THE PENNSYLVANIA STATE UNIVERSITY
SCHREYER HONORS COLLEGE

DEPARTMENT OF ACCOUNTING

THE EFFECT OF ACCOUNTING FRAUDS ON THE CAREERS OF OUTSIDE DIRECTORS: THE ROLE OF DIRECTOR INDEPENDENCE

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Abstract

In this study, I examine the moderating effect of director independence on the association between the accounting frauds and the career outcomes of outside directors. I use a data set of all 38 previous outside directors of four prominent firms identified by the SEC as having committed financial statement fraud. My results show that reputation damage resulting from accounting frauds does have a negative impact on outside directors’ future directorship job market prospect, but the negative effect is reduced for independent outside directors. My results hold after controlling for a director’s past directorship experience. I also investigate whether frauds impact the current executive positions of the outside directors. Results indicate that independent outside directors are less likely to lose their executive roles in other firms.
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Introduction

This study analyzes outside director job markets empirically after their association in an accounting fraud of a publicly traded corporation. Are outside directors negatively impacted by an accounting fraud? David Yermack claims, “To date most studies of the market for outside directors have focused on directors’ accumulation of seats on additional boards, finding some evidence that fewer offers for new directorships occur for board members of firms that perform poorly.” (Yermack, 2003). The production of fraudulent financial statements is one indication of poorly performing firms. Therefore, fewer offers for directorships are a response to board members not fulfilling their duty.

However, little research about the independence of these outside directors has been examined. The level of independence contributes to the magnitude of reputation damage for a director in a scandal. Other research consistent with (Fich & Shivdasani, 2005) has indicated the effects on future directorships that come from reputation damage. I want to observe the consequences that reputation damage has on the job markets for outside directors in the future director labor market and their current executive positions in other firms.

Due to time and resource constraints, a study about the impact on the existing directorships of outside directors is not examined. There will be no coverage on the retaining or ousting of directors in other firms. However, this study is important because it will allow future investors and corporations to consider the significance of independence and reputation in their selection of future directors. In addition, current outside directors will become more aware of the consequences from reputation damage if they lack independence.

This paper investigates whether director independence helps moderate the negative impact of accounting frauds on outside directors’ future job market prospect.
including all 38 outside directors of Adelphia, WorldCom, Tyco, and Enron serving during the period of the fraud is examined. The 38 outside directors do not include those who passed away during their tenure on the board. I select the 38 directors by examining 10-K documents on the EDGAR System within the SEC website. Most 10-K documents selected for each firm are from 1997 to 2002, the time period when fraudulent financial activities occurred. In the 10-K, I determine whether the members of the board are inside or outside directors by checking if they hold executive positions. Directors that are not executive officers are initially determined to be outside directors. Some directors on the board are not executive officers but are other employees in the corporation. Therefore, a research on the background of each outside director will be conducted to determine if they are truly an outside director. Background information includes a history of the directors’ prior experience as an executive and director of other firms. Some of this information is included in the 10-K, while other descriptions of directors are found in the Schedule 14A in the EDGAR system.

After obtaining a list of outside directors, their independence will be determined through a process involving research on the Internet. Lack of information found in publications on the careers of these selected outside directors forces the use of the Internet. The amount of previous directorships and executive positions at other firms are recorded. In addition, I tracked the number of directors that acquired new seats on boards of other firms. To examine the impact of reputation damage on the current jobs of outside directors, I researched their tenure as an executive of another firm. Those outside directors that are no longer executives of corporations during the same year as the scandal are considered as impacted by the reputation damage.

Studying the independence of an outside director is important, because directors have a fiduciary duty to remain faithful to their investors. The fall of prominent corporations such as Adelphia, WorldCom, Tyco, and Enron caused immediate concerns about the effectiveness and competency of boards amongst all corporations. From an agency theory perspective, the presence
of independent non-executive directors on company boards, should help to reduce the notorious conflicts of interest between shareholders and company management” (Solomon, 2004). Outside directors were perceived to be essential to establishing reliable corporate governance. Shareholders trusted these outside directors because of their implicit minor financial interests.

Outside directors’ reputations for future job markets rely on their independence at the firms. I find evidence that the job markets of outside directors are impacted by the reputation damage they receive from association in an accounting scandal but the negative effect is smaller for independent outside directors. Based on data collected, 33% of independent outside directors were able to find new directorships. In contrast, only 10% of non-independent directors could obtain the same outcome. The results for the executive job market are similar. 100% of independent outside directors and only 50% of non-independent outside directors were able to retain their current executive positions.
Defining Board of Directors

Corporate governance is defined as the way policies are managed and enforced within a corporation. An important way governance is established is through a Board of Directors. The board determines the purpose of the company, agrees to the strategies that will achieve those goals, and lays down the values and policies that will guide management (Tricker, 2009). When the owners, outside shareholders, appoint a board of directors, they are seeking for a group of trustworthy people to represent their interests. The goal of a board is to ensure long-term growth for the corporation’s shareholders. In addition, stakeholders, including customers and employees, demand for sustained life of the company. Board members are expected to monitor the performance of the company in comparison to established goals, objectives, and policies. Other duties include close monitoring of Chief Executive Officer and remaining executive officers and providing any necessary feedback. If the CEO is not performing properly, then the board has authority to find a replacement. “A director is expected to spend the time and effort necessary to properly discharge such director’s responsibilities. Accordingly, a director is expected to attend meetings of the Board and committees of their affiliation.

