2002 – what is wrong with American corporations?

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In the early 1990's what had started as tech boom in America had the whole country (as well the world) under its spell in no time. American markets rose through most of the 90's, technology related companies sprouted like mushrooms, salary ranges sky rocketed in the many related sectors. The overall picture was a time for great hope and expectation. People trusted the big or small companies alike and preferred to invest in the stock market as much as they could afford believing that the possibility of a low or negative return was next to impossible. It was a time for dreams to come true, magic to happen. Internet business started to pick up and thousands of competing companies vied for a piece of that market. That was a time for companies to go public, to sell shares. People crazily bought shares of companies that had very little real value (assets). Companies frequently were valued by their potential in the share market, which very often reached billions of dollars. They were trusted to report the facts each quarter and the whole country waited to hear larger numbers, bigger share values. But in the mid 2000 a big chunk of that 90's success was exposed as mythical - and markets staggered back to pre-boom levels before many could even fully understand what was all the chaos about.

Declaring bankruptcy has become almost a trend lately. Companies that came into being overnight are found filing either chapter 7 (liquidation proceedings) or chapter 11 (reorganization proceedings). In the year 2000 total of 35,472 business filings were recorded in US. That number went up to 40,099 in 2001. Non-business filings took a good leap in 2001 (1,452,030) from 2000 (1,217,972). In 2002 for the first three quarters total business filings in US totaled to 28,904. Non-business filing for the same period was 1,152,101.

Among the largest 24 bankruptcies since 1980, 7 happened in 2002 and another 5 in 2001. In 2002 WorldCom Inc. declared bankruptcy on July 21st with total pre-bankruptcy asset of $103,914,000,000. The other's in the list are as following: Conseco, Inc (December 18, 2002) with pre-bankruptcy asset of $61,392,000,000; Global Crossing Ltd. (January 28, 2002) with pre-bankruptcy asset of $30,185,000,000; UAL Corp. (December 9, 2002) pre-bankruptcy asset of $25,197,000,000; Adelphia Communications (June 25, 2002) pre-bankruptcy asset of $21,499,000,000; Kmart Corp. (January 22, 2002) pre-bankruptcy asset of $14,600,000,000; NTL, Inc (May 8, 2002) pre-bankruptcy asset of $13,390,000,000. Some of the widely discussed bankruptcy had happened in just the previous year. To mention couple of them: Enron Corp (December 2, 2001) pre-bankruptcy asset of $63,392,000,000 and Pacific Gas and Electric Co. (April 6, 2001) pre-bankruptcy asset of $21,470,000,000. It is notable that most of the bankruptcy filings done by large corporations are for chapter 11, which is basically a reorganization proceeding, generally for business entities. The debtors maintain control of the business unless the Court appoints a trustee. Very few actually go for Chapter 7, which is actually liquidation proceedings; generally a trustee sell the assets and the company cease to operate.

So, clearly, even after filing chapter 11 a company may continue to operate in a normal manner, keeping the whole endeavor somewhat transparent to the consumers. Some large companies, such as those in the airline industry, have declared bankruptcy numerous times before succeeding or closing down altogether. When oil industry giant Texaco filed for bankruptcy, nobody stopped buying its gasoline. Macy's continued to have its annual Thanksgiving Day parade in New York, even when it was in bankruptcy. "In the last two decades, Americans have learned to fly on airplanes, buy from retailers, eat in restaurants, and go about their lives doing business with companies in bankruptcy," says Elizabeth Warren, a professor at Harvard Law School in Cambridge, Mass. "That changes the calculus ... for a company to file in Chapter 11."

"That's what bankruptcy is best at: handling financial mistakes. It doesn't solve operating mistakes," says Jeffrey Morris of the University of Dayton School of Law.

Texaco used bankruptcy to solve a financial problem. In 1985, it lost a court case to rival Pennzoil and was faced with an $11 billion judgment. The company declared bankruptcy and ultimately settled the suit for $3 billion. Airline TWA and the supermarket Grand Union have been in bankruptcy multiple times before being bought up by rivals. It is perceived that companies file bankruptcy as the last resource and statistics says if a company has filed once, it has a 6 to 10 percent chance of filing a second time. But many of these are large companies. Since Chapter 11 is time-consuming and incurs big costs, the small firms are often left with only viable choice - liquidation.

