothers reported their Repo 105 transactions as sales, instead of debt, which they should have done. By accounting for these transactions as sales, the company reduced their leverage by removing roughly $50 billion of assets off their balance sheet, and using the cash collections as a way to pay off some of their liabilities. The company failed to disclose that they were accounting for these transactions as sales, and instead disclosed that they were financing, which is considered false financial reporting (Schapiro 26-27).

The Lehman Brothers' auditors were those at Ernst & Young. In the midst of investigation, a spokesman for Ernst & Young stated "Our last audit of the company was for the fiscal year ending November 30, 2007. Our opinion indicated that Lehman's financial statements for that year were fairly presented in accordance with Generally Accepted Accounting Principles (GAAP), and we remain of that view" (Merced 14). Due to the ambiguity of whether or not these transactions were actually illegal, the SEC made the decision not to sue anyone or press criminal charges. The SEC's decision also stemmed from the fact that the Lehman employees may not have been fully aware of the Repo 105 transactions, and therefore decided it would be difficult to prove that the intention to commit fraud was apparent. The Commission also claimed that since Lehman Brothers' leverage ratio had a decreasing trend, the Repo 105 transactions would not be considered material to investors anyway (Levine 10). Lehman Brothers was not required to restate their financial statements in the years surrounding the investigation and bankruptcy.

On September 15, 2008, Lehman Brothers filed for bankruptcy, which was the largest in history, even including the bankruptcy of Enron. A combination of their risky accounting practices, namely the controversial scandal involving Repo 105 and the U.S. financial crisis are to blame for the bankruptcy of the once prosperous company.

COMPARISON/CONTRAST
AMERICAN INTERNATIONAL GROUP, INC. /
LEHMAN BROTHERS HOLDINGS, INC.

The accounting fraud scandals perpetrated within American International Group, Inc. and Lehman Brothers Holdings, Inc. were very different. Compared to the fraud scandals of Waste Management and Enron, before the implementation of the Sarbanes-Oxley Act, these more recent cases seem to be smaller scale cases. This is a direct result of the implementation of SOX, which calls for more monitoring and control of the auditing and accounting business. In terms of their similarities, AIG and Lehman Brothers both perpetrated fraud in order to achieve a desired accounting result, due to previous criticisms and financial standing. Both companies executed sham, or phony, transactions in order to achieve their desired results. However, this is where their similarities end. Unlike AIG, the SEC did not press charges or sue anyone in relation to the accounting scandal that took place within Lehman Brothers. The differences in the clarity of the case, due to the types of accounting practices performed, was a direct cause in this decision. Since Lehman Brothers had gone bankrupt, it seems that the SEC simply did not interfere, and instead let Lehman Brothers suffer the fate of the financial crisis and the consequences of their actions. Unlike the other three accounting fraud scandals analyzed, Lehman Brothers was not required to restate their financial statements, so the differences in reported financials versus restated financials is not available.

IMPACT OF ACT

Since the implementation of the Sarbanes-Oxley Act in 2002, there have been questions of whether or not the act has been more beneficial than costly, and if the act has actually proven successful. One key factor in these inquiries is the occurrence of accounting fraud after the enactment of SOX. If the Sarbanes-Oxley Act was implemented to combat the accounting fraud occurring within these large, publicly traded companies, then why is accounting fraud still occurring?

According to an opinion article written in 2012 by Michael Peregrine, a partner at the law firm, McDermott Will & Emery, Sarbanes-Oxley has not failed at all, but rather, has made a huge corporate difference. It has reformed corporate responsibility and fiduciary duties to the company and shareholders. After the implementation of the act, corporate governance and expectations increased for executives and officers of companies. This, in turn, made the shareholders and general public more aware of corporate responsibility, which resulted in more attentiveness being paid to operations and controls of companies. Although this opinion does not directly mention the occurrence of accounting fraud, it clearly states that SOX has achieved an important aspect of corporate governance and responsibility, and improved from where it once was (Peregrine 1-3).

Another opinion article published in The New York Times in 2012 was written by Kayla Gillan, a former deputy chief of staff to the Chairman of the SEC. She also believes that SOX has been a beneficial and successful new law. Similar to the statements made by Peregrine, Gillian states that in the months after the act's passage, investor confidence quickly saw improvement. She also explained that although SOX increased the cost of participating in capital markets, most investors have claimed that these costs are outweighed by the increase in confidence they have for corporate financial reporting. Gillian also explained that although the act was implemented to prevent accounting fraud, no law has the ability to abolish it altogether. However, SOX has prevented certain instances of fraud from occurring. Now that Sarbanes-Oxley is in effect, internal controls are more effective; auditors comply with stronger standards;

auditors are more competent and engaged in auditing and financial reporting; and the SEC spends more resources in reviewing and insuring that information provided to the market is accurate and faithfully represented. Her opinion states that enhancing investor protection is what SOX was designed and implemented to do, and therefore has accomplished this (Gillian 2-4).

