Trouble in FBI, Enron, World Com, More; 2002

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Roy Jenne
Sep 26, 2007
NCAR, Boulder CO
Sometimes the whistle needs to blow
(These stories are mostly for 2002)

Corporate malpractice

In praise of whistleblowers

Whistleblowing is good for society, but bad for careers. It should be good for both.

Blow the Whistle ... Then Watch Out!

A Secret Service agent blows the whistle on his agency and winds up the target of investigators

Enron

WorldCom

A Staffer Ordered To Commit Fraud Balked, Then Caved

Pushed by WorldCom Bosses, Accountant Betty Vinson Helped Cook the Books

Taking on the Navy

- The Navy had bad welds on some ships
- They could have killed people
- She complained about the bad welds
- The brass destroyed her career

May 2005
PERSONS OF THE YEAR

The Whistleblowers

CYNTHIA COOPER OF WORLDCOM
COLEEN ROWLEY OF THE FBI
SHERRON WATKINS OF ENRON

Dec 30, 2002

Time
The Year of the Whistle-Blowers

Sherron Watkins had warned Enron chairman Ken Lay about the company's shabby accounting, only to learn later that one reward considered by Enron was her firing. Coleen Rowley wrote her now famous memo blasting the FBI for how it handled the Zacarias Moussaoui case, only to receive threats for being "disloyal." And Cynthia Cooper exposed illegal bookkeeping at WorldCom, only to be alternately screamed at and patronized (and lose nearly 30 lbs. in the process).

All three had great tales to tell, but Watkins and Cooper were almost as adamant as Rowley in not wanting to speak with any reporters. Thanks to Chicago correspondent Maggie Sieger, who persuaded Rowley, and staff writer Amanda Ripley and reporter Amanda Bower, who spoke with Cooper and Watkins, the three agreed to a joint interview in Minneapolis on Dec. 7. "Rowley was intrigued by the chance to meet Cooper and Watkins," says Sieger. "Here were two other people who had tried to do the right thing, not for personal gain but to correct a wrong."

This is where three women of ordinary demeanor but exceptional guts and sense come into the picture. Sherron Watkins is the Enron vice president who wrote a letter to chairman Kenneth Lay in the summer of 2001 warning him that the company's methods of accounting were improper. In January, when a congressional subcommittee investigating Enron's collapse released that letter, Watkins became a reluctant public figure, and the Year of the Whistle-Blower began. Coleen Rowley is the FBI staff attorney who caused a sensation in May with a memo to FBI Director Robert Mueller about how the bureau brushed off pleas from her Minneapolis, Minn., field office that Zacarias Moussaoui, who is now indicted as a Sept. 11 co-conspirator, was a man who must be investigated. One month later Cynthia Cooper exploded the bubble that was WorldCom when she informed its board that the company had covered up $3.8 billion in losses through the prestidigitations of phony bookkeeping.

These women were for the 12 months just ending what New York City fire fighters were in 2001: heroes at the scene, anointed by circumstance. They were people who did right just by doing their jobs rightly—which means ferociously, with eyes open and with the bravery the rest of us always hope we have and may never know if we do. Their lives may not have been at stake, but Watkins, Rowley and Cooper put pretty much everything else on the line. Their jobs, their health, their privacy, their sanity—they risked all of them to bring us badly needed word of trouble inside crucial institutions. Democratic capitalism requires that people trust in the integrity of public and private institutions alike. As whistle-blowers, these three became fail-safe systems that did not fail. For believing—really believing—that the truth is one thing that must not be moved off the books, and for stepping in to make sure that it wasn't, they have been chosen by Time as its Persons of the Year for 2002.

Who are these women? For starters, they aren't people looking to hog the limelight. All initially tried to keep their criticisms in-house, to speak truth to power but not to Barbara Walters. They became public figures only because their memos were
May 2002

Last May, when Rowley upbraided her beloved FBI in a secret 13-page memo, she thought she was on a private rescue mission. In her view, it was not a reprimand but an act of redemption. It was not about speaking truth to power, because people like Rowley don't see much difference between the two. Truth is power—that's how you catch the bad guys.

Since Sept. 11, the 48-year-old had muzzled her grief about the bureau's failures—specifically, about how it ignored cries from her office to take seriously the case of Zacarias Moussaoui, a French-Moroccan who spoke poor English and had signed up at a local flight school, keen to fly a 747. Eight months after the attacks, Rowley and others got a chance to tell what they knew. Staff members of the House and Senate Intelligence Committees' joint inquiry into the attacks invited her and others to come to Washington for a private interview.

"I've got to remember!"

"Initially, I just started writing down points that I didn't want to miss when I was going to do my interview," she says. "I went to bed Wednesday night and was up all night, saying, 'Oh! I've got to remember to say this, got to remember that.' Thursday night I went to bed thinking, Man, am I tired. Well, I couldn't sleep all night long. The same type of thing. I've got to remember this and remember that." About 2:30 a.m. Friday, Rowley had had enough. "I said, 'This is ridiculous. I'm on 36 hours without sleep. If I jut it down, first of all I won't forget it. And I won't have to keep reminding myself of things to say. I'll get it out of my system, and I'll be able to sleep.'"

So she went to the office and sat at her desk writing until her husband Ross called 16 hours later, around 7 p.m. By Monday morning, she had written 33 pages. This is more than just my own notes to myself, she decided. And she knew the memo was explosive enough to need some protection. Just 3½ years from retirement and her family's sole breadwinner, she tacked on two sentences of self-preservation at the last minute, asking for federal whistle-blower protection. At the time, she did not know exactly what it was—nor that the

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French officials and other intelligence sources established that Moussaoui was affiliated with radical fundamentalist Islamic groups and activities connected to Osama bin Laden. Minneapolis agents pushed headquarters for approval to dig deeper, fearing—before Sept. 11—that he might be part of a larger scheme to hijack commercial jetliners. He has since been indicted as a co-conspirator.

It will never be known whether the agents could have prevented the attacks if they had received the green light earlier, Rowley is quick to point out. "But if it's at least possible we could have gotten lucky and uncovered one or two more of the terrorists in flight training prior to September 11th," Rowley wrote in her memo. And yet, three days after the attacks, Director Mueller expressed his shock that terrorists were training on U.S. soil. "The fact that there were a number of individuals that happened to have received training at flight schools here is news, quite obviously." Six days after the attacks, the rhetoric became even bolder. Said Mueller: "There were no warning signs that I'm aware of that would indicate this type of operation in the country." Worrying that the new director had not been well briefed on the Moussaoui case, Rowley and her colleagues repeatedly tried to get a message to Mueller so he could modify his statements. But they received no response. After more information about the Moussaoui investigation became public, along with a memo from a Phoenix agent who had noted a pattern of Arab men signing up at flight schools, Mueller still insisted that the FBI could not have done anything to limit or prevent the destruction. Only after Rowley's memo was made public did Mueller revisit his assessment, with a feeble double negative: "I cannot say for sure that there wasn't a possibility we could have come across some lead that would have led us to the hijackers."

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Congress angry!
BY AMANDA RIPLEY

In Clinton, Miss., the headquarters of WorldCom rises out of the moonscape of Waffle Houses and Pizza Huts like a dark steel mother ship.

Last June, Cooper told the audit committee of WorldCom's board that the company had been playing dirty with its accounting practices. She knew as she said it what would happen. Within days, the company fired its famed chief financial officer, Scott Sullivan, and told the world that it had inflated its profits by $3.8 billion—the largest accounting fraud in history. The number has since grown to $9 billion, and counting. Her colleagues have been placed in handcuffs and led past TV cameras. Shareholders have lost some $33 billion since the news broke, and soon at least...

Her division is probably the most secure at the company. And it is quite obvious that she is heartbroken. "There have been times," says Cooper, a woman not given to intense displays of emotion, "that I could not stop crying."

The next day, Cooper told the head of the audit committee about her findings, but she still held out hope that there was a reasonable explanation. She and her team began looking for ways to somehow justify what they had found in the books. Finally, they confronted WorldCom's controller, David Myers, who admitted he knew the accounting could not be justified, according to an internal-audit memo.

That's when Cooper's heart sank. Soon after, she called her mother in exhaustion. "There are some things terribly, terribly wrong at WorldCom," Patsy remembers her daughter saying. "And I was just pained at the tone of her voice." Several times Cooper told her colleagues she was concerned about what this would mean for the families of implicated WorldCom executives. "One of the things about Cynthia," says an employee who has worked closely with her, "is that if she has...

So far, Cooper says, she is encouraged by the changes at her firm. The company has carried out many of her recommendations. And she firmly believes there is a point to all of the loss. "There really is a corporate-governance revolution across the country."

But she has not been personally thanked by a single senior executive at WorldCom, her colleagues say. And there is grumbling that some employees think the company could have borrowed its way out of its problems and avoided bankruptcy if she had stayed quiet. Some people who used to smile and chat with Cooper and her team by the coffee maker don't do that anymore. "What gets me angry is that after all she has done, you would think she would be rewarded," says a friend and colleague at WorldCom. "She went through a battle, one of the biggest battles in corporate America."

Dec 30, 2002
Time
The Party Crasher

By Jodie Morse and Amanda Bower

On Feb. 13, the day before she gave the first of two damning testimonials to Congress, Enron vice president Sherron Watkins spent the afternoon in a cluttered conference room in the Rayburn House building on Capitol Hill. It was a cram session of sorts, a final chance for Watkins, her attorney and congressional staff members to review the dozens of subpoenaed documents she would be quizzed on the next morning. As they ate cold pizza, someone drew her attention to an e-mail titled “Confidential Employee Matter” that had been written by one of Enron’s external lawyers. “Per your request,” it began, “the following are some bullet points on how to manage the case with the employee who made the sensitive report.” Her eyes skipped halfway down the page: “Texas law does not currently protect corporate whistleblowers. The Supreme Court has twice declined to create a cause of action for whistleblowers who are discharged...” Her pulse quickened. “I’m reading this and I’m thinking, Oh my God, it’s [dated] two days after I met with Ken Lay. Talk about shoot the messenger. I can’t believe they looked into firing me,” she says, sounding wounded even now in the retelling. “It was a horrible response. There’s nothing in there to remind them to remember the code of conduct, the vision and values.”

This was how hard Watkins had fallen for Enron. Here she was, almost six months to the day since she first warned chairman Kenneth Lay of “an elaborate accounting hoax.” Her boss had long ago conflated her hard drive, and she had been demoted 33 floors from her mahogany executive suite to a “shabby office” with a rickety metal desk and a pile of make-work projects. The atmosphere had grown so ominous that she had called office security for advice on self-defense. But still, Watkins simply could not fathom that this company, the one she had tried to save from itself, had considered taking away the job she loved.

The next morning Watkins appeared before the tangle of cameras in her pertinential blazer, with her pastor seated directly behind her. For five hours, she patiently explained the intricacies of the financial schemes that had allowed the energy giant to conceal billions of dollars of debt in dubious partnerships. Though Watkins had not worked in accounting for a decade, she knew the arcane material cold, making it sound as simple and intelligible as long division. She was relaxed enough to give the Representatives a taste of her piercing Texas wit. But her square jaw clenched whenever she spoke about her feelings for the company. She firmly indicted several top executives, yet she insisted that Lay was a “man of integrity.” And she spoke almost wistfully of Enron’s “electric” atmosphere, of people “energized to change the world.” It was Valentine’s Day, and she was still very much in love.

For months afterward, Watkins faithfully went to work each day. In the absence of any real assignments, she could only bear witness to all that she had wrought, looking on as Enron auctioned off everything down to the sign at its headquarters (price: $44,000) and as the firm’s esteemed accountants, Arthur Andersen, went down in their own wave of scandal.