Visibility and accountability are just some of the characteristics that shareholders and stakeholders desire in a board. Although duties may differ, each director in a board has equal responsibilities. However, not all boards engage in the same activities. Directors could be very involved in some corporations while in others they delegate work to the CEO and other management members. A board can also vary in size, depending on the allocation of inside and outside directors. Today, most major corporations in the United States have more outside directors than inside directors.
Defining Outside Directors

Inside directors include executive management and other members who are employed by the corporation. In contrast, outside directors are essentially non-executive members of the board that have no management responsibilities within the organization. During the 20th century, there was an emphasis placed on the amount of outside directors in a corporation. People believed that more outside directors would lead to greater independence. Peter Drucker claims, “The control of a large corporation is such a complex job and requires such constant attention that the outside board member, who has his own affairs to look after, can know very little about the business – too little on the whole to be useful as an outsider” (Drucker, 1993). Critics about outside directors claim that not all of them know how the business and industry functions. Some of the outside directors in companies were just attorneys that never had any experience in industries such as cable, energy, or telecommunications. However, these members were perceived to be important because inside directors possessed difficulty in remaining independent. The knowledge that inside directors have about operations could impair their judgment. Essentially, inside directors could monitor their own performance and approve any unwarranted actions.

Boards that include a combination of non-executive and executive directors are known as unitary boards. Today, a majority of public companies and not-for-profit companies have mostly non-executive directors. Outside investors desire visibility and accountability in their directors. Therefore it has created greater emphasis on the addition of outside directors. Many non-executive directors typically have authority to question the decisions of the executive directors. However, the lack of independence can impair this authority.
Defining Independence

Outside directors are broken down into two categories: dependent and independent. Some corporations include outside directors that had various interests with management. Unfortunately, the four accounting scandals that occurred in the millennium had about half of their outside directors who were not independent. Anil Shivdasani believes “an board is considered to be independent if 50% or more of directors are independent. We define directors to be independent if they are not current or former employees of the firm, and do not share any family or material business relation with the firm or its management.” (Fich & Shivdasani, 2005). Essentially, independence is considered as working with integrity. A director that receives extra compensation or perks for services provided would breach independence. In addition, directors that look out for their own interests instead of the shareholders would breach independence.

The reputation damage from association with an accounting fraud is suggested as a reason for a decrease in outside directors’ participation in new boards. Nell Minow claims a financial statement fraud, “severely impairs the personal credibility of the individuals involved” (Hopkins & Iwata, 2003). Independence is a factor that affects the reputation of a director. If a director was not independent during their time on the board of an accounting scandal, then their reputation is affected more negatively. Reputation damage also impacts the decisions of these former directors. Their decision not to pursue the director job market also contributes to the decline of these outside directors in other boards. One reason for this decision is to mitigate the reputation damage from a fraud.
Corporate Governance in America During the Millenium

Governance problems revealed themselves to citizens in America shortly after the burst of the technology bubble in 2000. During this time, the amount of companies involved and the magnitude of these scandals raised doubts about the visibility of the board. One of the problems with the corporate governance structure of publicly traded firms was the surprising lack of independent auditors. In addition, some of the outside directors in the audit committee that collaborated with the auditors were not independent. Each of the four corporations involved in fraud had a majority of non-executive directors, but not all of them were independent. The non-independent directors included those that had close relations with the CEO, employment with the company in the past, and other business interests. Those non-independent directors were liable and had to pay a significant portion of legal settlements.

Another problem was that some directors served on many other boards. For example, an outside director for a manufacturing firm was also on the board of pharmaceutical, automobile, and travel corporations. Besides the affiliation with many boards, the disparity in industries confirmed the doubts of the director’s knowledge. It is impossible to have twenty non-executive jobs and pretend that the job is done properly. (Tricker, 2009). Despite the lack of knowledge, the participation in many boards provided the directors with experience that other corporations find important. Thus, executives were able to find plenty of opportunities to serve on boards as outside directors. In the 2000s, John Mendelsohn served on the board of two significant frauds, Enron and Imclone. His negligence and incompetence of the industries were noted, but no significant damage affected his career because of his experience. In 2002, the government quickly responded to these problems and enacted the Sarbanes-Oxley Act. In response, only independent directors were allowed to serve on audit committees, shareholders had to approve the plans for stock options of the directors, and subsidized loans to any director were prohibited
Many of the directors had been serving on the boards of other corporations during their tenure in Adelphia, WorldCom, Tyco, or Enron. After their resignation, only a few outside directors resigned from the other boards they served. Former Enron directors; Robert Jaedicke and Wendy Gramm notably resigned from their other boards. It is assumed that the outside directors were able to keep their seats on previously elected boards because the corporations were pleased with their work. For example, Gordon Macklin still served on the board of five corporations. Hopkins writes, “An Overstock official said executives and Overstock's legal counsel discussed the reports and Macklin. They concluded they were pleased with his work as an Overstock director and gave him a vote of confidence” (Hopkins, Iwata).
The Sample

All observations are based on the information researched in the Appendix. An examination of all 38 outside directors from four prominent accounting frauds was performed. These directors were selected by observing the 10-K archive on the EDGAR System at the SEC website. Research was conducted on the Internet to find the correct corporation on the EDGAR System. For example, there were various companies titled Tyco with different states of incorporation. The EDGAR system on the SEC website displayed the filings for each year. Only the 10-K that related to the years during the scandals were considered. Within the 10-K; inside directors, executive officers and other employees were separated from the rest of the board. Further examination on the employment background of the directors found in the 10-K enabled the determination of outside directors. The information on the careers of the outside directors after the scandals is found through the various news articles on the Internet. Businessweek and Forbes provided the majority of information regarding future directorships and current executive positions of previous outside directors.
Findings

