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Boerner on Enron Fallout: "Crisis of Confidence"

***Editor's Note:** The continuing fallout from the Enron debacle—in terms of legislation, regulation and litigation—offers an opportunity for issue management practitioners to alert their companies to the tangible effects of good or poor attention to reputation. **Hank Boerner** shares his thoughts on the parameters and key players involved in the current "crisis of confidence."*

As issue managers, we know that signal detection is a critical skill for identifying, scoping, analyzing and monitoring issues, and quite necessary as we develop strategies for and act on critical issues of concern to our organizations. What went wrong at Enron in the signal detection process? How important are the lessons of the Enron crisis situation to us as individual corporate issue managers? (Especially if we are not involved in the financial reporting function?)

At a January corporate board level forum in New York City, the head of research for a major Wall Street house stated her views quite bluntly:

"We are facing a major crisis of confidence in this country. Everyone is or will be affected. This crisis atmosphere affects corporate management, members of boards, accountants, auditors, financial analysts, security regulators, rating agencies, and investors. This crisis is much bigger than just the Enron debacle. This is a crisis of confidence for the accounting profession, the auditing profession and especially for corporate management. Only 'the truth' can help us cure the problem.

"Many investors no longer believe any company's financial statements," she said. "They do believe what the financial media has to say; they do continue to believe what financial analysts report (their analysis and recommendations); but investors are rejecting wholesale what corporate managers are saying about their company's financial performance. That is not good...this is the worst [crisis of confidence in business] that I have seen in my career of 30 years..."

"Investors are rejecting wholesale what corporate managers are saying about their company's financial performance."

Market Performance Causes Further Uncertainty

The spreading "crisis of confidence" regarding investing has been created and further aggravated by a series of disappointing events, especially in the financial markets:

- The rapid 1999-2000 downturn in the feverish 1990s Bull Market
- The dramatic collapse of the NASDAQ bubble, with the composite index falling from over 5,000 to below 2,000
- The disappearance of New Economy companies (e.g., the dot-com companies)

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- The restatement of previous earnings by many large firms of both Old and New Economies
- The failure of experienced auditors to detect fraud at high profile companies
- The inadequate experience of some younger financial analysts who had not previously experienced serious market downturns and cannot cope with the changes taking place
- The ties of some financial analysts to their firm's investment banking arms
- The collapse of the share price and ultimate bankruptcy of Enron
- The inability of the regulatory framework to keep pace with state-of-the-art communications technologies that operate in real-time

"The over-arching issue is financial reporting in all its aspects."

News Velocity Adds Complexity

Perhaps among the most important points that we as corporate issue managers should consider as we monitor external events is the speed and increasing velocity with which rumors, news and advice now flow from experts and third parties of all types to the public-at-large. Thanks to CNBC, MSNBC, CNNfn, hundreds of Web sites, and on-line chat rooms, all types of information about publicly owned companies are transmitted instantly to individual and institutional investors. This information could be factually based or totally made up—doesn't matter. Much of the information will affect market behavior in some way.

Technology has changed the nature of financial communication and disclosure. The regulatory environment in which we operate is based on foundations established in the depths of the Great Depression—in 1933 and 1934. For example, the original investor protection legislation called for annual and quarterly reports to be filed (today's 10-K and 4-K); today, CNBC reporters want to know now what the CFO is predicting for next year's revenue results. The rules of the road on corporate financial reporting have become quite murky and byzantine for many in the corporate suite.

Accounting standards, Congressional legislation, Securities & Exchange Commission rules and regulations—all are not able to keep pace with the Internet, 24/7 cable television, 18-hour trading days (from Singapore around to San Francisco), instant news reports, Web conferencing, and other recent developments enabled by technology.

Lessons for Issue Managers

The important issue shapers swinging into action post-Enron will now need to be carefully monitored. The overarching issue is financial reporting in all its aspects: how a company identifies and reports its revenues, profits and per-share earnings; what the company does not report in its regulatory filings ("as reported," or GAAP results); reporting innovations such as pro-forma (or "what-if") reporting; the enormous pressure on senior managers and boards of directors to outdo the last quarter, and other factors.

Who are the important issue shapers?

- Members of Congress—Congressional committees/subcommittees
- The Financial Accounting Standards Board (FASB)
- The Securities & Exchange Commission (SEC)
- Individual state securities administrators.
- Debt & Credit Rating Agencies (Standard & Poors)
- Financial Analysts
- Money Managers (large institutional investors)
- Pension Fund regulators (U.S. Department of Labor)
- Pension Fund Trustees (especially public employee funds)
- The Accounting Profession (including auditors)

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- Shareholder Advocates
- Corporate Governance Activists
- The Media
- Corporate Management
- Boards of Directors

The combined media reach of these players is awesome. The grand sweep of issues to be examined and debated will be very broad. A clue as to where this may be going: Federal Reserve Chairman Alan Greenspan is referring directly to the lack of ethics that he sees among corporate managers and financial managers and makes pointed references to the root causes of stock market mania and the manipulation of financial results to meet investor demands or expectations. He sees the need to restore certain ethical standards within the corporate community and on Wall Street—companies need to do the right thing.

Surely, the protection and promulgation of "ethical standards" should be within the purview of the corporate issue manager...who, quite often, serves as the de facto keeper-of-the-conscience of the corporation.

What it Boils Down To: Trust

We would caution ourselves not to let the debate about seemingly arcane subjects—such as obscure rules in the accounting standards—cloud over the real issues at the heart of the debate: It is all about *trust*. Trust in corporate managers, trust in boards of directors, and trust in the complex corporate financial reporting process. Restoring faith and trust in the entire system of share-owning, and establishing or maintaining high levels of trust for senior corporate management and the board, should be one of the guiding principles of good issue management.

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