Only now, a year later, has she begun to think of fashioning a life without Enron. In November, she left her $165,000 job. But her future is shaky. She plans to start a global consulting firm to advise company boards on governance and ethics, though cases privately chuckle at the thought of opening up to the gimlet-eyed Watkins. The first to speak out,
FBI whistle-blower Coleen Rowley says her bosses blocked efforts that could have foiled some of the 9/11 hijackers

Inside: Full details of the

Were Warnings Ignored? In an explosive letter to the head of the FBI, Minneapolis agent Coleen Rowley accuses the agency of thwarting an investigation that could have helped foil some of the 9/11 hijackers.

Dear Director Mueller:

I feel at this point that I have to put my concerns in writing concerning the importance of the FBI's role in the prevention of terrorist attacks against the United States and the need to improve the response to such threats.

We have a duty to act on credible intelligence and evidence that may indicate a terrorist plot. The FBI has a critical role in gathering and sharing information with other agencies.

I believe that the FBI's response to the September 11 attacks was hampered by a culture of secrecy and a lack of cooperation with other agencies.

I have concerns that the FBI's handling of the 9/11 hijackers was inadequate. I believe that the FBI missed opportunities to intercept communications and track movements of the hijackers.

I believe that the FBI's failure to act on the information it had could have prevented the attacks.

I feel that certain facts, including the following, were not investigated thoroughly:

- The Minneapolis office's handling of the information it had on the hijackers
- The FBI's coordination with other agencies
- The FBI's response to the September 11 attacks

I urge you to take action to address these concerns and ensure that the FBI is adequately prepared to prevent future terrorist attacks.

Sincerely,

[Signature]
HOW THE FBI BLEW THE CASE

The inside story of the FBI whistle-blower who accuses her bosses of ignoring warnings of 9/11. A reading of her entire memo suggests a bracing blueprint for change

By ROMESH RATNESAR and MICHAEL WEISSKOPF
WASHINGTON

FEW AMERICANS LOVE ANYTHING about their government as much as Coleen Rowley loved the FBI. When she was in the fifth grade, Rowley wrote a letter to the bureau's headquarters in Washington and got back a booklet called 100 Facts About the FBI. From that point on, she dreamed of becoming an agent. Friends say she protested when her dean at the University of Iowa Law School refused to let an FBI recruiter on campus; she lost the battle but applied for a job on her own and was hired as a special agent after earning her law degree in 1980. She took pride in being a pioneer, part of the first wave of women fighting to be taken seriously in the bureau's male-dominated, button-down culture. She worked her way up the ladder as an FBI lawyer—handling applications for searches and wiretaps, working organized-crime cases in New York City and becoming, in 1995, chief counsel in the Minneapolis field office. She won a reputation as a highly disciplined professional, opinionated, principle and supremely devoted to her job. For seven years in the 1990s, she doubled as chief spokeswoman for the Minneapolis office, fending off the media hordes during big cases like the 1999 arrest of St. Paul housewife Sara Jane Olson, a former member of the Symbionese Liberation Army who had been on the lam for two decades. Despite the stress and the risks, Rowley, a suburban mother of four, has never worked anywhere else. She is the family breadwinner, a competitive long-distance runner, a person, by all accounts, of substance.

All of which helps explain why friends and colleagues of Rowley were impressed but not altogether surprised when she put her career on the line last week to blow the whistle on the terrible failings of her beloved FBI. "She is the kind of person who always does what is right when nobody's watching," says one friend. "That's why she came out." American life seems uniquely capable of producing stories like hers—a loyal public servant who clings to her belief in the system until a betrayal of that faith makes it impossible to stay silent. Rowley, unable to sleep at 3 a.m. one night in early May, drove to the office and wrote the first draft of a memo. She spent a week fine-tuning it, setting it aside for days, anguish and at times doubting whether she could go through with it. Summoning her courage last Tuesday, she at last fired off the 13-page letter ("from the heart," she writes) to her ultimate boss, FBI Director Robert Mueller, and flew to Washington to hand-deliver copies to two members of the Senate Intelligence Committee and meet with committee staffers. The letter accuses the bureau of deliberately obstructing measures that could have helped disrupt the Sept. 11 attacks. The FBI re-
call about Moussaoui... identified him point, [but] even after the attacks [a attempting to block the search of [his] Center attacks as a mere coincidence.
Rowley’s Diagnosis—and Mueller’s Rx for the FBI

AGENT ROWLEY charges FBI bosses for obstructing the investigation of Moussaoui’s failure to share information and misleading the public about who knew what and when. She criticizes the bureau’s culture for being too focused on chasing and prosecuting national security cases. Although the last thing the FBI or the country needs now is with hints she writes, the bureau must “come clean.”

DIRECTOR MUeller said last week that the Justice Department will pursue Rowley’s complaint and acknowledged that the agents need better access to their own files and information for investigations. Among other things, her Office of Intelligence will better analyze clues from foreign sources and a computer system upgrade. But are her remedies enough to heal the dysfunctional organization Rowley describes?

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<td>INFORMATION ISN’T DISSEMINATED</td>
<td>The director is creating a “flying squad” of investigators to drop into hot spots. His Office of Intelligence will employ more specialists to analyze raw data.</td>
<td>Mueller’s plan to centralize decision making, she says, will hurt the FBI’s ability to respond to threats.</td>
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<td>CAREERISM AND FEAR RULE</td>
<td>Management shake-up. Mueller has replaced most HQ chiefs with his own team and has divided up the deputy director’s responsibilities.</td>
<td>The agency is too small to operate at the level of expertise and resources it needs.</td>
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<td>INVESTIGATIONS ARE DELAYED by a “culture of fear” that rewards passivity, Rowley says.</td>
<td>A post-Sept. 11 law makes it easier for the feds to conduct secret, unannounced searches, get counterterrorism search warrants and tap electronic communications.</td>
<td>Field commands need to track threats and the long process of obtaining counterterrorism warrants can lead to warrantless collection of evidence.</td>
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<td>BUREAUCRATS SQUELCH AGENTS</td>
<td>Hire hundreds of new agents and assign most to fighting terrorism. Recruit people fluent in Arabic and other Middle Eastern and South Asian languages.</td>
<td>Agents are put in harm’s way, she says, and then exposed to the stigma of coming out of federal service withCounts them as failures who have been discredited.</td>
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<td>NOT ENOUGH PERSONNEL</td>
<td>A request from the Phoenix office to canvass the nation’s flight schools was dismissed for lack of manpower.</td>
<td>It’s a colossal indictment of our chief law-enforcement agency’s neglect in the face of the biggest terrorism operation ever mounted on U.S. soil. It raises serious doubts about whether the FBI is capable of protecting the public—and whether it still deserves the public’s trust.</td>
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Everyone’s first question was why? Why would an FBI agent deliberately sabotage a case? (I know I shouldn’t be flippant about this, but jokes were made that the key FBI HQ personnel had to be spies or moles, like Robert Hansen [sic], who were actually working for Osama bin Laden to have so undercut Minneapolis’ effort.)
I have deep concerns that a delicate and subtle shading/skewing of facts by you and others at the highest levels of FBI management has occurred and is occurring ... I think your statements demonstrate a rush to judgment to protect the FBI at all costs.

highest levels of FBI management has occurred and is occurring. Just 2½ years from retirement, Rowley is now fretting about reprisals, friends say. She closes her letter by acknowledging “the frankness with which I have expressed myself” and asking for federal whistle-blower protection.

Her words had an unintended resonance last week as the country tried to make sense of chilling warnings from Mueller and other top officials who rattled off a litany of “inevitable” terrorist attacks against the U.S. as if they had all just been to a screening of The Sum of All Fears. By now, most Americans know better than to feel safe, but last week the Bush Administration helpfully reminded us just how frightened we’re supposed to be. Coupled with an FBI advisory about possible al-Qaeda attacks on the Statue of Liberty and the Brooklyn Bridge, the stream of official doomsaying caused a new round of jitters in time for summer vacation.

Though uncorroborated and vague, the terror alerts were a political godsend for an Administration trying to fend off a bruising bipartisan inquiry into its handling of the terrorist chatter last summer. After the wave of warnings, the Democratic clamor for an investigation into the government’s mistakes subsided, but Rowley’s memo had members of both parties turning up the heat again. Senate majority leader Tom Daschle seized on the document as reason to appoint an independent commission to examine intelligence failures prior to Sept. 11, an idea the White House intensely opposes. Daschle says he will bring a bill to the floor of the Senate next week, when Congress returns from recess. The chairmen of the joint panel of the House and Senate Intelligence committees, which is investigating the attacks, said they will begin hearings next week. As the inquiry moves forward, Rowley is likely to become a star witness. Last week Iowa Republican Charles Grassley offered Rowley written assurance that her job won’t be jeopardized if she cooperates with the Senate’s investigations. Grassley warned Mueller to ensure that “there is no retaliation” against her.

In a star-obsessed culture, Rowley is a healthy reminder that it’s often people who shun the limelight—strong-willed people with more guts than glamour—who force themselves to step up and speak out when everyone else is keeping quiet. She dresses simply and wears large spectacles that have a habit of sliding down her nose. She takes her lunch to work every day and often arrives long before any of her co-workers. “She goes the extra mile on everything,” says Larry Brubaker, a retired agent and
PHOENIX BLUES In closed-door Capitol Hill hearings last week, FBI agent Kenneth Williams reportedly said his memo could not have prevented the 9/11 attacks

former colleague. "Coleen always looks stressed. She is very high energy." In her letter, she comes off as passionate and informed, and her controlled legal arguments are punctuated by piquant asides, dark humor and bursts of deep feeling. As her name rolled off the tongues of every politician and talking head in Washington last Friday, she remained on the job in Minneapolis and at home in a tree-shrouded cul-de-sac in Apple Valley, where she lives with her husband, four kids and 14-year-old Newfoundland. On Friday evening she made a brief appearance at the door of her home. "The situation is, I can't make any comment at all. It'll just be counterproductive," she told reporters from TIME and the Associated Press. "I don't want any publicity. The whole point is that it will be completely undercut if there is any."

As the Minneapolis field-office lawyer, Rowley had a supporting part in the drama that ended with the December indictment of Moussaoui. But she was ready the moment agents phoned her on the night of Aug. 15, 2001. Instructors at the Pan Am flight school near Minneapolis-St. Paul had phoned the FBI the previous day, reporting that a student with bad English had showed up asking for instruction in how to fly a 747. Federal agents arrived at Moussaoui's hotel on the 15th and asked for his immigration papers; when the documents showed evidence of a possible visa violation, agents from the Immigration and Naturalization Service arrested Moussaoui on charges of overstaying his visa.

With Moussaoui in custody, the Minneapolis FBI agents began hunting for information on the suspect's past. In the late 1990s, it turns out, French police had placed Moussaoui on a watch list: using London as his base, Moussaoui shuttled in and out of Kuwait, Turkey and Continental Europe, forming ties with radical Islamist groups and recruiting young men to train and fight the jihad in Chechnya. French intelligence officials also believed Moussaoui spent time in Afghanistan, and his last trip before arriving in the U.S. last February was to Pakistan. A French justice official says the government gave the FBI "everything we had" on Moussaoui, "enough to make you want to check this guy out every way you can. Anyone paying attention would have seen he was not only operational in the militant Islamist world but had some autonomy and authority as well."