Impact on Future Directorship Job Market

Only 8 of 38 former outside directors examined were able to find new directorships in the job market. Fich and Shivdasani claim, “the presence of an outside director that serves on a board of another firm facing a financial fraud class action suit significantly raises the probability of a fraud class action suit. This suggests that directors that have been previously associated with allegations of financial fraud are more likely to confront similar allegations on other boards” (Fich & Shivdasani, 2005). Perhaps the reputation damage obtained by the fraud lowers the job market for outside directors. However, the independence of the director during the fraud can also impact their future director job market. Based on the data collected, Figure 1 provides evidence that independent directors associated in an accounting fraud are more likely to obtain future directorships. Out of all 38 outside directors, only 18 of them were independent. The 20 directors that breached independence had more difficulty. Independent outside directors had a 33% success in finding new director positions, while only 10% of non-independent found success in the same market. In addition, three of the four firms examined were composed of a board that was less than 50% independent.
Figure 1. Future Directorships Based on Independence

Fraud firms typically consist of significantly fewer independent outside directors than the average corporation (Dechow, Sloan, and Sweeney, 1996). However, those few independent outside directors have less reputation damage than the non-independent. “In an efficient director labor market, directors who perform their board functions effectively are likely to be rewarded with additional board appointments and benefits; those who perform poorly will be penalized by loss in their positions and benefits” (Srinivasan, 2005).

During data collection, this study considered another possible reason for the greater success in the director job markets of independent directors. A confounding variable of the amount of previous directorships impact the ability to obtain future directorships. Figure 2 highlights the importance of experience as a director.
The columns in Figure 2 are divided into groups that are evenly divided as possible. 20 outside directors ranged from zero to three previous directorships. In contrast, 18 outside directors had from 4 to 10 previous experiences as a director of another corporation. Based on the data, 38.9% of the outside directors with more than four past directorships were able to find new seats as directors in the market. Only 5% of those directors with less than three prior experiences had success finding new directorships.

In addition, the amount of previous directorships has a positive relation with the independence of the outside director. Figure 3 shows how directors with less than three prior directorships are mostly those who breached independence during the accounting scandals. 13 of the 20, 65%, outside directors with less than three prior directorships were not independent while serving as a director of the four examined firms.
In contrast, the former directors of the fraudulent firms with more than four previous experiences as director were mostly independent. Only 7 of the 18, 38.9%, of outside directors with more than four previous directorships breached independence during the period of frauds. Figure 4 provides a graphical representation.
Evidence from these figures suggests that directors with more previous experience are more likely to be independent.
Figure 5 and Figure 6 exhibit the percentage of future director positions acquired by independent outside directors after controlling for their previous experience. In both figures, the director job market is greater for those who are independent.
Despite the reputation damage from being associated with a fraud, outside directors can mitigate the magnitude of the damage by remaining independent. The reputation damage from breaching independence in firms with fraudulent financial statements is evident from all the figures.
Impact on Current Executive Jobs

Besides future job prospects in directorships, the reputation damage from a fraud also has an impact on the current executive jobs of outside directors. In determining the impact on the current jobs, I only considered those directors that were executives in publicly traded corporations. This study is concerned about the future job markets for public companies in order to provide insight for shareholders and other publicly traded corporations. Therefore, I excluded those directors that were lawyers or owners of their own firms. In addition, outside directors that held employment in universities were not considered. Due to the exclusions, a sample of only 17 outside directors was examined.

Figure 7. Relationship between Independence and % of Directors Retaining Executive Positions
Evident in Figure 7 is the importance of outside directors remaining independent. All nine independent outside directors retained their executive positions at other firms. However, half of the eight non-independent directors were no longer executives of their publicly traded company. There are two possibilities for this outcome, either the director was fired or they voluntarily left the corporation as an executive.

![Figure 8. Relationship between Previous Directorships and % of Retaining Executive Position](image)

As considered in the analysis of future directorships, the percentage of directors keeping their employment as an executive of another firm could be impacted by previous director experience. Once again, prior experience could be a confounding variable affecting the careers of directors in executive roles. Based on Figure 8, directors with one or less prior executive experiences have 75% success in retaining their executive positions. In contrast, seven of nine directors keep their executive careers if they had two or more prior executive experiences. Unlike future directorships, the difference in the job markets for amount of previous executive experience is only about 3%, from 77.8% for directors with many prior experiences to 75% for those with few.
According to Figure 9 and Figure 10, the number of prior experiences as an executive makes little difference in determining the independence of the directors.
Conclusion

To assess the effect that an accounting fraud has on the careers of outside director, this thesis examined the careers of all the outside directors of four accounting scandals in the millennium. Confirming the importance of independence in boards, it also examined those directors that received inappropriate compensation from executives. In assessing 38 outside directors, the previous experience, current employment, and future consequences were assessed quantitatively.

One implication from this study is that independence during an accounting fraud can mitigate the reputation damage on the careers of outside directors. In addition, independence suggests that an outside director has greater chance of retaining their executive careers. These results hold even after controlling for a director’s prior experience as an outside director.

In regard to the quantitative analysis, the results support what was expected. However, due to time and resource restrictions, more research could have been completed. For future research, this thesis can be improved by selecting more outside directors and firms. It would be beneficial to also include firms that committed fraud after Sarbanes-Oxley. In addition, research could be improved by examining the consequences on the other current directorships of the directors. It would be interesting to find out if an accounting scandal will cause outside directors to lose their other board memberships. Finally, a statistical analysis including a test for significance would help inform shareholders better about the implications.
APPENDIX A: RECENT ACCOUNTING SCANDALS

The following subsections will highlight the incompetence of the boards that served for the four prominent firms. Each of the boards did not perform the necessary requirements to ensure fiduciary duty. Aware of their negligence, some outside directors attempted to limit their liability to the fraud. However, attempts to salvage reputation from the scandal will not improve the chances of obtaining future seats of other boards. The independence and experience of the outside directors for each scandal are explained. In addition, decisions to resign from serving as an outside director are described.

