

An explanation of the causes and effects of the enron accounting scandals

[Business](#), [Accounting](#)



From the 1980s until now, there have been a lot of accounting scandals which were widely announced on by media. The result of this situation is many companies were bankruptcy protection requests, and closing. One of the most widely reported emulation of accounting scandals is Enron Company. Enron Corporation is one of the largest energy companies in the world. Enron was founded in Houston, Texas, America in July 1985 by the consolidation between Houston Natural Gas and InterNorth of Omaha, Nebraska (" Enron and Enderson: The story", n. d.). According to Sridhanran, Dickes & Caines (2002, p.), Enron's rank number is the seventh in the United States by Fortune magazine in April 2002.

Their businesses were sale of nature gas, electricity sector, water, metal, broadband and newsprint. Enron has been altered from the old economy company to the new economy company and focus on HFV (Hypothetical Future value). The profits were grown by buying electric at stable prices from the suppliers and sale the different prices for customers. When the falsehood of their profits was opened, the investors withdraw the capital. Enron start collapse (" Case study: The collapse", n. . , pp. 1-2). Definitions Accounting scandals are political and business scandals using illegal accounting systems and fraud in the financial statements. According to Hanson (2002, p. 1), Enron accounting scandal is the most important commonfailurein the banks during the 1980s in the United States. This leads to changing in business and the law. When Enron was bankrupt, the economy of America was dropped, and many employees were lost their jobs. Outline and Limitations The assignment will explain two main reasons and two effects of Enron accounting scandal.

The assignment will conclude with review the Enron accounting scandal and giving the lessons for another company. The Causes of Enron Accounting Scandal Business Fraud A business fraud is one of the most important reasons which made bankruptcy of Enron. Firstly, limited partnership companies were opened by CFO Andy Fastow. He used many partnership companies such as J. P. Morgan Chase and Merrill Lynch to hide their enormous debts and losses from investors. They borrowed the great amounts of money from financial institutions to buy many assets; this led to wrong view about Enron condition.

It helped the stock price increase (" Enron accounting scandal", 2009). In addition, the financial strategy, the business consultants and the accounting techniques are wrong choice of Enron. They used established investment money to build securitization abilities. According to Buondonno, David, Pufky and Rollings (n. d. , pp. 11-12), Enron has distorted the financial statements using the complex methods. They used fake companies (SPEs) to move money between different banks and created false financial statements. This led to misunderstanding of shareholders about the real financial statements.

Moreover, Enron predicted the future market of energy price. As a result, the sale prices of Enron known as mark-to-market, which control the energy trading business and the reports which they want to show. Furthermore, Enron used wrong accounting system. They used mark-to-marked trading which is greatly hard to change to another system. The reports were shown losses or gains on the stock and security price at the end of the year. Enron

was able to use SPE (special purpose entities) to trade in legal time or illegal time so that income could change to correct with investor expectances.

Lastly, Enron had a huge negative dollar cash flow from bank loans. They needed to pay around two million dollars per day by cash. A Corruption and a Lack of Accounting Techniques According to Buondonno, David, Pufky and Rollings (n. d. , pp. 18-20), Management level and accounting level were forgotten in Enron situation. Andrew Fastow, the Chief Financial Officer (CFO) of Enron used his power to corrupt by using his knowledge into the agreements and making the bonuses from the agreements. Andrew and his wife got benefits from Enron to buy Chewco where his wife is owner.

He controlled subsidiary companies to buy stock and hid debt for Enron. Enron did not follow the accounting rules. Every mistake in accounting needs to note and describes for shareholders know, and writes on the financial statements. In 2001, Accountants cannot combine Chewco into the Enron's financial statement. This lead to misunderstanding report which show the financial statement of Enron such as a decrease Enron income and an increase Enron's reported debt. In addition, Enron tried to make maximize profits by break the law.

Therefore, dishonesty in the financial statement, corruption and a lack of knowledge and skills of accountants are the causes of the Enron's bankruptcy. The Effects of Enron Accounting Scandal on Employees and shareholders When Enron was bankrupt, the most affected people are Enron's workers and shareholders. Many people lost their jobs, their whole pension and all of the shareholders lost their money (Dunder, n. d.).

According to Raver (2006, p4-5), Enron stocks prices were increased nearly double in one year by many ways such as legal and illegal way.

The stock price was increasing so fast, many Enron employees bought Enron stock assaving money, and also their pension are in Enron's stock too. When Enron was failing, Enron's stock price was decreasing until no longer value, many Enron workers lost all their money, their jobs and also their pension lost too. For this reason, they almost have nothing; they only have social security funds. The suddenly decrease of the value in Enron stocks influenced the retreat savings of thousands Americans who are not Enron employees. Many Americans saved their money in the index funds.

Enron's stock was formed by the different sources of investment, such as the state pension plans, university and other non-profit foundations (Sridharan, Dickes & Caines, 2002, p. 4). Therefore, when Enron scandal was happened, this entailed many effects on workers, shareholders and Americans who are not Enron employees. They lost their money, their jobs and their future. The United States and the Stock Market Enron accounting scandal helped American improve their knowledge of business and accounting. This leads to changing in the U. S. aw to protect people from the business fraud (Raver, n. d. , p. 4). They fortified retirement security of American, and limited on selling stocks for employees (Sridharan, Dickes & Caines, 2002, p. 8). Moreover, the stock market was affects by the Enron accounting scandal, Enron's stock was \$80 per share. When the Enron accounting scandal was discovered, the price of Enron's stock fell down less than \$1 (" Enron stock

prices", n. d.). Conclusion The Enron accounting scandal is one of the biggest problems of cheating in accounting in America.

It changed the most American life, and people behold themselves to know the answers of cupidity and break the law in business. The Enron accounting scandal has many reasons such as business cheating, the corrupt of the power person and inexperience of accountants. For this reasons, Enron bankruptcy had many effects on Americans social such as workers, shareholders, the American economy and the law. The lesson from Enron accounting scandal were found by many ways such as the conflict of interest between two roles played, employees' protection, changing in business managements, and ethics in business, cautious investment.