

Finance director

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Lack of proper corporate governance can be a disaster for companies. In recent years, major Australian companies such as HIH, One. tel and Harris Scarfe failed under dramatic and high profile circumstances. As a result, executive and non executive directors from each of these companies have spent time in jail. They were vastly different companies, operating in different industries, and failed for very different reasons. However, there was one common link between them. All had poor corporate governance. In this paper, I would like to take the One.

tel collapse as one example and analyse how it went collapse through its poor corporate governance. One. Tel's business One. Tel was was established by Jodee Rich and Brad Keeling in 1995. Its business grew rapidly and expanded into Europe and the USA. One. Tel had 2.4 million customers world-wide including 500,000 in the United Kingdom. One. Tel came to do business reselling Optus Mobile Phone Services, reselling Telstra Local and Long Distance International Calls, reselling Telstra internet services, selling pre-paid phone cards for long distance calls, and set about but did not complete constructing a mobile phone network of its own.

A huge expansion of activities and liabilities was involved in constructing the network, including contracts committing expenditure of more than \$1.1 billion with Lucent Technologies. The Group associated with One. Tel employed 3000 workers throughout the world and had many subsidiaries. In 1999 News Ltd and Publishing and Broadcasting Ltd made investment around \$1 billion in One. Tel. Impact of One. tel's collapse The collapse of One. Tel was the 4th biggest corporate collapse in Australia. One. Tel was

placed in administration and subsequently into liquidation in May 2001 with estimated debts of \$600 million. One.

Tel's 1, 400 workers, who were owed a total of \$19 million in accrued entitlements were dismissed. Problems in the structure of One. tel One. Tel's rapid expansion was way beyond its financial capacity coupled with its misguided management decision. It was also badly hit by the changes in the European network providers and more generally, One. Tel was caught up in the international collapse of dotcom ventures. The company's high risk, low yield strategy, with generous incentives for new customers could not be sustained in the small Australian market which had six mobile phone providers – the second largest number of any country in the world.

The fatal flaw in the business model of the company was that the telecom services were offered to subscribers at lower than the price the company was paying for them itself. It could only survive as long as it could raise new capital investment more rapidly than it was burning money. There is a number of factors that led One. Tel' to collapse. Each factor is discussed in details below. Focus on sales volume while operating at a loss Figure 1 shows One. Tel's sales revenue and profit after tax in 1999 and 2000 respectively. The firm's sales revenue showed successive growth to reach \$653.

4 million in 2000 which is about double of the sales revenue of the previous year. However, this dramatic increase in the sales revenue did not result in higher profitability. One. Tel's profit dropped from \$7 million to -\$291 million between 1999 and 2000. The reason is simply because the company was focusing on increasing sales rather than making profit. Surprisingly, while the

company is making a loss of \$291, One. Tel's top six executives were paid a total remuneration of \$1, 595, 000. Furthermore, \$6, 904, 000 were given to each of the two executive directors as a performance bonus. Issue of shares to cover up deficit

One. Tel has been also investing in current and non-current assets at an increasing rate in all the years it operated. Its cash expenditure for acquiring current and non-assets went up to \$87. 5 million and \$614. 9 million respectively in 2000. One. Tel's ever increasing investments in tangible and intangible assets and its deepening cash deficit in operating activities were financed by issuing both debt and equity. It issued equity capital of \$430. 3 million and \$818. 8 million in 1999 and 2000 respectively and raised \$58. 9 million and \$139. 8 million of debt in 1999 and 2000 respectively.

It could only survive as long as it could raise new capital investment and debts more rapidly than it was burning money. Inappropriate board structure
The board of directors is the ultimate decision making body of an organization and is responsible for major investment, financial and operation policies, and strategic directions of the company. It also provides an important supervisory role of company executive management. Moreover an audit committee and other board committee such as remuneration committee also play important role as a component of corporate governance. It is quite doubtful that One.

Tel had a proper board structure. For the year 1997-98, One. Tel had four members in the board with two joint managing directors (chief executive officers) and two non-executive directors of whom one acted as the chair of the board. All board members were subject to election each year except one

of the managing directors. This ensured that at least one of the existing managing directors remained as one of the CEOs for all times. One. Tel never had a regular, designated chair in the board. In 1997-98, one of the managing directors was appointed as the chair for one of the eight meetings held in the year.

In 1998-99, the non-executive chair attended seven of the ten board meetings held in the year, but presided over only four meetings. Of the remaining six meetings, four were presided by a managing director, one presided by another managing director and one presided by the finance director and company secretary. Thus, there are serious questions about the role and efficacy of the board chair as a non-executive director. During 1999-2000, John Greaves who had been the non-executive chair since May 1995, attended all 12 board meetings during the year but presided over 10 of the 12 meetings.

Jodee Rich, one of the managing directors presided over one meeting and then the finance director presided over another meeting. Further, the largest two investors in One. Tel, James Packer and Lachlan Murdoch attended nine and seven of the 12 board meetings in 1999-2000, respectively. Thus, corporate governance practice in One. Tel suggests excessive influence of the CEOs in the board, dual role played by the CEOs and inadequate monitoring of board activities by the non-executive directors and inadequate participation in the board meetings by the major shareholders.