Adelphia Scandal

In June 2002, Adelphia filed for bankruptcy and was later revealed to have committed an accounting scandal resulting in the arrest of chief executive John J. Rigas. Timothy and Michael Rigas, the sons, were also indicted on committing securities fraud. Although the cable company was a publicly traded entity, there was an essence of a family-run business. The Rigases all had special classes of voting stock that prevented other shareholders from questioning their control. In fact, almost half of the board was comprised of the Rigases and Peter Venetis, John’s son-in-law, who were inside directors. The Rigases handpicked every outside director. This composition of the board contrasts the majority of the boards in US corporations. The inside directors of Adelphia had an influence on the suggestions by outside directors. When the audit committee asked for the disclosure of money the Rigases had borrowed, Timothy Rigas persuaded outside directors to not disclose those amounts to the public.

In May 2002, all four members of the Rigases resigned their positions on the board. A special committee was formed to replace the empty positions. Critics claimed the special
committee includes members that are tainted by influence of the Rigas family. ("Suit Seeks New Board for Adelphia") The special committee comprised of Erland E. Kailbourne, Dennis P. Coyle, and Leslie J. Gelber. There were doubts about Kailbourne’s independence because he was hired near the beginning of the fraud in 1999. Kailbourne also was elected as temporary CEO after the arrest of John Rigas. Therefore in January 2003, a lawsuit was filed to prohibit current board members from participating in the election of new directors. Due to the lawsuit, in June 2003, “four board members appointed during the Rigas era finally agreed that they would step down when the company emerges from bankruptcy” (McCafferty). William Schleyer, successor of Kailbourne as CEO, claims, “As Adelphia moves forward we are actively seeking additional independent candidates who will further enhance the Board’s corporate governance, legal and policy expertise” (“Last Directors from Rigas Era Leaving Adelphia”). The outside directors during the scandal are found in Table 1.

<table>
<thead>
<tr>
<th>Outside Director</th>
<th>Years Active (during scandal)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dennis P. Coyle</td>
<td>1997 - 2002</td>
</tr>
<tr>
<td>Peter J. Metros</td>
<td>1997 - 2002</td>
</tr>
<tr>
<td>Perry S. Patterson</td>
<td>1997 - 2000</td>
</tr>
<tr>
<td>Erland Kailbourne</td>
<td>1999 - 2002</td>
</tr>
<tr>
<td>Leslie Gelber</td>
<td>1999 - 2002</td>
</tr>
</tbody>
</table>

Table 1. Outside directors during height of Adelphia Scandal
Source: SEC

In June 2002, the directors of Adelphia refused to pay the legal costs and expenses for the Rigas family. Typically, Adelphia provides payments for executives regarding legal fees and expenses unless the board finds that their duties were intentionally breached. Critics questioned this decision of the directors as an attempt to limit their liability of involvement with the fraud. ("Adelphia Family's Legal Costs at Issue").

During the height of the scandal, the directors were part of the Compensation Committee.
Two directors affiliated with FPL Group, Inc. were elected as outside directors of Adelphia.

Therefore, the independence of Dennis Coyle and Leslie Gelber is questioned because Adelphia purchased the cable television subsidiary of FPL Group in 1995 for $127.5 Million of preferred stock in exchange. (“Adelphia and FPL in Deal”). In addition, both Coyle and Gelber lacked any prior experience as a board member. During the same year, WorldCom directors faced even more scrutiny.
WorldCom Scandal

From 1999 to 2002, WorldCom executives used aggressive fraudulent accounting methods to cover the financial decline of the company. Scott Sullivan, CFO, was able to accomplish the fraud by not reporting the proper expense of transactions and inflating revenues. In June 2002, internal auditors revealed that WorldCom had inflated profits by $3.8 million. At that time, the findings led to the collapse of the largest accounting fraud in history. On July 21, 2002, WorldCom filed for bankruptcy.

<table>
<thead>
<tr>
<th>Outside Director</th>
<th>Years Active (during scandal)</th>
</tr>
</thead>
<tbody>
<tr>
<td>James C. Allen</td>
<td>1999 - 2002</td>
</tr>
<tr>
<td>Judith Areen</td>
<td>1999 - 2002</td>
</tr>
<tr>
<td>Carl J. Aycock</td>
<td>1999 - 2002</td>
</tr>
<tr>
<td>Max E. Bobbitt Jr.</td>
<td>1999 – 2002</td>
</tr>
<tr>
<td>Stiles A. Kellett Jr.</td>
<td>1999 - 2002</td>
</tr>
<tr>
<td>Gordon S. Macklin</td>
<td>1999 - 2002</td>
</tr>
<tr>
<td>John A. Porter</td>
<td>1999 - 2002</td>
</tr>
<tr>
<td>Lawrence C. Tucker</td>
<td>1999 – 2002</td>
</tr>
</tbody>
</table>

Table 2. Outside directors during height of WorldCom Scandal
Source: SEC

The outside directors during the scandal are found in Table 2. In January, 2005, ten former directors of WorldCom agreed to pay $54 million to end a class-action lawsuit. Together, the directors had to pay $18 million while $36 million came from directors’ insurance (Morgenson). Typically, directors depend on their insurance to cover the costs regarding lawsuits and settlements. This settlement sets a new precedent for directors as they are now targets for harsher criticisms. Rarely were the directors required to pay for a settlement out of their own pockets. Apparently, the outside directors did not understand the transactions involved with the
telecommunications industry (Hopkins). In addition, Nell Minow, and editor of the Corporate Library claims, “The members of the audit committee are not professionally engaged in the practice of auditing or accounting and are not experts in the fields of auditing or accounting” (thestreet.com).

