

# [Balance sheet and enron derivatives trading](https://assignbuster.com/balance-sheet-and-enron-derivatives-trading/)

How did the corporate culture of Enron contribute to its Bankruptcy? Once a sound company listed in fortune 500, Enron, lead to downfall because of deceptive accounting system incorporated within the organization.

Enron’s dubicious finance finally collapsed in Dec 2, 2001 as it filed Bankruptcy in New York Bankruptcy court. The corporate culture of Enron focused on financial performance neglecting the stakeholder’s value .

The relentless emphasis on the importance of the shareholder’s value created the conditions for the disconnection of Enron from their essential oral underpinnings, encouraging them to concentrate exclusively on financial performance, and to neglect stakeholder’s common interest, but the essential interests of the economies and communities in which they operate.. The problem with established economic theories of corporate governance is that they misconceive the irreducible corporate governance, at the same time as underestimating the complexity of the phenomenon. Clarke, 2005) The ‘ rank and yank system implanted by Skilling created the worst situation as the employee started the rivalry between each other in terms of making money at any ost violating the corporate culture.

Fewer rewards were given to those who produced sustainable financial fortune and the bottom ranked employees were forced out The bad fortune of the company was destined by Enron’s management incentive system. Destructive business culture was implanted as Enron primarily focused on employees self worth rather than company’s worth.

Extra rewards were provided to those candidates who contributed on promoting productivity. Those who contributed themselves on controlling the existing resources were not skewed with any incentives. The company’s profit was under a billion dollar but the average compensation of top 200 executives was over 1.

4 billion. Employees at the executive level were promoted quickly that left the lack of good executive skill at the vacant level. The Bankruptcy of $63 billion company was significantly contributed by its business culture incorporated by Skilling and the value promoted among executive level and mid-level of management during his era from 1996 to 2001. The ethics among the upper level implanted by Skilling made the company inevitable from its death .

Skilling himself described in the U. S Senate testimony that the reason of Enron’s debacle as a ‘ Classic run on the bank ‘ had for years focused on taking profits now and worrying about the details later’. Fowler, 2002) The evil culture on Enron had features like high risk accounting, undisclosed off balance sheet statements, over compensation, unnecessary employee competition and lack of teamwork. ‘ With the introduction of off-balance sheet companies, it slid trom creative to economic and social destruction. Enron’s losses on speculative and strategic moves reached such proportions that management desperately turned to a ualitatively new and more reckless gambit, improperly structured partnerships, hedge transactions, and deliberately falsified accounting.

Unlike proper off-balance sheet transactions, these new counterparties were capitalized with Enron’s own stock and managed by insiders. The financing of the partnership in effect meant that Enron was ensuring itself . An Enron derivatives trading increased and became more complex, it relied increasingly on financial strengths of hand that grew rather than contained the contagion. “(Kobrak, 2009) Did Enron’s bankers, auditors, and attorneys contribute to Enron’s demise? If so, what was their contribution? Vinson and Elkins supported to fgure out some of the special purpose partnership of Enron.

The law firm serving Enron for several years believed to support the legal deals which was illustrated as fraudulent by several law firms later Enron’s bankruptcy trustee is negotiating to settle claims with V&E for $30 million.

As part of the deal, the law firm will also drop its claim for $3. 9 million in legal fees billed to Enron before the company went out of business, a small fraction of the $162 million the firm charged Enron from 1997 to 2001. The Securities & Exchange Commission is investigating the advice that V&E and other outside law firms gave the company.

And in the same class action in which they have targeted the banks, plaintiffs’ lawyers are preparing to unleash a new volley of evidence on June 13 to support allegations that V&E should be liable for some of the $40 billion in investor losses resulting from the energy giant’s collapse.

(Business Week, 2006) Merrill Lynch faced prosecution from Securities and Exchange Commission for aiding and abetting Enron’s securities fraud. SEC stated that Merrill Lynch and its former xecutives aided and abetted Enron’s earnings by disfiguring and manipulating the datas in the year ending 1999.

They assisted Enron to overstate their financial results. Those fraudulent transactions added about approximately $60 million to its fourth quarter of 1999 income. Merrill Lynch also assisted to increase the earning per share price from $1.

09 to $1. 17 in the same year. SEC prosecuted Enron stating the Nigerian Barge deal in which Merrill Lynch allegedly bought the barge for $28 million. Following the oral assurance of the CFO, Fastow, only $21 million has been financed nd Fastow assured that Enron would buy Merrill Lynch’s investment out in six month with a 15% guaranteed rate of return.

Although Merrill lynch agreed the oral assurance of Fastow but the internal document of Merrill Lynch stated that the transactions was not lawful and appropriate. According to the SEC, Merrill Lynch violated its fiduciary responsibility to investors who entrusted it as an asset management company to use their money prudently, in a manner consistent with their financial goals.

Instead, the company helped Enron create a false “ sale” of three barges. Designed to look like a sale, in reality the transaction was an “ asset parking” arrangement i. e.

Just a loan designed to help Enron meet its profit target in the last quarter ot 1 (Merrill bought an interest in a number ot Nigerian barges trom Enron with the understanding that it would be paid back with interest within six months.

) In late 1999, Merrill Lynch also extracted an $8. 5 million structuring fee for another deceptive deal designed to inflate Enron’s income by about $50 million, through two complex energy options trades (Lenazun, 2010) Arthur Anderson was Enron’s auditor who used to measure Enron’s books of accounts and financial statements.