



CPA MUTUAL

Financial (mis)statements: Fabricating numbers continues

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You think Sarbanes-Oxley is going to cure the financial reporting mess highlighted by Enron, Adelphia, Tyco and others? That sending a few CEOs and CFOs (maybe even a spouse or two) to jail will bring sense to all the other misfeasors? Think again!

A recent detailed analysis of more than 120 companies in the S&P 500 – which comprise almost 40 percent of the index's market capitalization – revealed that fabricating numbers is still happening at an alarming rate. In a study conducted by RateFinancials Inc., it is estimated that one-third of these leading public companies file financial statements that do not accurately represent their true financial position.

A RateFinancials study found:

- 75 percent of companies used complex financing devices to shift long-term financial obligations off their balance sheet.
- 64 percent made unreasonable assumptions and forecasts when calculating future pension liabilities. Although many companies run large, long-term funding deficits within their pension plans, GAAP allows companies to post net positive pension assets.
- 28 percent used aggressive revenue recognition techniques.
- 47 percent of the financial statements reviewed were ranked “above average” or “acceptable.” 14 percent were rated “below average” and 1 percent were rated “poor.”

Keep this in mind as well: 67 percent of CFOs attending a 1998 *Business Week* Forum of CFOs said they had been asked by senior company executives to misrepresent corporate financial results. 67 percent!!!

I doubt this is just a Fortune 500 company issue. I'd be willing to bet that this may occur in companies whose future may be dependent upon positive operating results or certain loan covenants. Motivation for misstatements may also occur when compensation for highly paid CEOs or managers is tied to bottom-line performance.

As always, auditors must have some degree of professional skepticism. Just maybe now, as Chef Emeril likes to say, “We need to kick it up a notch!”