A climate of fear ... has chilled aggressive FBI law enforcement action/decisions ... FBI headquarters is staffed with a number of short-term careerists ... there is unevenness in competency among headquarters personnel ... The ranks of FBI management are filled with many who were failures as street agents.
ROWLEY TO MUELLER

"We Could Have Gotten Lucky"

In the day or two following September 11th, you, Director Mueller, made the statement to the effect that if the FBI had only had any advance warning of the attacks, we (meaning the FBI) may have been able to take some action to prevent the tragedy. Fearing that this statement could easily come back to haunt the FBI upon revelation of the information that had been developed prior to September 11th about Moussaoui, and others in the Minneapolis Office, immediately sought to reach your office through an assortment of higher level FBIHQ contacts, in order to quickly make you aware of the background of the Moussaoui investigation and forewarn you so that your public statements could be accordingly modified. When such statements from you and other FBI officials continued, we thought that somehow you had not received the message and we made further efforts. Finally, when similar comments were made weeks later, in Assistant Director Caruso's congressional testimony in response to the first public leaks about Moussaoui, we faced the sad realization that the remarks indicated someone, possibly with your approval, had decided to circle the wagons at FBIHQ in an apparent effort to protect the FBI from embarrassment and the relevant FBI officials from scrutiny.

Everything I have seen and heard about the FBI's official stance and the FBI's internal preparations in anticipation of further congressional inquiry, has, unfortunately, confirmed my worst suspicions in this regard. After the details began to emerge concerning the pre-September 11th investigation of Moussaoui, and subsequently with the recent release of the information about the Phoenix memo, your statement has changed ... the official statement is now to the effect that even if the FBI had followed up on the Phoenix lead to conduct checks of flight schools and the Minneapolis request to search Moussaoui's personal effects and laptop, nothing would have changed and such actions certainly could not have prevented the terrorist attacks and resulting loss of life. With all due respect, this statement is as bad as the first! It is also quite at odds with the earlier statement (which I'm surprised has not already been pointed out by those in the media!) I don't know how you or anyone at FBI Headquarters, no matter how much genius or prescience you may possess, could so blithely make this affirmation without anything to back the opinion up (other than your stature as FBI Director. It is thus, as with most predictions ... no one will ever know what impact, if any, the FBI's following up on those requests, would have had. Although I agree that it's very doubtful that the full scope of the tragedy could have been prevented, it's at least possible we could have gotten lucky and uncovered one or two more of the terrorists in flight training prior to September 11th, just as Moussaoui was discovered ...

See time.com for an edited version of the 13-page memo.
T H E  W H I S T L E - B L O W E R

among other things, the search turned up crop-dusting information, a letter to Moussaoui from an al-Qaeda operative in Malaysia and a notebook that contained an alias eventually traced to the roommate of hijacker Mohamed Atta.) According to Rowley, the supervisor has since been promoted. FBI officials refused to comment on the tampering charge last week; Mueller also demurred, passing the contents of the memo to the Justice Department's inspector general.

Rowley admits that she is outspoken—"those who know me would probably describe me as, by nature, overly opinionated and sometimes not as discreet as I should be"—but her memo is bound to strike a nerve with other FBI agents, who have long complained about the careerist, risk-averse approach of the desk jockeys in the Hoover Building. It's hard not to conclude after reading her account that the FBI's sprawling bureaucracy is hopeless. "Career enhancement," she writes, supersedes law-enforcement concerns at the headquarters, which is staffed by agents with little field expertise serving short, 18-month terms and others so eager to rotate out to the field that they keep their heads down. Among field agents, the bureau's byzantine process of reviewing RSA requests is notorious. Says one retired field officer: "You send your application to headquarters, and they'll sit on it so long and keep it for weeks and weeks ... then you have to do it all over again. It's like a catch-22."

As Washington's cycle of blame spun up again last week, the official caught in the blades was Robert Mueller, who until now has impressed many critics with his intelligence, energy and commitment to reform. Though the director did not comment on the specifics of the Rowley memo, he issued a statement that signaled he is serious about fixing his broken institution. "I am convinced that a different approach is required," he said. "There is no room for the types of problems and attitudes that could inhibit our efforts." One of his ideas is to create a new "flying squad" of terrorist specialists based in Washington—but longtime field agents, like Rowley herself, are ap-

we discern that there was a plot that would have led us to Sept. 11? No. Could we have? I doubt it." But in its most searching passage, Rowley's letter lays out the case that the FBI made fateful miscalculations by failing to see a possible connection between the Minneapolis investigation of flight student Moussaoui and the bunch of Phoenix agent Kenneth Williams—posed in a report to HQ two months earlier—that al-Qaeda operatives were attending U.S. flight schools. Law-enforcement and congressional sources told Time that both reports landed on the desk of Dave Frasca, the head of the FBI's radical-fundamentalist unit. The Phoenix memo was buried; the Moussaoui warrant request was denied.

In Rowley's admittedly speculative view, more decisive action might have enabled the authorities to put the pieces together in time. FBI counterterrorism officials continue to dispute that line of reasoning. They doubt Moussaoui was the 20th hijacker: there is no hard evidence that any of the 19 hijackers communicated with Moussaoui, and he showed up for flight school months after the others had completed their training. (They have a darker worry: that he was on an entirely different suicide mission and that his cell mates are still at large.) And the survey of flight schools proposed by Williams would have had a hard time identifying Atta and his cadre, who were done with school and gearing up for Sept. 11.

"No one will ever know what impact, if any, the FBI's following up of these requests might have had," Rowley writes. In a way, she's right—for every American, what might have been will be maddeningly, eternally unknowable. But Rowley has at least forced the FBI and the Administration to confront their failures directly and publicly, rather than sweep them under a self-stitched rug of wartime immunity. The congressional investigations may yet get bogged down in finger pointing and political grandstanding, but for now they represent the main opportunity to learn the lessons that could help guard against the next 9/11. Before Rowley came along, the Administration had succeeded in derailing such inquiries by calling them unproductive and suggesting that its critics might be unpatriotic. Last week a patriot came forward to help steer the country back toward the truth.

—Reported by Michael Duffy and Elaine Shannon/Washington, Maggie Sieger/Minneapolis and Bruce Cumley/Paris

F I R E D  U P  T h e letter lit a fuse under Senators Shelby and Graham, above, and Rep. Pelosi, but Bush opposes an independent inquiry palled by the plan. In their view, anything that shifts more power to the Hoover Building will only reinforce the culture of fear and indecision that the hijackers managed to exploit. Rowley wrote to Mueller, "Your plans for an FBI headquarters 'super squad' simply fly in the face of an honest appraisal of the FBI's pre-September 11 failures."

It's likely Mueller will have plenty more accounting to do. He has already been pressed to explain why the FBI did not investigate Moussaoui more aggressively; on May 8, he told members of the Senate Judiciary Committee that the lead Minnesota case agent "did a terrible job in pushing as hard as we possibly could with Moussaoui. But did
Abu Zubaydah has shared some valuable information, says a senior U.S. intelligence source. "He's not b.s.ing us on everything." Then again, says Congresswoman Nancy Pelosi, senior Democrat on the House Intelligence Committee, "he is also very skilled at avoiding interrogation. He is an agent of disinformation."

But Abu Zubaydah's statements jibe with claims made by other detainees in Guantanamo Bay, Cuba, that landmarks may be struck during holidays—a strategy also endorsed by al-Qaeda training videos. Meanwhile, agents had noticed an increase in terrorist "chatter" picked up by telecommunications surveillance in recent months. "We couldn't just blow it off," says the senior intelligence official—especially given the firestorm over whether agencies could have done more to prevent 9/11. "How many times did someone get in trouble for issuing a warning that didn't happen?" a U.S. counterterrorism official asks rhetorically.

So the call was made to New York City, but the ambiguity persisted. "We never viewed it as a warning or an alert, like, 'The bridge is going to get hit within the next two days,'" says an FBI official. "It was more like, 'Out of an abundance of caution, we're telling you this.' It was just historical, lower-priority stuff." New York Police Department representatives on the task force passed along the information to their supervisors, who called N.Y.P.D. commissioner Raymond Kelly. He decided to post officers at both the statue and the bridge and make random checks of cars entering the city. On Tuesday, reporters inquired about the police presence. Kelly thought the FBI was going to publicize the advisements, according to deputy police chief Michael Collins, and he had been given permission by the local FBI office to tell the press himself, which he did. Sometime late Tuesday evening, the FBI posted a short statement on its website confirming the warning.

On Wednesday, however, FBI spokesman Joseph Valiquette said the bureau never intended to make the information public. And Bush Administration officials have privately said they are furious with New York officials. "There are some things the general public has to know, and quite frankly, there are some things they don't have to know."

TIME/CNN POLL

Several Bush Administration officials have warned that additional terrorist attacks may occur in the U.S. at any time. How much attention have you paid to these warnings?

A great deal

Just a little

None at all

Based on warning

To divert attention

How much confidence do you have in the吓en or the FBI to prevent future terrorist attacks in the U.S.?

A great deal

Just a little

Not much

None at all

CIA

FBI

It's inevitable. There will be another attack. We will not be able to stop it. I wish I could be more optimistic."
Chief says FBI wasn’t aggressive

Robert Mueller says agency might have been able to detect terror attacks

By Eric Lichtblau and Josh Meyer
Los Angeles Times

WASHINGTON — FBI Director Robert S. Mueller III acknowledged Wednesday that in the weeks before Sept. 11 the bureau failed to aggressively pursue “red flags” in Minnesota and Arizona that could have led investigators to the terrorist hijackers.

Mueller’s concession was at odds with the Bush administration’s previous assertions that authorities could not have done anything to disrupt the attacks. And it came as the FBI disclosed that it had unearthed two additional memos indicating that authorities may have missed terrorist warning signs.

In a 1998 memo, an FBI pilot in Oklahoma City reported to his supervisor that he was suspicious about the “large numbers” of Middle Eastern men receiving flight training at area airports. The pilot said the “recent phenomenon” could be related to “planned terrorist activity.” The supervisor who received the memo did not report the suspicions to Washington at the time, and the matter was never investigated, a senior FBI official said.

In a second memo, intelligence officials reported that a Middle Eastern nation had tried to buy a flight simulator in violation of U.S. restrictions. FBI officials on Wednesday did not divulge the date of that memo or the country that tried to buy the simulator. They did say that both documents had both been forwarded to members of Congress who are examining why the U.S. intelligence community failed to detect the Sept. 11 attacks in advance and whether warnings were missed.

Please see FBI on 4A
Although FBI officials downplayed the significance of the two new memos, they appear to fit a pattern of what Mueller described as missed opportunities and lax counterterrorism analysis. Acknowledging that "we must change," he unveiled an FBI reorganization plan that he said was aimed at developing a more aggressive, proactive approach to pursuing terrorism leads and preventing future attacks.

"There was not a specific warning" (before Sept. 11) about an attack on a particular day. But that doesn’t mean that there weren’t red flags out there, there weren’t dots that should have been connected to the extent possible," a contrite and sometimes defensive Mueller told reporters in an extraordinary two-hour briefing. He acknowledged that he himself had unwittingly misspoken last fall in denying the existence of pre-Sept. 11 warnings.

The jury's still out on whether the FBI could have done anything to detect what was going to happen on Sept. 11, he said. Had the bureau done a better job of following up on leads around the country, he said, "I can't say for sure that there wasn’t a possibility that we would come across some lead that would have led us to the hijackers."

The FBI has come under blistering attack in the last several weeks following disclosures that bureau officials in Washington failed to act last summer either on a warning from an agent in Phoenix about suspicious Middle Eastern flight students or on efforts by agents in Minneapolis to get a search warrant for the computer and personal belongings of flight student Zacarias Moussaoui, who was being held on immigration violations.