All these are reflections of weak corporate governance structure at One. Tel for all the years it operated. At the end of June 1999, One. Tel's board comprised eight members which included five non-executive directors. The

Audit Committee of 1997-98, 1998-99, and the Finance and Audit Committee of 1999-2000, Remuneration Committee of 1999-2000 and Corporate Governance Committee of 1999-2000 were all comprised of the same two non-executive directors, Rodney Adler and John Greaves, who had close links with the CEOs. This is despite the fact that One.

Tel had three other non-executive directors at least for part of 1998-99 and for the whole of 1999-2000. Manipulation of financial report One. Tel was hiding its losses in early years by adopting non-conservative accounting policies. The real performance and financial condition of One. Tel has been hidden away from the major shareholders by their 'too much dependence' on the CEOs for information and presumably by non-attendance of a few board meetings. As late as 30 March 2001, One. Tel board meeting was told that 'everything was fine'. Even later than that, on 1 May 2001, One.

Tel's cash crisis was simply termed as 'timing issue'. Improper billing systems Although sales revenue had been increasing each year, enough cash was not being collected to finance the aggressive corporate expansions. One. Tel's hunger for building a large customer base too quickly by offering cheap call rates and offering credit to customers without stringent credit checking may have brought allegedly lower quality customers who were very slow in making payments, if not defaulted on their debts. Its accounts receivables were building up and in 1999-2000, only 55% of the new sales revenue were collected within the year.

One. Tel was getting massive sales as it cashed in on the deal with optus. The company rode high on this with no real thought for the consequence and the pull back of funds from Optus that would eventually come when those

customers failed to pay. Entrance to existing market The company's high risk, low yield strategy, with generous incentives for new customers could not be sustained in the small Australian market which had six mobile phone providers, the second largest number of any country in the world. One. Tel initially started its business as a re-seller of mobile telephone services.

By 1997, it decided to build its own mobile network. It undertook a very aggressive strategy of expanding into new markets without consolidating its position in the existing markets. To fuel its growth of market share, it was even undercutting Telstra, the largest competitor and the market leader in the Australian telecommunications market. External auditor The audit function has been a crucial part of ensuring the fair representation of company financial statements. However, One. Tel and its external auditor failed to place proper auditing. From 1997 to 2000, One.

Tel was audited by the same firm, BDO Nelson Parkhill. The auditor issued unqualified audit opinions for all these years. In January 2001, One. Tel switched its auditor to Ernst ; Young, who complained to the senior management that provisions for bad debts were too low. The 1998-99 financial statements of One. Tel are a case in point on the company's accounting practices. Submission of the full accounts to the ASIC revealed that the company had deferred \$48 million of expenditure and a loss of more than \$40 million had been concealed (Barry, 2002).

Subsequently, the ICAA examined the One. Tel financial reports and identified 48 items of concern. Both the audit partner, Steven La Greca, in charge of One. Tel and BDO Nelson Parkhill were reprimanded by the ICAA's disciplinary committee and were fined \$48000. The committee also

concluded that the audit report was in breach of the Corporations Law, Australian accounting standards and Australian auditing standard Regal proceedings against One. Tel and its directors ASIC launched civil penalty proceedings against some directors and officers of One.

Tel for breache of the statutory duty of care and diligence under section 180(1) of the Corporations Act 2001. The proceedings initially brought by ASIC were against four defendants, arising out of the collapse or on-sale of overseas subsidiaries. However, The New South Wales Supreme Court eventually dismissed ASIC's civil proceedings against Jodee Rich and the company's Finance Director, Mark Silbermann in November 2009 while the other two directors, Keeling and Greaves were subject to a disqualification from being a director for ten years and four years, and liable to pay compensation of \$92 million and \$20 million respectively.

Things can be learnt The collapse of One. Tel highlights the importance of good corporate governance, in particular, the need for an effective board of directors for monitoring management, the need for independent, non-executive directors for making a board effective and curbing the excessive influence of the CEO and the strategic importance of managing cash flows, in particular collection of accounts receivable. One. Tel is also a lesson for large investors. Large investors should always participate actively in the management of the firm.

A major shareholder cannot take the risk of relying on other shareholders to provide valuable information on management activities and corporate performance. There is also a lesson for all firms that a desire to grow too fast too soon could be a recipe for a disaster. This is an old reminder to all living

firms. Moreover, One. Tel was pricing its services below cost even on a cash basis, which is unsustainable in the long run. Conclusion Through this study, I have identified how One. Tel went collapse. It is obvious that there was lack of focuses on business basics, that is to make a profit rather than increasing sales volume.

In addition, poor governance of board structure in One. Tel reduced the chance of problems being detected by the board of directors soon enough to save the firm from financial distress. One. Tel had always consumed cash at an alarming rate, and it had always been an act of faith to believe it could outlast its deep pocketed rivals like Telstra, Optus and Vodafone. Bibliography Barry P. , 2009. ' Who Wants to Be a Billionaire? The James Packer Story' Plessis, J. D. J. Hargovan, A. Plessis, J. D. J & Bagaric, M. , 2009. ' Principles of Contemporary Corporate Governance'. Cambridge University Press. One. Telcase study[DVD]. CPA Australia.

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