Although outside directors, their independence is of most concern. Most of the board is composed of executives from acquired corporations. Unfortunately, they listened to anything Bernie Ebbers said in order to reap the benefits. Charles M. Elson claims, “It seems that directors were so beholden to the CEO that no one came forward to say: `Hey, we're in serious trouble here, and what are we doing to do about it?'” (“How Ebbers Kept the Board in His Pocket”). In fact, some of them accumulated wealth through the perks of flying in a corporate jet and obtaining large amounts of WorldCom stock. The compensation that was received blinded the judgment of some of the directors, specifically Max E. Bobbitt. Greed took over the conscience of Bobbitt, who only served as an outside director for one other firm. Lavish gifts also spoiled the independence of outside directors at Tyco.
Tyco Scandal

From 1997 to 2002, Tyco executives especially CEO L. Dennis Kozlowski performed illegal activities that were hidden from the board. This scandal included frauds on undisclosed compensation, secret loans, undisclosed transactions, and fraudulent trading. Apparently, these loans made were specifically for the benefit of the executives. Millions of dollars were provided to Mark Belnick, former general counsel, Dennis Kozlowski, former CEO, and Mark Swartz, former CFO. (Ferrell, Fraedrich, Ferrell).

Unfortunately, for the shareholders and stakeholders, the board was completely oblivious to the actions committed by executive management. Kozlowski went to great measures to prevent outside directors from understanding the transactions (Symonds). Apparently, Kozlowski controlled the flow of all information. He even had a hand in the internal audits of Tyco, which are usually reported to the board. If the board were doing their duty, they would have asked for the internal audit report from the internal auditors directly instead of Kozlowski. An observant board would have monitored transactions to prevent corporate loans to executives. In addition, a responsible board would never allow the finance department to be responsible for Tyco’s SEC filings. The outside directors during the scandal are found in Table 3.

<table>
<thead>
<tr>
<th>Outside Director</th>
<th>Years Active (during scandal)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Richard S. Bodman</td>
<td>1997 - 2002</td>
</tr>
<tr>
<td>Stephen W. Foss</td>
<td>1997 - 2002</td>
</tr>
<tr>
<td>Frank E. Walsh, Jr.</td>
<td>1997 - 2001</td>
</tr>
<tr>
<td>Joshua M. Berman</td>
<td>2000 – 2002</td>
</tr>
<tr>
<td>Wendy E. Lane</td>
<td>2000 - 2002</td>
</tr>
<tr>
<td>Joseph F. Welch</td>
<td>2000 – 2002</td>
</tr>
<tr>
<td>John F. Fort, III</td>
<td>1997 – 2002</td>
</tr>
<tr>
<td>James S. Pasman, Jr.</td>
<td>1997 – 2002</td>
</tr>
</tbody>
</table>
Tyco’s corporate governance system has never been the most independent. It had been composed of Joshua Berman, a former outside counsel; James S. Pasman, Jr., from ADT; W. Peter Slusser, from ADT; Richard S. Bodman, a venture capitalist; Stephen W. Foss, CEO of textiles; Joseph Welch, CEO of Bachman; Wendy Lane, a private equity investor; and John Fort, former CEO of Tyco; and Frank Walsh. Most of these directors had been with Tyco for at least ten years and were familiar with Kozlowski’s behavior. However, the tenure of the directors should have hinted at the potential lack of complete independence. In fact, Swartz, Bodman, Walsh, and Foss all received some sort of compensation. (Ferrell, Fraedrich, Ferrell, 2009). The other directors that were independent, who did not receive benefits from Kozlowski, had only one or two experiences on a board.
Enron Scandal

The Committee on Governmental Affairs United States Senate published, “At the May 7 hearing, the expert witnesses testified that the independence and objectivity of the Enron Board had been weakened by financial ties between Enron and certain Directors” (United States. Cong. Senate. Committee on Governmental Affairs). The directors with financial ties included John Wakeham, John A. Urquhart, and Robert Belfer. Table 4 lists the outside directors during scandal.

<table>
<thead>
<tr>
<th>Outside Director</th>
<th>Years Active (during scandal)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Robert A. Belfer</td>
<td>1997 – 2001</td>
</tr>
<tr>
<td>Norman P. Blake, Jr.</td>
<td>1997 – 2001</td>
</tr>
<tr>
<td>Ronnie C. Chan</td>
<td>1997 – 2001</td>
</tr>
<tr>
<td>John H. Duncan</td>
<td>1997 – 2001</td>
</tr>
<tr>
<td>Wendy L. Gramm</td>
<td>1997 – 2001</td>
</tr>
<tr>
<td>Ken L. Harrison</td>
<td>1997 – 2001</td>
</tr>
<tr>
<td>Charles A. LeMaistre</td>
<td>1997 – 2001</td>
</tr>
<tr>
<td>John Mendelsohn</td>
<td>1999 – 2001</td>
</tr>
<tr>
<td>Jerome J. Meyer</td>
<td>1997 - 2001</td>
</tr>
<tr>
<td>Paulo V. Ferraz Pereira</td>
<td>1999 - 2001</td>
</tr>
<tr>
<td>Frank Savage</td>
<td>1999 - 2001</td>
</tr>
<tr>
<td>John A. Urquhart</td>
<td>1997 - 2001</td>
</tr>
<tr>
<td>John Wakeham</td>
<td>1997 - 2001</td>
</tr>
<tr>
<td>Herbert S. Winokur, Jr.</td>
<td>1997 - 2001</td>
</tr>
</tbody>
</table>

Table 4. Outside directors during height of Enron Scandal

Source: SEC

In May 2004, 12 outside directors agreed to pay $1.5 million of their own money to settle a lawsuit. “Outside directors at scandal-ridden companies are generally well-protected from
criminal prosecution and civil lawsuits. Prosecutors must prove that outside directors acted with criminal intent, a much higher bar than accusing board member of failing to pay attention at meetings or scrutinize the actions of corporate management” (Masters, Day). Since Enron directors had to pay out of their own pockets, it exhibits a sense of criminal intent and lack of independence
APPENDIX B: THE OUTSIDE DIRECTORS

Adelphia’s Outside Directors

Information about the directors was obtained with the 10-K filed by the SEC. Various other sources including Businessweek and Forbes were used to find current whereabouts of the directors.