In a letter to Mueller last week that has stoked the flames, Coleen Rowley, the general counsel for the FBI in Minneapolis, said officials at headquarters had set up a “roadblock” that prevented her office from pursuing suspicions that Moussaoui was a terrorist.

Moussaoui, who authorities now think was planning to be the “20th hijacker,” was charged after the attacks with conspiracy and faces the death penalty.

In his briefing Wednesday, Mueller thanked Rowley repeatedly for her critique and said her letter “points squarely to a need for a different approach” toward counterterrorism.

Mueller, a longtime prosecutor who took over the FBI a week before the attacks, continued to insist that no single episode in Minnesota, Arizona or anywhere else could by itself have led investigators to the Sept. 11 plot. But, he said, “putting all the pieces together over a period of time, who is to say?”

The Phoenix and Minneapolis investigations were both routed through the same FBI office in Washington — the Radical Fundamentalists Unit — but authorities say the unit chief never saw the Phoenix flight-training memo before Sept. 11.

The Phoenix memo, recommending that the FBI canvass flight schools around the country to search for suspicious Middle Eastern students, was remarkably similar to the Oklahoma City bombing.
WASHINGTON — Saying that the FBI's own rules have provided terrorists with a "competitive advantage," Attorney General John Ashcroft on Thursday unveiled new guidelines that will permit agents to more freely conduct surveillance at libraries, political rallies and religious gatherings, surf the Internet and mine commercial databases for information.

The new rules give FBI agents the power to attend public events open to any other citizen to seek signs of terrorism. Ashcroft noted that state and local police already do this.

The changes give the FBI — whose primary mission now is preventing terrorist attacks — greater ability to gather the intelligence it needs, he said. They loosen guidelines imposed after FBI domestic spying scandals of the 1960s and 1970s.

"Men and women of the FBI in the field are frustrated because many of our own internal restrictions have hampered our ability to fight terrorism," Ashcroft declared. "The current investigative guidelines have contributed to that frustration."

But the rule changes, which take effect immediately, quickly drew sharp criticism from civil liberties groups, political activists and some members of Congress, who said they could encourage snooping without cause and a return to the kind of abuses for which the regime of then-FBI Director J. Edgar Hoover became infamous.

"Americans have not forgotten the abuse of civil liberties which took place in the '60s and '70s under the name of law enforcement," said Rep. Dennis Kucinich, D-Ohio. "We have to make sure that civil liberties are not placed in jeopardy."

Laura Murphy, director of the national office of the American Civil Liberties Union, contended that the FBI already has enough authority to develop terrorism cases. "They are taking advantage of the public's concern about 9/11 ... and they are rushing in a whole new set of powers," she said.

Ashcroft said the new guidelines include safeguards limiting domestic surveillance to matters involving terrorism and barring the retention of nonrelevant information. President Bush also vowed that civil liberties would be protected, telling reporters earlier in the day that "the initiative that the attorney general will be outlining today will guarantee our Constitution, and that's im-

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Continued from 1A

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• Guidelines are not likely to run afoul of federal courts. Page 12A

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Please see GUIDELINES on 3A

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Sometimes the whistle needs to blow
(These stories are mostly for 2002)

Corporate malpractice
In praise of whistleblowers

Whistleblowing is good for society, but bad for careers. It should be good for both

Blow the Whistle… Then Watch Out!

A Secret Service agent blows the whistle on his agency and winds up the target of investigators

Enron

WorldCom

A Staffer Ordered To Commit Fraud Balked, Then Caved
Pushed by WorldCom Bosses, Accountant Betty Vinson Helped Cook the Books

Taking on the Navy

- The Navy had bad welds on some ships
- They could have killed people
- She complained about the bad welds
- The brass destroyed her career
In praise of whistleblowers

When Philip Bowman was chief financial officer of Coles Myer, an Australian retailer, he exposed the fact that a vice-chairman had used a big chunk of the retailer’s money to buy shares in a company that he, the vice-chairman, controlled. The case made headline news. Yet even after a two-year court battle to win compensation for wrongful dismissal, Mr Bowman was, in effect, ostracised from working in his home country. He says that companies that might have hired him worried about skeletons lurking in their own cupboards.

Yet Mr Bowman was lucky: he moved to Britain and subsequently became chief executive of Allied Domecq, the world’s second-largest wines and spirits group. Sadly, few whistleblowers’ stories end so happily. Many ruin their careers, and sometimes even their health. Because of society’s aversion to people who are often seen more as snitches than as heroes, those who blow the whistle (and put up with the persecution and harassment that almost invariably follow) have to be abnormally persistent. They become obsessive about their cause and blind to other aspects of their life. Many end up pursuing personal vendettas as well as the wrongdoing that originally sparked their action.

Whistleblowers provide an invaluable public service. An employee who (to quote Black’s Law Dictionary) “reports illegal or wrongful activities of his employer or fellow employees” can save his organisation millions, quite apart from carrying out his public duty. The American government claims that going on.)

Employers themselves are reluctant to provide such an environment, although there are some notable exceptions (see page 55). Such an attitude is understandable: whistleblowers rarely bear good tidings for a company’s share price. Yet in the long run they can save their employers far more than they cost, for instance by uncovering embezzlement. Even in cases such as price-fixing or cartels, where revelations by whistleblowers may unequivocally damage a company, it can be better to provide a forum that stops the practice without the glare of publicity that comes when trustbusters knock on doors at dawn.

This month, Britain’s financial-services regulator is setting up a hotline for whistleblowers. Uniquely, British law sees a substantial role for regulatory bodies acting as an independent outside party that is at the same time discreet and knowledgeable about industry practices. In America, there is legislation in the pipeline designed to speed up the processing of whistleblowing cases. More legislation and more independent intermediaries are certainly welcome. But ultimately the answer is for employers, in both private and public sectors, to learn to appreciate the merits of whistleblowing, and to reward genuine whistleblowers with promotion rather than the sack. They might even then eliminate the malpractices that trouble their conscientious employees in the first place—and what a good thing that would be.
Tell Management about problems
(Then what happens?)

- Some are quickly fired
- Some are moved to a distant office

Dec 2003
Roy Jensen
Boulder, Colo

Page 20
Letters to the Editor

Blow the Whistle . . . Then Watch Out!

In response to Joann Lublin's Managing Your Career column "Saving Your Career After Earning a Name As a Whistle-Blower," Feb. 5.

In most states, a whistle-blower is recognized only as someone who has exposed illegal activities within a governmental organization and not privately or publicly held companies. Folks such as Sherron Watkins at Enron are rarely given a special status or legal protection merely for uncovering an ugly practice or incident, legal or not.

After only four months in a management position at a large Fortune 500 firm, I discovered within my department an unethical practice and culture of soliciting from and accepting lavish gifts from vendors and suppliers in exchange for favorable consideration and favoritism in purchasing decisions and contract negotiations.

When I confronted management on the issue and its clear violation of company rules and basic business ethics standards, I was quickly escorted to the parking lot where the parking decal was scraped from my car and my company I.D. confiscated. I was history.

Short of attempting to create a shareholder lawsuit against the company over the cost of such fiscally and ethically unsound policies, I had no rights or means to appeal my firing.

I've certainly had my share of awkward moments in subsequent job interviews when attempting to explain this experience. Corporate whistle-blowers do indeed face a rocky path, and little recourse, in the current climate of morally declining business cultures.

Jack Liles
Atlanta

Jack saw unethical practices
He objected
And was quickly fired

Wall Street Journal
CHRISTINE CASEY'S heart was in her mouth when she telephoned the Securities and Exchange Commission (SEC) in September 1999. Over the previous nine months, Ms Casey was later to declare in court, she had come to believe that her employer, Mattel, was misleading its shareholders about its likely future sales performance. As she picked up the phone, she imagined federal agents at her doorstep, daring undercover missions to gather evidence and, ultimately, respect for making her company better. Three years later, she has lost her job and (because big American employers routinely check applicants' litigation histories) any chance of getting another like it. She also lost the lawsuit she brought against Mattel for wrongful dismissal—and Mattel is now petitioning the court in the hope of recovering its legal costs from her.

Not long ago, it was celebrity bosses whose balking pates and bulging waistlines filled the covers of America's news magazines. Now those same magazines showcase the whistleblowers who are packing the bosses off to jail. Last month, Time put three female whistleblowers—from Enron, WorldCom and the FBI—on its cover, as its "Persons of the Year". Business Week declared that it would "not be too cliche" to call 2002 the "Year of the Whistleblower", and cheerfully looked forward to a new age of squealing on the boss. Yet however heart-warming, this optimism depends crucially on the balance of incentives on offer to those who are brave (or foolhardy) enough to blow the whistle.

Ms Casey's experience is not encouraging. She joined Mattel, a big toymaker, in 1994. In 1997 the company put her to work developing a system to allocate production among its factories. But Ms Casey soon discovered a bigger problem: Mattel's official sales forecasts were so high that managers, who were meant to use them to plan production, routinely ignored the numbers. It was "a joke around the office," she says. Some managers kept two sets of figures, Ms Casey's documents show. Others would ring around to find out what they should really tell their factories to produce. The problem was most acute for Mattel's most profitable product: a pink plastic doll called Barbie.

The toy industry can be a treacherous business. "Your customers are two feet tall, their tastes are hard to determine, and they don't have a lot of money," as Ms Casey puts it. But Barbie's enduring success had turned Jill Barad, the doll's chief marketer, into a star. By 1997, it had propelled her right to the top of the company. By then, however, Barbie's fortunes were peaking. What Ms Casey saw—as early as late 1997—clearly pointed to falling demand. Yet Ms Barad, who was relying on the company's internal sales forecasts to make public profit forecasts, kept reassuring shareholders and remained upbeat through 1997, 1998 and for a good part of 1999. Mattel denies that its sales forecasts were inflated during that period, and says that the earnings guidance it gave was based "upon management's best judgment of the market place at the time".

In February 1999, Ms Casey approached Ned Mansour, a Mattel director. She had a proposal, she told Mr Mansour, that would fix the inflated numbers and help Mattel to forecast profits more accurately. At first, Mr Mansour appeared to be friendly. As Ms Casey persisted with her idea, however, the company grew hostile, she says. In August, one executive called her into his office and screamed at her, telling her he wanted her "out". The same month, she got a negative performance review. All previous reviews had been full of praise.

Mattel then stripped her of most of her work and put her in a cubicle next to a pile of packing boxes. In October, she wrote to Mattel's former chief financial officer, Harry Pearce, expressing her concern that "misrepresentation of earnings projections has made the company vulnerable to shareholder litigation". Having failed to get Mattel's human-resources department interested in her treatment (on the contrary, they harassed her as well, she says), she declined to negotiate an offer of money from Mattel to waive her legal rights, and resigned the following month.

Little support from the law
In November 2000, Ms Casey filed suit against Mattel. Mattel hired John Quinn, a lawyer famous for fighting (and winning) business lawsuits. Mr Quinn portrayed Ms Casey as a grasping, self-interested career woman who would do anything to climb the corporate ladder. Last September, the judge ruled in favour of Mattel, finding that Ms Casey's treatment was not sufficiently intolerable to warrant a finding of constructive discharge, and that she was not protected by whistleblower laws because she had made proposals to senior management instead of explicit complaints. Ms Casey is appealing.

