REUTERS

Governance important in corporate results-report

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Despite a spate of regulatory and accounting reforms, the quality of earnings reporting remains unacceptable and murky, according to a UBS report.

Even with the passage of tougher new governance requirements, a more active Securities and Exchange Commission and tougher accounting standards, the quality of earnings probably will not be acceptable until 2005, UBS analyst David Bianco said in the report released last week.

“Unfortunately, while some improvement has occurred, we think far more improvement remains needed to bring the quality of earnings back to acceptable and even historical levels,” he wrote.

In this year's report on the quality of earnings of companies that make up the Standard & Poor's 500 , Bianco ranked corporate governance as being as important as special charges, employee stock options and litigation.

Good governance practices may allow a company to reap benefits through lower borrowing costs, directors and officers insurance premiums, and litigation expenses, as well as fewer regulatory problems and lower cost of capital – all of which could help boost a stock price.

Using results from a September report compiled by GovernanceMetrics International, which rates companies by their governance policies and practices, Bianco said companies with the lowest-rated governance practices consistently had negative shareholder returns over 3-, 5-and 10-year periods.

Some of the highest ranked companies include Colgate-Palmolive Co. (CL.N), Pfizer Inc. (PFE.N), General Motors Corp. (GM.N), DuPont Co. (DD.N), and 3M Co. (MMM.N), according to GovernanceMetrics.

Among the lowest ranked companies are King Pharmaceuticals Inc. (KG.N), Qwest Communications International Inc. (Q.N), Westar Energy Inc. (WR.N) and Dynegy Inc. (DYN.N)

Dynegy Spokesman David Byford said that in the past year or so, the company has recruited nine new board members and has instituted new internal controls to bolster its governance.

Westar has instituted a slate of new measures since it replaced its management over the past year or so.

All of the company's board members, except its chief executive, are independent of the company, and it split the role of chairman and chief executive.

A representative from King Pharmaceuticals did not immediately return calls for comment. The company's chairman and CEO resigned last month. A Qwest representative said the board in February 2004 revised its guidelines on significant governance issues.

Corporate governance came to the forefront of investors' concerns following the scandals at Enron, WorldCom and other companies.

In another recent report, independent research firm RateFinancials said financial statements still fail to paint a clear picture of companies' conditions.

That report showed 75 percent of the 120 companies studied still use off-balance-sheet financing, an accounting practice that allowed Enron to keep some transactions from investors.

Additionally, a recent survey by CFO Magazine found that since 2001 about 20 percent of financial executives said they felt more pressure to use aggressive accounting measures to make results appear more favorable, and half said that they faced the same amount of pressure as they did three years ago.