Dennis P. Coyle

Dennis Coyle served as General Counsel and secretary of FPL Group, Inc. and Florida Power & Light Company from 1989 to 2005. During that time he served as a director in the height of the Adelphia scandal. After the scandal, Coyle returned to his duties at FPL Group and remained in law practice before retiring in 2005. According to Lew Hay, CEO of FPL Group, “Dennis helped put in place many of the corporate governance principles that have served our company well, ensuring that we remain a company that is on the leading edge in our governance policies and practices” (FPL Group).

Erland E. Kailbourne

Since leaving Adelphia, Erland Kailbourne has found many job opportunities. He is currently the Chairman of the Board at Albany International Corporation and Financial Institutions, Inc. (Erland Kailbourne: Executive Profile & Biography – BusinessWeek) In addition, he is a director at New York ISO, The John R. Oishei Foundation, Rand Capital Corporation, Allegany Co-op Insurance Company, USA Niagara Development Corp, Farash
Corporation, and the Max and Marain Farash Charitable Foundation. (Corporate Executives & Directors Search Directory)

**Peter J. Metros**

A director of Adelphia since 1986, Metros is one of the longest tenured members of the board. He was also a director of Adelphia Business Solutions, a subsidiary. After resigning as board in 2003, no concluding evidence has been found about his career opportunities. It is assumed that he has retired or is involved with private organizations.

**Perry S. Patterson**

In addition to Peter Metros, Perry Patterson was elected as director in 1986. He has practiced law since 1997 in Cloudersport, Pennsylvania. Patterson has also served as President Judge of the Court of Common Please of the 55th Judicial District in Potter County, Pennsylvania. He resigned as director of Adelphia in 2000 at the age of 83. No evidence of his job prospects was found. It is assumed he has either retired or continued to practice law.

**Leslie Gelber**

In 1999, Leslie Gelber was elected as director of Adelphia and chosen as President and CEO of Caithness Corporation. Gelber has previous executive experience with Cogen Technologies, Inc. and ESI Energy, a former subsidiary of FPL Group, Inc. He was also Director of Corporate Development for FPL Group and held executive positions at the Group’s cable television and information services subsidiaries. After leaving duties as director of Adelphia, Gelber returned to Caithness Corporation and currently still serves as President and CEO.
WorldCom Outside Directors

Information about the directors was obtained by the 10-K filed by the SEC. Various other sources including Businessweek and Forbes were used to find current whereabouts of the directors.

Max E. Bobbitt

Since becoming a director of WorldCom in 1992, Max Bobbitt left Alltel in 1995 and became President and CEO of Metromedia China from 1997 to 1998. Metromedia China was a subsidiary of Metromedia International Group that was claimed to have poor corporate governance. Before the scandal was revealed, Bobbitt was claimed to have created a plan to remove Bernard Ebbers as CEO of WorldCom. This plan backfired and was scrutinized because the board had supported Ebbers’ every move in the past. Bobbitt has had experience as a director at Verso Technologies, Inc., and Metromedia China Corporation. Before his resignation from the board, Bobbitt owned 434,000 shares of WorldCom stock. Currently, Bobbitt acts as a technology consultant.

Carl J. Aycock

Aycock was one of the founders of LDDS, original company before WorldCom’s expansion, but had left the company and served on the board. He served as secretary of WorldCom from 1987 to 1995. No evidence of future jobs was found after the WorldCom settlement.
Stiles A. Kellett, Jr.

Stiles Kellett is a wealthy investor from Atlanta, Georgia. Kellett has served as director of WorldCom since 1981. He resigned on October 27, 2002 and had to pay $120,000 in response to his use of corporate jets. In the past, Kellett had an agreement with Ebbers to use corporate aircraft for $1 a month and a fee of $400 per hour. He has been a director at Netzee, Inc., Air2web and Virtual Bank. His independence with WorldCom was severely flawed as his shares in stock rose significantly from one million shares in 1996 to 4 million shares in 1998.

Clifford L. Alexander

Clifford joined the board in 1998 after the merger between MCI and WorldCom. He left in 2000, but it is believed that WorldCom executives were applying fraudulent schemes in their financial accounting during his three years as director. Alexander also worked under Jimmy Carter as Secretary of Army from 1977 to 1981. In addition, he has served on the board for American Home Products Corporation, IMS Health, and Dreyfus funds. He is currently on the Board of Governors for the American Stock Exchange.

Gordon S. Macklin

James C. Allen

James Allen also joined the board in 1998. He was the CEO of Brooks Fiber Properties until its merger with WorldCom in 1998. Previous directorship experience includes Completel LLC, David Lipscomb University, Family Dynamics Institute, and Xspedius, Inc. Allen owned around 413,000 shares of WorldCom stock during its collapse.