Mattel has not escaped entirely unharmed, however. Last month, the company settled shareholder lawsuits (which had alleged deliberately misleading inflation of sales forecasts) for $122m, but without acknowledging any wrongdoing. Ms Barad left Mattel in February 2000, with $50m in her pocket. Mr Mansour left the following month, with $5.8m. Ms Casey, on the other hand, appears to have failed to get her information even properly looked at by the SEC. In its latest correspondence, dated December 4th, the agency advises her to contact the commission's "office of investor education".

Under legislation passed last summer, managers face stiff new penalties—including the possibility of long jail sentences—for retaliating against whistleblowers. The new laws also beef up the board's audit committee as a conduit for internal complaints. Ms Casey says that what is really needed is a responsive outside investigator, anonymity, protection from former employers and, above all, the potential to earn a large reward for a job that, she now knows, can carry a heavy cost. So far, she has nothing to show for her efforts except regrets.
The European Commission has never fully recovered from the corruption scandal that forced its then members to resign en masse in 1999. Stories of false contracts, lax financial controls, complacency and cronyism crystallised much of the public distrust of the “Brussels bureaucracy”. Romano Prodi, who took over as head of the commission later that year, promised that henceforth there would be “zero tolerance” of corruption. But now a new scandal has broken, containing several of the elements that brought down the Santer commission four years ago.

Earlier this year the European Union’s anti-fraud office, OLAF, alerted French prosecutors to a “vast enterprise of looting” at Eurostat, the commission’s statistical service. Senior managers, said OLAF, had set up secret bank accounts and funnelled EU cash through them to contractors, including companies that they themselves had helped set up and whose boards they sat on. The worth of these contracts was sometimes artificially inflated; others may have been for work that was entirely fictitious. Over €300,000 ($340,000) was siphoned off into “black accounts”.

The commission was first alerted to trouble at Eurostat years ago—and barely stirred. One official who complained about dubious contracts was sucked into a costly legal action. When she asked the commission for support, it was refused; she later had a nervous break-down, retiring on an invalidity pension at the age of 37. Almost three years passed before Michaela Schreyer, the budget commissioner, read one crucial memorandum on the goings-on at Eurostat. The commissioner nominally in charge of it, Pedro Solbes, has refused to accept responsibility, telling the European Parliament this month that he could not be held accountable “for things I didn’t know about”. The unimpressed parliamentarians have now summoned Mr Prodi to testify before them in September. Belatedly, the commission is getting tough: on July 23rd it announced that it had cancelled contracts with four of Eurostat’s preferred partners, besides launching an investigation into which other commission departments might have been running black accounts.

So is this just further confirmation of the popular prejudice that the Brussels bureaucracy is rife with corruption and incompetence, a gurgling drain choked with European taxpayers’ hard-earned cash? Unsurprisingly, things are a bit more complex than that. It is not certain that the black accounts set up by Eurostat were used for the personal enrichment of the officials involved. The most pernicious activity so far proven is illicit funding of a staff volleyball team. Officials familiar with the investigation think that these accounts may originally have been set up to give Eurostat a way to pay for research quickly, without going through the commission’s cumbersome procedures. But there is also a strong suspicion that, even if the secret accounts were at first intended to serve a relatively virtuous purpose, they may have been used as time went on. As one investigator puts it, “Once you step outside the established procedures, you lose the presumption of innocence.”

The whole tortuous tale shows that it is not true that the commission is indifferent to fraud. Alas, things are worse than that. The commission has elaborate procedures to prevent financial irregularities. But these have not just proved insufficient; indirectly, they may actually have made the problem worse. Driven crazy by the amount of form-filling and box-ticking required of them, commission officials have got used to cutting corners. Further investigations may demonstrate that Eurostat’s black accounts were by no means unique in the EU’s bureaucracy. And once people get into the habit of doing things off the books, the road to perdition is wide open.

There is little doubt that in some ways EU financial regulations are ridiculously cumbersome. Aid projects run by the commission have been notoriously slow in delivering the money they promise to worthy causes. Officials in the commission’s research department complain that many top European scientists cannot be bothered to apply for EU money, because of the number of bureaucratic hoops they have to jump through. “Nobody can really follow all the rules,” complains one senior official, “there are just too many. It took three years for my department to find a way to buy in outside data.”

Yet while the commission is top heavy with rules and regulations, it lacks a culture of responsibility. As Mr Solbes’s words to the European Parliament demonstrate, nobody seems willing to say “the buck stops here”. Arguably, he, whose most pressing task is to keep life secure for the euro, should have been able to rely on his senior officials to crack down on malpractice in a statistics bureau in Luxembourg. But an official familiar with the Eurostat investigation argues that “the big problem is that there is nobody in the commission who has the responsibility and power to say that a given practice is unacceptable or a given person must be fired.” Instead the buck is passed, memorandums are left unread and investigations drag on for years—until the press or the European Parliament get hold of them.

Plus ça change...

After the last big scandal, the European Commission promised a radical overhaul of the way it worked. Fresh procedures were put in place, a new anti-fraud office was set up, and whistle-blowers were promised special protection. But many of the conclusions of the external investigation into that scandal still ring uncomfortably true. It argued that “the multinational character of the commission itself lies at the heart of some of its problems”, creating not only “differences in the interpretation of procedures” but also “unhealthy national allegiances that can cut across the formal structures of the commission”. The report concluded that it was difficult to find anyone in the commission with “the slightest sense of responsibility” for financial control. Four years on, how much has really changed?
The Party Crasher

BY JODIE MURSE AND AMANDA BOWER

On Feb. 13, the day before she gave the first of two damning testimonials to Congress, Enron vice president Sherron Watkins spent the afternoon in a cluttered conference room in the Rayburn House building on Capitol Hill. It was a cram session of sorts, a final chance for Watkins, her attorney and congressional staff members to review the dozens of subpoenaed documents she would be quizzed on the next morning. As they ate cold pizza, someone drew her attention to an e-mail titled “Confidential Employee Matter” that had been written by one of Enron’s external lawyers. “Per your request,” it began, “the following are some bullet thoughts on how to manage the case with the employee who made the sensitive report.” Her eyes skipped halfway down the page: “Texas law does not currently protect corporate whistle-blowers. The Supreme Court has twice declined to create a cause of action for whistle-blowers who are discharged…”

Her pulse quickened. “I’m reading this and I’m thinking, Oh my God, it’s [dated] two days after I met with Ken Lay. Talk about shoot the messenger. I can’t believe they looked into hiring me,” she says, sounding wounded even now in the retelling. “It was a horrible response. There’s nothing in there to remind them to remember the code of conduct, the vision and values.”

This was how hard Watkins had fallen for Enron. Here she was, almost six months to the day since she first warned chairman Kenneth Lay of “an elaborate accounting hoax.” Her boss had long ago confounded her hard drive, and she had been demoted 33 floors from her mahogany executive suite to a “skanky office” with a rickety metal desk and a pile of make-work projects. The atmosphere had grown so ominous that she had called office security for advice on self-defense. But still, Watkins simply could not fathom that this company, the one she had tried to save from itself, had considered taking away the job she loved.

The next morning Watkins appeared before the tangle of cameras in her periwinkle blazer, with her pastor seated directly behind her. For five hours, she patiently explained the intricacies of the financial schemes that had allowed the energy giant to conceal billions of dollars of debt in dubious partnerships. Though Watkins had not worked in accounting for a decade, she knew the arcane material cold, making it sound as simple and intelligible as long division. She was relaxed enough to give the Representatives a taste of her piercing Texas wit. But her square jaw clenched whenever she spoke about her feelings for the company. She firmly indicted several top executives, yet she insisted that Lay was a “man of integrity.” And she spoke almost wistfully of Enron’s “electric” atmosphere, of people “energized to change the world.” It was Valentine’s Day, and she was still very much in love.

For months afterward, Watkins faithfully went to work each day. In the absence of any real assignments, she could only bear witness to all that she had wrought, looking on as Enron auctioned off everything down to the sign at its headquarters (price: $44,000) and as the firm’s esteemed accountants, Arthur Andersen, went down in their own wave of scandal.

Only now, a year later, has she begun to think of fashioning a life without Enron. In November, she left her $365,000 job. But her future is shaky. She plans to start a global consulting firm to advise company boards on governance and ethics, though now privately chuckle at the thought of opening up in the gimlet-eyed Watkins. The first to speak out,
In the line of fire

A Secret Service agent blows the whistle on his agency and winds up the target of investigators

BY CHITRA RAGAVAN

Carter Kim has spent nearly two decades chasing bad guys. The former Honolulu cop and 18-year Secret Service veteran earned top reviews and cash awards of some $13,000 for his work busting counterfeits and forgeries. He served on the elite presidential protective detail. Today, he’s the subject of an internal Secret Service investigation.

Kim’s case is a doozy. The charges range from lost evidence to sloppy fieldwork to coverups. It could lead to the end of a top officer’s career. But it could also smear the reputation of the historic Treasury Department agency best known for protecting the life of the president. In the past few years, the role of the Secret Service has grown enormously, to include high-profile missions like security operations for the Super Bowl and the Olympics in Salt Lake City. But the higher profile has brought embarrassment. At the Olympics, agents left plans for protecting Vice President Dick Cheney at a souvenir shop. The service also is fighting a federal discrimination lawsuit filed by more than 250 African-American agents. And now, U.S. News has learned, the service is embroiled in a controversy involving its trademark mission: investigating counterfeiting.

That was the work Kim performed, as head of criminal investigations, at the Secret Service field office in Las Vegas—and which led the 43-year-old Korean-American to file an Equal Employment Opportunity lawsuit in March. He’s charging that the agency discriminated against him because of his race. Spokesman Mark Connolly said the agency would not comment on a pending case. At the heart of the matter—according to interviews and Kim’s three sworn statements to the Secret Service Equal Employment Office, the U.S. Office of Special Counsel, and the Secret Service inspection division—is his charge that the Secret Service mis-treated him after he blew the whistle on an alleged coverup of missing evidence in the Vegas field office.

In his filed EEO complaint, Kim says that he told his boss, Special Agent in Charge Joseph Saitta, that security for the office’s evidence vault was lax. Entry logs, which tracked access to the vault, were incomplete. The vault was left unlocked at night. Kim had complained of other security lapses for three years. “The office was crashing and burning,” says Kim. For example, he claims that STU-keys—classified encryption devices inserted into secure telephones—were rarely locked up.

In November, the Treasury Department’s inspector general alerted the Las Vegas office that an audit was imminent. Kim alleges in his EEO complaint that Saitta told the agents not to volunteer information because “we have a one-voice policy” and Saitta was that voice. Saitta declined to comment for this story, saying he was unfamiliar with the complaint. Kim charged in a signed sworn statement before three Secret Service inspectors that, as the agents prepared for the audit, Saitta told him to create fictitious documents to hide the gaps in the entry logs. Kim says he obeyed reluctantly. "The general culture of the Secret Service is you don’t tattle on your boss," says Kim. He says he made sure the fake logs were never used.

Faking it. More problems were discovered: Counterfeit money, turned in by Vegas banks and casinos, went missing. Also missing were items from a "speech kit"—including fake money—that agents use to teach casinos to spot forgeries. Kim alleges, in his statement to inspectors, that Saitta told an agent to mark the missing items from the speech kit as destroyed. Even evidence seized from forgers and counterfeitors—a laptop computer, keyboards, and computer peripherals—couldn’t be found. Kim charges in the discrimination complaint that Saitta ordered agents to scour the office for substitute equipment that could pass for evidence—and that Saitta even joined in the search. Before the audit, Kim, on his own initiative, says he ordered an agent to remove all the fakes. Even so, the audit found problems with the handling of evidence. Afterward, Kim set about trying to correct then.