Perhaps 2002 will forever be remembered as the year of corporate crime. According to The Multinational Monitor the 10 worst corporations in 2002 were: ARTHUR ANDERSEN, BRITISH AMERICAN TOBACCO, CATERPILLAR, CITIGROUP, DYNCORP, M&M/MARS, PROCTER & GAMBLE, SCHERING PLOUGH, SHELL OIL, WYETH.

The 2001 list had included: ABBOTT, ARGENBRIGHT, BAYER, Coca-Cola, ENRON, Exxon Mobil, Philip Morris, SARA LEE, SOUTHERN, Wal-Mart.

The list was compiled considering not only the merit of business practices but also on the ground of ethics and humanity.

Now comes the most important question. Why the corporations fail? Corporations go bankrupt when they can no longer meet the obligations to their creditors. This is a result of some combination of unusually risky investments and unduly high debt. Bankruptcy is the limiting step in the process of reallocating capital, and the optimal number of bankruptcies is not zero. Another important problem is that both the federal and state governments have passed many laws that protect corporate management against the interests of the general shareholders. The most important of those laws is the federal Williams Act of 1968, which requires any person or group that acquires more than 5 percent of the shares of a corporation to provide extensive information within 10 days to the corporation, the exchanges, and the Securities and Exchange Commission (SEC) and increased the authority of the SEC to regulate tender offers. Following the Williams Act, the number of hostile takeovers declined in the 1970s and, following a series of court decisions and state anti-takeover laws beginning in the late 1980s, the number of hostile takeovers declined again in the 1990s. The primary protection of general shareholders against an abuse of authority by corporate management, thus, has been substantially eroded by public policy. The second simple cure for what ails American corporations, thus, is to begin to reverse this process by repealing the Williams Act of 1968.

Looking back on 2002, it is difficult not to reach a conclusion that the big corporations won. They were confronted with a crisis of epic proportions, but they still managed to survive with devastating losses and marred reputations.

After the fall of Enron both the business community and the Republican Party tried to make it an isolated case of misdemeanor by an individual company. For some time, it appeared that corporate and Republican bias would resist any meaningful legislative response to Enron until the WorldCom scandal hit. WorldCom proved beyond any doubt that corporate scandals were not isolated, and fueled the continuing downward spiral of the stock market. By summer, Republicans had shifted their rhetorical posture and showed enough willingness to make some changes. By the end of July, even House Financial Services Committee Chair Michael Oxley, R-Ohio, was forced to retreat on most of his objections to a modest accounting bill. President Bush signed it by the end of the month.

Sarbanes-Oxley bill may somewhat limit the profit-making ability of the big accounting firms, but it is clearly in the self-interest of the broader corporate class. Only a whistleblower protection provision in the bill offers the prospect of advancing broad public interest objectives. In the absence of a more significant corporate reform regulations there is virtually no challenge for the corporations regarding questionable business practices and wrongdoings in the near future.

Now, lets bring the most important players of this drama. The CEOs - a privileged group of top business people who made extraordinary personal fortunes even as their companies were heading for disaster. They made their money at the top of the market, selling shares in companies whose values rocketed in 1999 and 2000. Today their companies, many in the telecommunications sector, have crashed, destroying hundreds of billions of dollars of investor wealth and almost 100,000 jobs. Yet the executives and directors of these bankrupt companies have walked away with gross earnings of $3.3 billion, a stunning pay-off for corporate failure.

Among the barons of bankruptcy are some familiar names. Ken Lay, former chairman and CEO of Enron, grossed $247 million. Jeff Skilling, former Enron president, grossed $89 million and Gary Winnick of Global Crossing, grossed $512 million.

Wall Street had a strong start to 2003 with stocks posting their best gains in more than two months. The Dow-Jones Industrials soared 260 points following the unexpected surge in manufacturing sector. If this is any indication of a better year than hopefully America may expect to get out its current sluggish economic growth. But considering the looming war on Iraq and heavy expenditure on war against terrorism one might wonder what waits in this year for this nation, as well as the world. But it’s obvious that the Corporations will be expected to behave - not only for their shareholders but also for their customers, workers, business partners, community, nation and the wider world.