Judith Areen

Judith served on the board from 1998 to 2002. From 1999 to 2001 she was on the audit committee and signed off on the 10-K’s. She previously was the Executive Vice President for Law Center Affairs and Dean of the Law Center at Georgetown University. Since 1976 she has been a professor at the university. Currently, she serves as Interim Dean and Paul Regis Dean Professor of Law. In the past, she has served as president of the Association of American Law Schools, board of trustees at Cornell, and governor of the District of Columbia bar. Areen owned around 114,000 shares of WorldCom stock during its collapse.

John A. Porter

Porter served on the board from 1997 to 2000. He was previously an executive with WorldCom until 1996, time before fraudulent accounting started. In April 2004, Porter filed for bankruptcy and had trouble paying off the settlement. He currently is unemployed. Porter owned around 6 million shares of WorldCom stock during its collapse (Coolidge).

Lawrence C. Tucker

Tucker served on the board from 1995 to 2000 but became an advisory director from 2000 to 2002. His compensation did not change from director to advisory director. He was previously a general partner of Brown Brothers Harriman & Co. His directorship experience

Tyco’s Outside Directors

Information about the directors was obtained by the 10-K filed by the SEC. Various other sources including Businessweek and Forbes were used to find current whereabouts of the directors.

Richard S. Bodman

Bodman served on the board from 1992 to 2002. He is currently the Managing General Partner at VMS Fund Administration and AT&T Ventures, LLC. In the past, he was the CEO of Comsat General Corporation and the President of Satellite Television Corporation. He was also a Partner at Touche Ross & Company. Previous directorship experience includes KNOLOGY Inc., Internet Security Systems, and Coppercom, Inc. Since the scandal he has become director of GridPoint Inc., Spacehab Inc. Questions have been raised about his independence after the disclosure that Mr. Kozlowski invested $5 million in his technology fund in 2000.

Stephen W. Foss

Stephen Foss served on the board from 1983 to 2002. He was a member of the compensation committee, where most of the scrutiny of the directors was placed. In the past, he has been the Chairman and CEO of Foss Manufacturing Company, Inc. He received payments for a total of $587,000 for leasing his aircraft to Tyco. No information has been found on his whereabouts after the scandal.
Wendy E. Lane

Wendy has served on the board from 2000 to 2002. Her past directorship experience includes Laboratory Corporation of America Holdings. Ms. Lane is also a director and Audit Committee member of both Willis Group Holdings, Ltd. and UPM-Kymmene Corporation, and a Trustee of the U.S. Ski and Snowboard Team Foundation. She is the President and Chairman of Lane Holdings, Inc.

John F. Fort, III

John Fort has served on the board from 1983 to 2002, but as an outsider since 1992. His past directorship experience includes Insilico Corp., and Roper Industries, Inc. He was the CEO of Tyco’s predecessor company from 1982 to 1992.

W. Peter Slusser

Slusser has been on the board from 1992 to 2002. He has been the President of Slusser Associates, Inc. He has also served as director of Ampex Corporation and Sparton Corporation.

Frank E. Walsh

Frank Walsh as a principal at Wesray Capital Corporation. He has served on the boards of Avis, Inc., Wilson Sporting Goods, Gibson Greeting Cards, Atlas Van Lines, Six Flags Corp., and WearEver Proctor Silex. Walsh has been claimed for committing a breach of fiduciary duty, inducing breaches of fiduciary duty and related wrongful conduct involving $20 million payment by Tyco, $10 million of that going to a charity where Walsh is a trustee (Sorkin).

Joshua M. Berman
Berman has been a director of Tyco from March 1, 2000 to December 5, 2002. Tyco provided Berman with compensation of $360,000 with health benefits, secretarial assistance, cell phone and electronic security services at his residences. In the past, he was a counsel to the law firm Kramer Levin Naftalis & Frankel LLP, which provided legal services to Tyco. He is currently unemployed and retired.

**Joseph F. Welch**

Joseph has served on the board from 2000 to 2002. Welch is the President and CEO of The Bachman Co. He has also served as a director for Detroit Diesel Corporation. Whereabouts of his careers after the scandal are unknown. It is assumed that he has returned to The Bachman Co.

**James S. Pasman**

Pasman has served on the board from 1997 to 2002. He has been the President and CEO of Intergroup, INC. He was also Vice Chairman, Executive Vice President, and CFO of ALCOA. His directorship experience comes from Kaiser Aluminum and Chemical Corporation, PNC Corp., PNC Bank, Bell Telephone Company of Pennsylvania, the Aluminum Company of America, National Intergroup Inc., Periman Oil Company, BEA Income Fund, Inc., and BT Insurance Funds Trust.
Enron’s Outside Directors

An article, “Former Enron Directors: Then and Now” by the Washington Post provides most significant information regarding director seats on the board after the collapse. Instead of the 10-K, information about the directors had to be obtained by Schedule 14A.

Robert A. Belfer

Robert Belfer has been a director at Enron since 1983. Belfer has been the CEO of Belco Oil & Gas Corporation, from 1996 to August 2001. He was also a CEO at Belfer Management LLC. Past directorship experience comes from GTI Group LLC and Glori Oil. He also has duties in education as he served for the boards of Albert Einstein College of Medicine, Kennedy School of Government at Harvard, and Weill Cornell University Medical College. He was a graduate of Harvard Law School. He currently does not have a seat on any board.

Norman P. Blake, Jr.

Norman Blake has served on the board since 1993. Blake is a former CEO of Comdisco, Inc., and has been a director since 2006. He has also been a director of OCD since 1992. Other CEO titles were obtained at the Olympic Committee, Promus Hotel Corporation, USF&G Corporation, and Heller International Corporation of Chicago. Mr. Blake is a member of the Dean’s Advisory Council at Purdue Krannert School of Management. He is currently a director at Owens Corning.