End of story? Not quite. With the Secret Service’s internal-affairs division visited Las Vegas in March for a routine inspection, Kim says he blew the whistle. A few weeks later, as Kim was preparing security arrangements for a visit to Las Vegas by former President George Bush, he found inspectors waiting for him. Kim says the agency is trying to nail him for the alleged coverup. "They took away my badge and my gun," says Kim. Kim was placed on administrative leave. Saitta has retired with full benefits. “Here’s a guy who tried to do the right thing, and he’s the one they’re hanging," says Ronald Schmidt, one of Kim’s attorneys. Kim says he deeply regrets joining the Secret Service. "I never ever thought my career would end like this."
Over the Line

A Staffer Ordered To Commit Fraud Balked, Then Caved

Pushed by WorldCom Bosses, Accountant Betty Vinson Helped Cook the Books

A Confession at the Marriott

By Susan Pulliam

JACKSON, Miss.—Betty Vinson has always kept her life well ordered. She posts one list on the refrigerator of what she needs to buy at Wal-Mart and another for the grocery store. She keeps a list of the clothes she wears to work so she doesn’t repeat outfits too often. The daughter of the former owner of a small typewriter shop, she is known among her friends for her spicy Texas chili.

In 1996, she took a job as a midlevel accountant at a small long-distance company. Five years later, her solid career took a sudden turn in a very sorry direction. Today Ms. Vinson, 47 years old, is awaiting sentencing on conspiracy and securities-fraud charges. She has begun to prepare her 12-year-old daughter for the possibility that she will go to jail.

The long-distance company grew up to be telecom giant WorldCom Inc., which melted down last year in an $11 billion fraud, the biggest in corporate history. Asked by her bosses there to make false accounting entries, Ms. Vinson balked—and then caved. Over the course of six quarters she continued to make the illegal entries to bolster WorldCom’s profits at the request of her superiors. Each time she worried. Each time she hoped it was the last time. At the end of 16 months she had helped falsify at least $3.7 billion in profits. Ms. Vinson refused to talk about her work for WorldCom or the case against her.

Ms. Vinson and two colleagues ended up confessing their accounting sins to federal officials in a Courtyard Marriott hotel room. As the investigation got rolling, she hoped to be considered a witness. When the Justice Department shifted the case midstream from Mississippi to more-aggressive prosecutors in New York, she became a target.

Ms. Vinson’s story is a cautionary tale for good corporate soldiers everywhere who find themselves ordered to do something wrong. In a recent speech to Wall Street executives, James Comey, the U.S. attorney prosecuting Ms. Vinson’s case, said that “just following orders” is not an excuse for breaking the law. As Ms. Vinson’s experience at WorldCom shows, sometimes it’s hard to tell right from wrong in the heat of a workplace battle. And when an employee’s livelihood is on the line, it’s tough to say no to a powerful boss. Ms. Vinson wasn’t alone in these predicaments. In a report issued this month, investigators hired by the company’s new board found that dozens of employees knew about the fraud at WorldCom but were afraid to speak out.

Love of Math

Ms. Vinson played on the high-school tennis team here in her hometown and translated her love of math into an accounting major at Mississippi College. She lived at home and spent the summers working in her father’s typewriter shop, which eventually closed after computers came into vogue.

Shortly after she graduated in 1978, she married Tom Vinson, her college sweetheart. Ms. Vinson took a series of positions at a small savings bank in Louisiana and then the Resolution Trust Corporation, there and in Kansas City. The couple moved home to Jackson in 1996, when Ms. Vinson got a job in the international accounting division at WorldCom making $50,000 a year.

The Vinsons moved to a quiet, manicured neighborhood on the outskirts of Jackson. They attended their daughter’s soccer games, took on home-improve-

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June 23, 2003

Wall Street Jour
Los Alamos directors resign after row over sacked whistleblowers

Geoff Brumfiel, Washington

Accusations of mismanagement and theft at the United States' most venerable nuclear-weapons laboratory have prompted the resignations of its top two managers.

On 2 January, John Browne and Joseph Salgado stepped down as director and deputy director of the Los Alamos National Laboratory in New Mexico. Their resignations are believed to have been requested by the University of California (UC), which has overseen the laboratory for the US government since 1943.

Congressional and Department of Energy officials are now demanding a review of the university's contract to manage the lab, whose once-formidable reputation has been tarnished by a succession of recent crises.

The resignations stemmed from allegations made in November, when two independent investigators hired by the lab released documents that they said showed endemic theft and credit-card fraud at Los Alamos. Laboratory officials said the alleged problems amounted to only a few million dollars, against the lab's annual budget of $1.3 billion for goods and services. Shortly afterwards, the lab fired the investigators, without giving any public explanation.

This angered the congressional and federal officials who oversee the lab. "The treatment of whistleblowers is a big issue for us," said a staff member on a congressional committee investigating the situation at the lab. This sentiment was strongly echoed by energy secretary Spencer Abraham in a letter sent to Richard Atkinson, the UC president, on 24 December, in which he said that the two investigators' dismissals were "of most immediate concern". Abraham had already dispatched the energy department's inspector general to look into the matter.

The incident is the latest in a string of embarrassing mishaps for the lab, which was the birthplace of the atomic bomb. In 1999, Los Alamos scientist Wen Ho Lee was accused of passing nuclear secrets to a foreign power (see Nature 398, 96; 1999); he was later acquitted. In 2000, computer drives containing secret bomb data disappeared from a secure vault and later reappeared behind a photocopier (see Nature 405, 725; 2000). Earlier that year, a nearby forest fire had threatened sensitive areas of the lab.

"A whole string of things have been happening over the past few years," says Robert Civik, a consultant who until 1999 worked as White House budget examiner for the energy department's national security programmes. "This could just be the straw that breaks the camel's back."

The series of incidents caused the energy department to put stipulations in its January 2001 contract with UC aimed at bolstering supervision and security at the lab. Chief

Insurers left reeling by disaster year

Quirin Schiermeier, Munich

Natural disasters caused record economic damage worldwide of US$65 billion last year — $20 billion more than in 2001 — according to an analysis by reinsurance company Munich Re.

The annual survey by Munich Re, which provides policies to back insurance companies, helps climate researchers to match their own predictions against what is actually going on. No one has conclusively tied any increase in the rate of extreme weather events to global warming — but Munich Re analysts predict that global warming will increasingly cause such events.

August's floods in central Europe were the most expensive disaster of the year (see Nature 418, 905; 2002), with damage costing some $18.5 billion, says the company.

But in terms of deaths and injuries, 2002 wasn't such a bad year. About 11,000 people were killed in natural disasters, compared with 25,000 in 2001, when earthquakes hit El Salvador and India.

The company's geoscience research group has been monitoring natural disasters for 30 years, using information from news agencies, the Red Cross and its own branches and clients in 150 countries.

The most notable trend during 2002 was the increase in extreme weather incidents, says Thomas Loster, head of climate risk research at Munich Re. "These observations are consistent with predictions made by the Intergovernmental Panel on Climate Change about more frequent weather extremes," says Loster. "Although single observations are not statistically significant, each is an important element of the climate mosaic."
Who cares about something as abstract as "corporate governance"? With the sudden collapse of Enron, plenty of big investors do. A fair assumption is that the catastrophe would not have occurred if the directors—in particular, members of the audit committee—had extracted their heads from the sand.

It’s a good told-you-so moment for Nell Minow, who, with partner Robert Monks, has made a career of lobbying for more accountability in corporations. In 1986 she joined Monks at his firm called Institutional Shareholder Services, where they advised institutional investors on proxy voting and used their podium to campaign against poison pills and insider directors. Next the pair started a money management business that bought shares of mismanaged companies, on the theory that a proxy battle might shape them up and realize untapped values. They sold both of those businesses. Their third venture is just at the starting stage: the Corporate Library, a Washington, D.C.-based research outfit that will rate boards of directors and indi-
individual directors on their diligence in protecting the shareholders who elect them.

Minow can lay no claim to knowing ahead of anyone else about the shenanigans that were going on at Enron, but she can take credit for warning, in general terms, that the board didn’t look like a committed one. In an October 2000 speech to the National Association of Corporate Directors, she noted that 4 of Enron’s 13 directors at that point owned no stock in the company, an unusual situation. “You can’t count on directors paying a lot of attention if they don’t have a financial stake,” she said.

Minow, 50, and Monks, 67, will publish some of their director ratings freely but aim to make a business out of selling the details to institutional investors and to the insurance companies that sell director- and officer-liability coverage.

Some early grades: Lucent’s directors get a resounding F for a multitude of reasons, including authorizing the purchase of a golf course (see below) as a management perk a few years ago. The Conoco board gets an F for giving Chief Gary Wendt a $45 million cash signing bonus: Corporate Library thinks a rescue artist should deliver results before getting a big payout. Minow and Monks reward Waste Management’s board with an A for running the company while its chief executive was ill.

Says Minow: “I am not trying to tell companies what color the widgets should be. I am trying to make sure that the system of checks and balances in corporate governance works.” But what gives these self-appointed guardians the right to judge what’s in investors’ interests? Just this: their success in spotting companies that could benefit from more attention to shareholder value.

Monks and Minow opened Lens Investment Management in 1992, playing a role in a decade of upheaval in the boardroom. This was when directors discovered that they were not, as John Kenneth Galbraith had opined in his 1967 book The New Industrial State, mere pawns of the chief executive; they could fire the chief. They did just that at IBM, Kodak, Westinghouse and 16 other big companies. Lens claims a 26% average annual return for the eight years to September 2000. The S&P 500 returned just 18%.

Monks and Minow sold Lens for $20 million in a deal in which Hermes, a British pension fund, bought the Lens name for use in Europe, and Relational Investors, a San Diego money management firm with a similar philosophy, took over its clients. Minow’s 13% stake gave her a take of $2.6 million.

They sold their proxy-advising firm, Institutional Shareholders, for $13 million in 1995 to Thomson, the Canadian business-data company, netting Minow $780,000 for her 6% stake.

If Minow is something of a scold, it could be because public service runs in her genes. Her father, Newton Minow, a lawyer who once sat on several boards, including Aon’s, was the Democratic chairman of the Federal Communications Commission in the 1960s; her mother, Josephine Minow, headed a child-abuse prevention group. In a famous speech in 1961, her father lambasted the television industry for creating “a vast wasteland.”

Nell and her two sisters, each of them now lawyers, were forbidden to watch TV. When she got to Sarah Lawrence, she did a little catching up on the medium. Then the censure gene reasserted itself. Since 1995 Minow has been running a Web site called Moviemom.com on which she rates the suitability of kids’ movies. The historical movie 1776 gets five check marks, the highest rating. The recent version of The Nutty Professor gets a pan. Minow and husband David Apatoff, a Washington attorney, have two kids, 15 and 17. Do her kids see movies with low ratings? Minow thinks not.

After getting a University of Chicago law degree in 1977, Monks got interested in corporate governance after meeting Monks, then a Labor Department administrator, in Washington. Corporate Library, their new venture, has a staff of 12 and retains an accounting firm as they gather hard-to-find information like chief executive pay contracts, directors’ attendance records and the percentage of outside directors. This part of the service is free on the firm’s Web site, www.thecorporatelibrary.com.

So, there are some quantitative components, but the grades are largely subjective. Procter & Gamble directors get demerits for approving accounting in which “nonrecurring” charges are becoming all too recurring (see related story, p. 106). She knocks Hewlett-Packard directors for okaying the merger with Compaq. Credentials won’t count for much. Enron filled its board with respectable types, including Robert Jaedicke, the Stanford University accounting guru, and look what happened there.