On the other hand, in a 2015 interview with billionaire investor Mark Cuban, the praises of Sarbanes-Oxley come to a halt. The interview was conducted by the Wall Street Journal Financial Editor, and focused on income inequality and Cuban's opinion of the SEC and their relationship to startup companies. During the interview, Cuban states that the SEC is making it harder for companies to become public due to the increased costs associated with new regulation. He voices his opinion of SOX when he states, "If you look at what's happened over the past fifteen years, we get overregulation because the SEC screwed something up. They didn't catch fraud at Enron or WorldCom, so we get Sarbanes-Oxley. If the SEC isn't paying attention to what's going on, we're going to have more disasters. Then the way this country reacts to disasters is to create even more regulation, right?" (Berman 8-10). Cuban's criticisms of SOX stem from the fact that regulation has increased, and costs associated with becoming a publicly traded company have increased.

CONCLUSION

In all of the above opinion and interview articles, the critiques and appraisals of SOX are all analyses that examine more than the just the occurrence of accounting fraud. It seems that the benefits of the act such as increased corporate responsibility; the use of internal controls; and improved competence and engagement from CEOs, top executives, and auditors have outweighed the negatives of the act, including increased costs, regulations, and difficulty of becoming publicly traded. Although there have been accounting fraud scandals since the implementation of Sarbanes-Oxley, it seems that the act has diminished the rate at which these scandals occur. I think the question of why accounting fraud occurs will always be to manipulate and enhance the financial standing and appearance of a company, as well as to increase power and income of top executives. Even though the Sarbanes-Oxley Act was implemented to combat accounting fraud, and increase regulations and oversight by the SEC, I believe that accounting fraud is almost too big to abolish, and that although, it can be significantly reduced, accounting fraud and scandals will remain a part of corporate America.

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Appendix I. Source: SEC.gov

ENRON CORP. AND SUBSIDIARIES
CONSOLIDATED INCOME STATEMENT

<CAPTION>

(In millions, except per share amounts)	Year ended December 31, 2000	1999	1998
<S>	<C>	<C>	<C>
Revenues			
Natural gas and other products	$ 50,500	$19,536	$13,276
Electricity	33,823	15,238	13,939
Metals	9,234	-	-
Other	7,232	5,338	4,045
Total revenues	100,789	40,112	31,260
Costs and Expenses			
Cost of gas, electricity, metals and other products	94,517	34,761	26,381
Operating expenses	3,184	3,045	2,473
Depreciation, depletion and amortization	855	870	827
Taxes, other than income taxes	280	193	201
Impairment of long-lived assets	-	441	-
Total costs and expenses	98,836	39,310	29,882
Operating Income	1,953	802	1,378
Other Income and Deductions			
Equity in earnings of unconsolidated equity affiliates	87	309	97
Gains on sales of non-merchant assets	146	541	56
Gain on the issuance of stock by TNPC, Inc.	121	-	-
Interest income	212	162	88
Other income, net	(37)	181	(37)
Income Before Interest, Minority			

Interests and Income Taxes	2,482	1,995	1,582
Interest and related charges, net	838	656	550
Dividends on company-obligated preferred securities of subsidiaries	77	76	77
Minority interests	154	135	77
Income tax expense	434	104	175
Net income before cumulative effect of accounting changes	979	1,024	703
Cumulative effect of accounting changes, net of tax	-	(131)	-
Net Income	979	893	703
Preferred stock dividends	83	66	17
Earnings on Common Stock	$ 896	$ 827	$ 686
Earnings Per Share of Common Stock			
Basic			
Before cumulative effect of accounting changes	$ 1.22	$ 1.36	$ 1.07
Cumulative effect of accounting changes	-	(0.19)	-
Basic earnings per share	$ 1.22	$ 1.17	$ 1.07
Diluted			
Before cumulative effect of accounting changes	$ 1.12	$ 1.27	$ 1.01
Cumulative effect of accounting changes	-	(0.17)	-
Diluted earnings per share	$ 1.12	$ 1.10	$ 1.01
Average Number of Common Shares Used in Computation			
Basic	736	705	642
Diluted	814	769	695