

## The next Enron? It's in the book

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Before the Enron Corp. scandal blew up, few outside the numbers-crunching world paid much heed to the inner workings of the accounting industry. Now, as distinguished accounting firms such as Arthur Andersen come under the hot glare of scrutiny, investigators are bearing down hard on the sanctioned accounting practices that companies employ - including those well within the bounds of law.

The inquiry has focused attention on what are known as U.S. generally accepted accounting practices, or GAAP. Jean-Marie Eveillard, a portfolio manager who runs several international funds for Arnhold S. Bleichroeder Inc., said these standards "give you a lot of leeway" if you are a corporate manager and have the "complicity" of your board of directors and auditors in cooking the books.

In the late 1990s, "the earnings of a great number of corporations were overstated," Eveillard said. A deep-value investor, he studies balance sheets and spent an unhappy few years disbelieving the rosy scenarios that emanated from corporate boardrooms and Wall Street.

He blamed the confluence of the GAAP standards, executive stock options and greed for creating the kind of cultures that led corporate managers to make their earnings appear significantly better than they really were.

Options distributed to a couple of dozen top executives, Eveillard said, provided them "the opportunity to be truly filthy rich if the price of the stock would go up quickly enough."

The incentive to cut corners in such cases "is enormous," he said. "It is human nature we are talking about. For them to be successful at being truly rich, they do not even have to run the risk of going to jail."

The U.S. GAAP rules are part of that problem. They are probably the most detailed in the world, and executives can take the view that everything not forbidden is permitted. Even if there is trouble afterward, it would be hard to send people to jail if they defended themselves by noting that they had complied with the GAAP standards.

Now the preoccupation in the markets is guessing what company is going to be the next Enron. There are several contenders, although it seems unlikely that anybody else would have taken creative accounting to a level that would match the accusations against the energy-trading Texas utility.

Although recent candidates for the "Enron-of-the-Month Club" have come from the United States, Eveillard is looking elsewhere, specifically Europe. "Inside America, if we are talking accounting fraud, I think there are not that many," he said. "Unfortunately, I think what has

been the prevailing practice among a great many large American corporations is pushing the envelope."

Eveillard said a growing number of European companies had adopted U.S. GAAP. A benign explanation would be that they want to present their books in a way that is easy for large American shareholders to understand, although a desire to play the GAAP game might be part of the reason as well.

Without offering names, Eveillard suggested that investors ought to take a close look at the accounting practices of European companies. Enron-like candidates may not jump out at you. The companies are likely to be healthy and may use options only sparingly, but beneath the veneer they could be operating under conditions that foster an overly aggressive corporate culture.