Indeed, aren’t most directors smart, responsible and ethical? "That’s the reason I am so interested in this issue," she enthuses. "Every director I’ve met is capable, honest and accomplished. The fact that they fail as a group is endlessly fascinating to me."

The Minow family tradition is alive and well.

THE GRADING GAME: Minow hands out a report card.

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Nell Minow thinks that America’s bosses still need better parenting (none of them new recruits) from the 1,500 largest S&P companies finds that the median salary rose by 9%, the median cash bonus by 24% and the median value of awards of restricted stock by almost 20% over 2002 levels. The median number of share options granted rose by 7.5%, and both the value of options held and the median value of options exercised held steady.

True, these results mainly reflect policies set at the start of 2002, before public outrage against corporate excesses really got going. But there are ominous signs: at Sprint, the board is buying Gary Forsee from BellSouth for $4.5m in restricted stock and a guaranteed bonus—“my favourite oxymoron,” says Ms Minow, who reckons that boards still pay bosses big rewards with little regard for performance. “The less variability the candidate is willing to take in on the pay package, the less suitable he is for the job, especially in a turnaround situation,” she says. Boards are bad at saying no to chief executives, who in effect set their own pay. “The overwhelming advantage the CEO has in selecting ‘his’ directors’ remains a formidable obstacle.

Where are the shareholders?

Still, there are hopeful signs. There will, she thinks, be more turnover in the boardroom in the next year than in the past ten—and “the new crowd will do better, or at least if they don’t, they won’t last long.” The Sarbanes-Oxley act does not alter much, she argues, but the listing rules that the New York Stock Exchange is proposing may do. The requirement that directors meet regularly without the presence of the chief executive will be immensely beneficial. She is also keen on a new Securities and Exchange Commission rule that will eventually require the disclosure of money managers’ proxy votes and voting policies.

But government has limited power to bring about governance change. The answer, argues Ms Minow, lies in the market: the government’s job ought to be to remove obstacles that prevent the market from working and stop shareholders exercising their power. Such a view is not surprising, given her background: she has worked since 1986 with Bob Monks, one of America’s best-known champions of better corporate governance, setting up Institutional Shareholder Services, which advises big institutions on casting proxy votes. The Corporate Library has built up a wealth of data on executive pay and contracts, and a database of the myriad ways in which directors are connected, rather than independent. It is now establishing a rating system for good governance, to be launched soon, on the theory that directors will care about the stigma of a bad grade.

Maybe they will. Certainly, shareholders are more assertive at this year’s annual meetings than they have been for a long time. Taking the lead, as ever, is Calpers, California’s state pension fund, which is urging General Electric’s shareholders to demand that its executives’ share options be performance-related. Shell’s shareholders have threatened a revolt over boardroom pay. Shareholders at Hewlett-Packard’s annual meeting kicked up a stink about a plan for generous severance packages for senior executives. And some technology companies are restricting the use of share options, in response to grumbles from investors.

Yet the worry is that, even after all the corporate scandals, so few shareholder resolutions are likely to succeed. Too many shareholders are content to let bosses remain largely unaccountable—the investing equivalent of leaving the kids in front of the TV while you go to the pub. If only more shareholders shared Ms Minow’s robust approach to corporate parenting.
When Martin L. Grass, the former Rite Aid Corp. chairman and CEO, was indicted in late June along with three other company managers, prosecutors tipped their hats to Joe Speaker—a little-known executive at the drugstore chain. Soon after becoming acting chief financial officer at Rite Aid in 1999, Speaker uncovered numerous errors in the company's accounts. He told Grass that the problems were serious enough to require a major restatement but feared the CEO would brush them aside. At the time, the Camp Hill (Pa.) company desperately needed to raise capital to pay debt from an acquisition spree. Grass was pleading with banks to extend a line of credit while trying to persuade the Securities & Exchange Commission to stop holding up a share offering.

What the then 40-year-old Speaker did next went beyond the call of duty. He contacted and personally hired Ralph C. Ferrara, a former SEC general counsel recommended by his brother Pete, a lawyer. Ferrara arranged a private meeting with Rite Aid's audit committee, led by Loews Corp. Co-Chairman Preston R. Tisch. Days later, the brothers drove to a secret Manhattan meeting. Over the next several hours, the acting CFO nervously relayed an incredible story of accounting chicanery. Inventories had been overvalued, bills were being paid out of reserves set aside to close stores, and millions in expenses had not been properly booked. According to one person present, he warned: “I'm in over my head.” Stunned, Tisch and other board members, including former Primerica Corp. Chairman Gerald Tsai Jr. and Hertz Group Inc. Chairman Leonard N. Stern, authorized him to hire whatever help he needed to dig into Rite Aid's books. In the end, $541 million in earnings over the previous nine quarters became $1.6 billion in losses.

Speaker will be a main government witness when Grass and three lieutenants go on trial early next year. All four have pleaded not guilty. A Rite Aid spokeswoman declines to comment. Speaker, son of a former Pennsylvania attorney general, also won't discuss his role in stopping what prosecutors say was one of the most audacious capers in corporate history. "Joe is an ordinary man who was put in an extraordinary position," says his lawyer, Philip Khinda. "And he responded in just the way we all hope we would."

This year, dozens of ordinary people have been put in extraordinary positions throughout Corporate America, and like Joe Speaker, they blew the whistle. Some are now familiar names, such as Enron Corp.'s Sheron S. Watkins (page 110) and WorldCom Inc's Cynthia Cooper. But most are middle managers who want to avoid the limelight. Behind the scenes, they have all played a critical role in providing enforcers with virtual road maps around complex accounting maneuvers. "Whistleblowers give us an insider's perspective," says Linda Chatman Thomsen, the SEC's deputy director for enforcement, "and have advanced our investigations immeasurably."

It would not be too glib to call 2002 the Year of the Whistleblower. The spectacular blowups at Enron and WorldCom have sensitized employees to the devastation caused by corporate crime. That has helped create a "do the right thing" culture in which employees believe they have little choice but to ring the alarm when they suspect misconduct, despite potentially high personal costs. Watkins and Cooper have helped recast whistleblowers from crackpots to national champions, says Stephen Meagher, a former federal prosecutor who represents whistleblowers. "The business of whistleblowing is booming," he says.

More important, the landmark Sarbanes-Oxley Act of 2002 gives those who report corporate misconduct sweeping new legal protection. An executive who retaliates against a corporate whistle-
blower can be held criminally liable and imprisoned for up to 10 years. That’s the same maximum sentence a mafia don gets for threatening a witness. The Labor Dept. can order a company to rehire an employee without going to court. And fired workers who feel their cases are moving too slowly can request a federal jury trial after six months. “This is a revolution in corporate free speech,” says Louis A. Clark, executive director of the Government Accountability Project, a Washington watchdog group that helped write the law. “It’s hard to overestimate its impact.”

Companies must rethink how they deal with whistleblowers and revisit a wide range of policies. They need to rewrite nondisclosure pacts, meant to keep company secrets inviolate, to differentiate whistleblowing from leaking. And they may no longer be able to enforce rules requiring employees to get permission to speak to the media or lawmakers. Even layoffs must be planned so they are not seen as retaliatory.

Corporate lawyers also have special responsibilities under the new law. If they come across evidence of misconduct, they must report it to top management. If there is no response, the lawyer must report higher up the line, to the board. The aim is to prevent lawyers from sitting idle—and claiming attorney-client privilege—when they see laws broken.

As a result, many executives will have to be coached on the whole phenomenon of whistleblowing, not unlike the sexual harassment training of a decade ago. “You’re going to see [corporate] policy changes that set the stage for cultural changes,” says John D. McMickle, a lawyer who represents whistleblowers at Chicago’s Winston & Strawn.

But these changes aren’t going to come quickly—and they certainly aren’t going to turn whistleblowing into a fast route to fame and fortune. In the movies, corporate truth-tellers are rewarded for their agonies with vindication. Jeffrey Wigand, the tobacco researcher who revealed that Brown & Williamson Tobacco Corp. knew tobacco was addictive (played by Russell Crowe in The Insider), got to see the industry brought to its knees. The heroes of Silkwood and The China Syndrome pay with their lives, but their dire warnings of the dangers of nuclear power turn out to be justified.

Movies, however, are made only about the precious few with appealing stories. For many, whistleblowers, tattling on the boss still means career suicide—with no applause. Indeed, half of the 200 respondents to an August survey by the National Whistleblower Center in Washington said they were fired after reporting misconduct. Those not canned often face retaliation, such as being demoted to a lesser job. If they leave, they are often blackballed in their industry. “Whistleblowers are like a skunk at a picnic,” says Senator Charles E. Grassley (R-Iowa), a long-time advocate of their cause in Congress. “There’s great peer pressure to get along in any organization.”

Ask Judy Collins, who was recently terminated from her job as a regional director of marketing for homebuilder Beazer Homes USA Inc. Just six weeks after joining the company in March, she alleges she came across financial irregularities as well as efforts to intimidate employees who raised questions. Two weeks after laying out her complaints in an e-mail to the company president, she was fired, she says, for a “personality conflict.” Beazer spokesman Ron Warren says the company will not comment on her charges.

Collins says she is now unemployable since her accusations have gotten around. By going public, she may have gone from a gadfly at one company to a perceived troublemaker the entire home-building industry now shuns. “I’ve gone in for four and five interviews in some cases,” she says, “but I
the edge of Death Valley. After six months, his job was eliminated. The whole experience, he says, was "hell." Bechtel says Parks’s charges were without merit. Now, he has done it again. In March, Parks filed suit against L.S. Starrett Co., maker of devices that test parts for planes and other complex machines. Parks charges that Starrett, for whom he worked as a subcontractor, tried to conceal from customers such woes as defects in operating software. His charges were bolstered by a Pentagon investigator in an affidavit unsealed on Nov. 6 in U.S. District Court in Greensboro, N.C. A Starrett spokesman denies the charges as "untested hearsay allegations." What makes Parks go to all the trouble? "I’ve asked myself that many times," Parks says.

Another type, the self-protectors, know about problems that could lead to an investigation. They might even be responsible for some of them. By coming clean, they clear their consciences—and lessen the likelihood of going to jail. That may explain the actions of Rite Aid President Timothy J. Noonan, who wore a wire and recorded Grass allegedly plotting to foil the grand jury investigation. On one recording, Grass is quoted as saying that investigators would never get hold of a computer containing evidence that he backdated letters “unless they use a Trident submarine.” On July 10, Noonan pleaded guilty to withholding information from investigators. In exchange for his cooperation, prosecutors are expected to seek probation. Noonan, through his lawyer, would not comment.

Then there are the corporate outliers, people who just don’t fit into the culture of the company. Many women working in an environment dominated by men are in this category. Watkins and Cooper, for instance, both worked in macho cultures. Whatever category they fall into, whistleblowers are going to find life a bit easier. Under the Sarbanes-Oxley law, they need only make a disclosure to a supervisor, law-enforcement agency, or congressional investigator—that could have a “material impact” on the value of a company’s shares. The Labor Dept. is responsible for investigating claims of whistleblowers who say they have been terminated, demoted, or harassed. So far, 16 people have filed complaints. Sarbanes-Oxley could also
Legal Affairs

HOLLYWOOD’S LOVE AFFAIR WITH WHISTLEBLOWERS
On the silver screen, they’re always vindicated—even if only posthumously

THE CHINA SYNDROME (1979)
JACK LEMMON’s character warned of dangers at a nuclear plant

SILKWOOD (1983)
Karen Silkwood, played by MERYL STREEP, died mysteriously

THE INSIDER (1999)
Big Tobacco is skewered by Jeffrey Wigand, played by RUSSELL CROWE

rescue some complaints that used to fall by the wayside. Christine Casey, for instance, claims she left her financial-analyst job at Mattel Inc. in 2000 after being pushed aside by supervisors as punishment for pointing out what she believed to be intentionally inflated sales forecasts. Her wrongful-termination suit, filed under a California whistleblower law, was thrown out of Los Angeles County Superior Court in September because, the judge said, Mattel did not fire her. Under the new law, though, the mere allegation of retaliation would have triggered a review. Mattel says it has nothing to add beyond the judge’s decision. Casey, who is appealing, says her fast-track career may have been permanently stalled by her choice to speak up.