Ronnie C. Chan

Most sources on the Internet do not mention Ronnie Chan as a previous director of Enron. Ronnie is an advisor for Shanghai Industrial Investment (Holdings) Co. Ltd. He is also a
director of Asia Society and serves on governing bodies of many universities in Hong Kong and
elsewhere, including the Indian School of Business. Currently, he serves as chairman and
director of Hang Lung Properties Limited and Grand Hotel Holdings Limited. Chan has sat on
two other boards since the Enron collapse.

**John H. Duncan**

Duncan has served on the board from 1985 to 2001. John Duncan has served on the
board from 1985 to 2001. In the past, he had been the president of Gulf & Western Industries
Inc. His previous experience as a director comes from EOTT Energy Corp., Chase Bank of
Texas, National Association, and Group I Automotive Inc. He currently is not on any board.

**Wendy L. Gramm**

Gramm has served on the board from 1993 to 2001. She was a director at IBP, Inc., State
Farm Insurance Co., Chicago Mercantile Exchange, and Invesco Funds Group, Inc. Gramm
resigned from Invesco Funds board after the Enron scandal. She currently does not serve on any
board.

**Ken Harrison**

Harrison had served on the board of Enron from 1997 to 2001. He was previously the
CEO of Portland General Electric Company, which was acquired by Enron on July 1, 1997. He is
just another member on the board that became a director after their previous company was
acquired (CorpWatch: Enron: Facts and Figures). His independence is in question.
**Robert K. Jadicke**

Robert Jaedicke has served on the board since 1985. He was previously a Professor (Emeritus) of Accounting at the Stanford University Graduate School of Business in Stanford, California. His association with Stanford stems back to 1961 and he served as Dean from 1983 to 1990. Boise Cascade Corporation, Wells Fargo & Company, California Water Service Company, GenCorp, Inc., and State Farm Insurance Co. had selected him as a director. He also served as an adviser to C.M. Capital Corp., an asset management entity. He is currently retired from any boards.

**Charles A. LeMaistre**

Charles LeMaister has been director since 1985. LeMaistre was previously the president of the University of Texas M.D. Anderson Cancer Center. He currently does not sit on any boards.

**John Mendelsohn**

John Mendelsohn has served on the board since 1999. Mendelsohn is an interesting person to research because he was also on the board of Imclone Systems Inc. during their scandal. He is currently the president of M.D. Anderson Cancer Center and does not seem to be affected at all by the scandals in the corporations he has been a director.

**Jerome J. Meyer**

Jerome Meyer has served on the board from 1997 to 2001. He had been the CEO of Tektronix, Inc. Esterline Technologies Corporation and AMP, Inc. had selected him as director. Meyer is currently on board and serves as the audit and operations committee of StanCorp Financial Group.
Paulo V. Ferraz Pereira

Paulo Pereira has served on the board since 1999. He had been a CEO of Meridional Fiancnail Group. Paulo is the president of a South American banking conglomerate. He is currently not serving on any board in the United States.

Frank Savage

Frank Savage has been a director of Enron since 1999. He had been the CEO of Savage Holdings LLC. Other executive positions held include VP of The Equitiable Life Assurance Society of the United States. He has also been a director of Lockheed Martin, Alliance Capital Management L.P. and Qualcomm Corporation. Savage stayed on the board of Lockheed Martin despite attempts to oust him from a seat.

John A. Urquhart

John Urquhart has served on the board of Enron since 1990. He has been the president of John A. Urquhart Associates, a consulting firm. Urquhart was also the CEO of Enron Solar Energy Inc. Therefore, his independence might be impaired. Other boards he has been a part of include Amoco/Enron Solar Partnership, Aquarion Company, TECO Energy, Inc., Hubbell, Inc., The Weir Group, PLC, and Catalytica Inc. Urquhart remained on the board of Catalytica until 2006. He is currently not serving on any boards.

John Wakeham

Wakeham had served on the board since 1994. He was on the U.K parliament from 1974 to 1992. He had been a director in a few publicly traded U.K. companies.
Herbert S. Winokur, Jr.

Winokur has been on the board of Enron since 1985. He was previously a president of Winokur Holdings, Inc. Winokur has served on the board of Penn Central Corporation, NAC Re Corporation, WMF Group, Ltd., Mrs. Fields Holdings, Inc., and DynCorp. He is a partner at Capricorn Holdings and has sat on two boards since the collapse of Enron.
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Bachelor of Science Degree in Accounting, Penn State University, Spring 2010  
Honors in Accounting  
Minor: Information Systems Management  
Thesis Title: The Effect of Accounting Fraud on the Careers of Outside Directors: The Role of Director Independence  
Thesis Supervisor: Bin Ke

WORK EXPERIENCE:

KPMG LLP., New York City, NY  
- Reconciled work papers for valid calculation of royalties in contract compliance  
- Analyzed cycle end time records for project management team and client review  
- Consolidated expense reports for analysis ensuring details are within client policy

Ametek Inc., Paoli, PA  
- Performed fixed asset tax depreciation project to minimize external consultancy  
- Consolidated subsidiary data to a centralized fixed asset tax depreciation system  
- Reconciled data between records from external consultancy & old databases

AWARDS:

- Jack Oppenheimer Family Scholarship – Awarded for Excellence in Academics  
- Robert W. Koehler Academic Excellence in Accounting Scholarship  
- Dean’s List – Each Year

ACTIVITIES:

- Business Student Council – Events Committee  
- Asian American Christian Fellowship - Treasurer  
- Spring Up Community Service – Volunteer

SKILLS:

SAP R/3, Microsoft Office Suite, Project, Visio, Dynamics GP, VB.net and RIA InSource  
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