There are critics who say the law doesn’t go far enough. Their main beef: Unlike those who expose government fraud, there are no financial incentives for corporate whistleblowing in the new law. Nor does the act cover private companies. But while the law isn’t perfect, Congress for the first time has erected a protective shield around employees who ring the alarm. Corporate managers had better brace themselves.

By Paula Dwyer and Dan Carney, with Amy Borrus and Lorraine Woellert in Washington and Christopher Palmeri in Los Angeles

BusinessWeek online
For more on Grassley and whistleblower sites, go to the Dec. 15 issue online at www.businessweek.com

This is a nasty headline, why? Roy Jenkins

WAS SHERRON WATKINS REALLY SO SELFLESS?

Whistleblowers have none other than Sherron S. Watkins to thank for the new coat of armor Congress gave them in the new Sarbanes-Oxley law. That’s ironic, given that the former Enron Corp. vice-president has never fit neatly into the whistleblower mold. Indeed, the woman made famous by her August, 2001, warning to Chairman Kenneth L. Lay is facing some revisionist criticism of her role at the company.

Watkins, 43, is getting heat for not taking her concerns about accounting and insider deals to regulators, the press, or even the company’s board. As Lay attempted to investigate her claims, she was selling some $45,000 worth of stock—for tax and diversification reasons, her lawyer says. Journalist Robert Brye, in his book Pipe Dreams: Greed, Ego, and the Death of Enron, portrays her as an overeager climber looking to grab a more important job by getting Chief Financial Officer Andrew S. Fastow fired.

One company exec even notes that Watkins failed to raise any red flags in 1999 when she was trying to sell Enron’s stake in a Caribbean power plant to an off-balance-sheet partnership run by Fastow. The deal ultimately fell through, but “not due to any lack of effort on her part,” says the source. The partnerships later played a significant role in underpinning investor confidence.

Watkins, who would speak only through her lawyer, Philip Hilder, insists she did not know the disturbing details that set off alarm bells for her until 2001. When she wrote her memo, she was simply trying to save Enron before it was too late. Says Hilder: “She acted entirely appropriately. She went to the management that she thought would rectify the problem in-house and did what a good employee should have done. It took moxie and courage.”

However, history judges Watkins’ role in the Enron charade, her story directly influenced Congress as it considered whistleblower protections. The revelation that Enron considered firing Watkins once she revealed that she was the memo’s author angered legislators. So they made sure to strengthen anti-retaliation protections in the law.

Watkins recently left her $165,000-a-year Enron job of her own accord when she found herself with little to do at the bankrupt company. But she leaves a big mark. Faced with Enron-like misconduct elsewhere, says a former Enron employee, “we’ll be much more assertive. We’ll not be intimidated.” That’s a legacy no revisionism can take away.

By Wendy Zellner in Dallas
THE WHISTLEBLOWERS

They raised the alarm about misdeeds at their employers—and made history in the process.

BARRON STONE
Duke Power
When Duke Power agreed in October to credit $25 million to utility customers in North Carolina and South Carolina, it was sweet vindication for whistleblower P. Barron Stone. The accountant had warned his bosses at the utility that they were overcharging ratepayers. When they wouldn’t listen, he told state regulators, triggering an investigation that resulted in the company, a unit of Charlotte (N.C.)-based Duke Energy Corp., agreeing to change its accounting and make customers whole. “I was just doing my job,” says Stone, who still works for the utility.

MARTA ANDREASEN
European Commission
As former chief accountant at the European Commission, Marta Andeasen touched off a furor last May when she refused to sign the EC’s 2001 accounts. By August, the 48-year-old Spaniard had been suspended from her job. Andeasen, who refuses to resign, claims the EC’s $100 billion budget is “out of control” and that the books are a mess. She was partially vindicated on Nov. 5, when an annual report by the EC’s financial watchdog highlighted persistent defects in the accounting system. Andeasen’s case is awaiting a full commission review.

SHERRON WATKINS
Enron
“I am incredibly nervous that we will implode in a wave of accounting scandals,” Sherron S. Watkins (left) wrote in that now-infamous six-page memo to then-Chairman Kenneth L. Lay. Watkins, a vice-president at Enron Corp., left the company in late November, was the only employee to take her concerns about its suspicious practices to the top. But even she was cautious: After drafting the memo, she asked her mom, a retired business teacher who lives near Houston, to look it over. Watkins, 43, is now co-authoring a book about her experiences and planning to consult on governance issues.

CYNTHIA COOPER
WorldCom
Acting on a hunch and a few tips, Cynthia Cooper and two other internal auditors took it upon themselves to dig into the accounting practices at WorldCom Inc. Because they suspected their bosses had cooked the books, they worked after hours to avoid detection. What they found—that the company had artificially boosted profits—led to the ouster of Chief Financial Officer Scott D. Sullivan. In June, the SEC charged WorldCom with civil fraud. Sullivan was indicted on fraud and has pleaded not guilty. The company, which owned up to misstating $38 billion in expenses, declared bankruptcy. Cooper, 38, remains at WorldCom.

WATCHDOGS IN ACTION

Best performance as a regulator by someone who isn’t one

When the feds stumbled over how to rein in Wall Street firms and restore investor confidence, New York State Attorney General Eliot Spitzer stepped into the void. He dug up incriminating e-mails that shamed Wall Street and laid bare the conflicts of stock analysts. Now he’s actually forcing financial firms to distribute independent research and to stop doling out IPO shares to favored executives.

Worst performance by a regulator who never should have been one

Anne M. Mulcahy while that company was under SEC investigation, and repeatedly demonstrated a poor grasp of Washington politics. He finally resigned on Nov. 5. This has to go down as the Bush Administration’s worst hire, yet.

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ENRON END RUNS

THE REAL STORY OF THE WATKINS MEMO

NEXT UP IN THE convoluted saga of Enron: the tale of Schuyler Tilney, a senior Merrill Lynch investment banker who took the Fifth in front of Congress on July 30. Tilney had more than just a professional relationship with Enron. His wife, Elizabeth, was once a senior member of Enron’s management team and “one of the closest confidantes” of former CEO Kenneth Lay, according to a source with detailed knowledge of Enron. And Schuyler, personally, was an investor in LJM, one of the off-balance-sheet partnerships used to conceal Enron’s losses.

More surprising, after Sherron Watkins wrote her famous whistle-blower memo, Lay sent her to talk to Elizabeth Tilney. Elizabeth had previously overseen Enron’s corporate communications and had worked on an internal employee “values” campaign. At the time Lay sent Watkins to her, she was handling communications and marketing for a subsidiary, Enron Energy Services. So Watkins wrote a second, two-page memo to Elizabeth suggesting that she have Lay go public about Enron’s shenanigans, including the LJM partnerships. Watkins wrote: “It’s very hard to know who in the organization is giving us good answers and who’s covering their prior work.”

It sure was. At the time, Watkins did not know that she was taking her complaints to the wife of the investment banker who helped Merrill Lynch win the job to raise funds for the LJM partnership and who had his own financial stake in it, according to Watkins’ lawyer, Philip Hilder. The conversation between the two women was “a one-way street,” says Hilder. “They [Enron management] wanted Sherron to have limited involvement.” Some of her Enron colleagues questioned Elizabeth’s apparent conflict of interest at the time, the source says.

The Tilney’s lawyer, Robert Stout, says there was no conflict, that Elizabeth was assigned to a subsidiary and had disclosed her husband’s role to top management: “Ms. Tilney had no authority to pick or choose among the many opinions about how to deal with the situation.”

Shows how seriously Lay took Watkins’ first memo, doesn’t it? A spokeswoman for Lay says that he has no response.

Emily Thornton and Wendy Zeltner

TALK SHOW “If you’re a CEO and think you can fudge the books in order to make yourself look better, we’re going to find you, we’re going to arrest you, and we’re going to hold you to account.” —President George W. Bush

AT THE TROUGH

WORLDCOM: A GIFT TO THE LAWYERS

RULE NO.1 IN A BANKRUPTCY: The lawyers get paid first. And in the case of WorldCom, there seems to be a race to the trough. Six law firms, plus investment bank Lazard Frères, are going after the long-distance carrier’s remaining nickel in a big way. Three are billing WorldCom at or above the once-unheard-of rate of $700 an hour.

Topping the list is Bill McLucas of Wilmer, Cutler & Pickering. He’s getting $715 an hour from WorldCom’s board to investigate the company’s dubious accounting activities. That is $5 an hour more than he got for doing the same at Enron. A respected former Securities & Exchange Commission enforcement chief, he can name his price to troubled firms trying to show how they’re coming clean. McLucas says it’s up to his firm how much he bills.

Superlobbyist Tommy Boggs is also billing $700 an hour to contain damage from congressional inquiries. Top lawyers at leading bankruptcy firm Weil, Gotshal & Manges are pulling in that amount as well. Neither Boggs nor Weil Gotshal lawyers would comment.

Hundreds of other lawyers, associates, and paralegals are billing for lesser amounts, depending on level of experience. And many firms haven’t even been named yet. Add in Lazard, which wants a $15 million “success fee” if it ends up restructuring WorldCom, and the bankruptcy fees may end up being the biggest on record.

Dan Carney
Uncooking the Books

How Three Unlikely Sleuths Discovered Fraud at WorldCom

Company’s Own Employees
Sniffed Out Cryptic Clues
And Followed Hunches

Ms. Cooper Says No to Her Boss

By Susan Pulliam
And Deborah Solomon

CLINTON, Miss.—Sitting in his cubicle at WorldCom Inc. headquarters one afternoon in May, Gene Morse stared at an accounting entry for $500 million in computer expenses. He couldn’t find any invoices or documentation to back up the stunning number. “Oh my God,” he muttered to himself.

The auditor immediately took his discovery to his boss, Cynthia Cooper, the company’s vice president of internal audit. “Keep going,” Mr. Morse says she told him.

A series of obscure tips last spring had led Ms. Cooper and Mr. Morse to suspect that their employer was cooking its books. Armed with accounting skills and determination, Ms. Cooper and her team set out on their own to figure out whether their hunch was correct.

By June 23, they had unearthed $3.8 billion in misallocated expenses and phony accounting entries. It all added up to an accounting fraud, acknowledged by the company, that turned out to be the largest in corporate history.

Their discoveries sent WorldCom into bankruptcy, left thousands of their colleagues without jobs and roiled the stock market.

At a time when dishonesty at the top of U.S. companies is dominating public attention, Ms. Cooper and her team are a case of middle managers who took their commitment to financial reporting to extraordinary lengths. As she pursued the trail of fraud, Ms. Cooper time and again was obstructed by fellow employees, some of whom disapproved of WorldCom’s accounting methods but were unwilling to contradict their bosses or thwart the company’s goals.

WorldCom is under investigation by the Justice Department and the Securities and Exchange Commission. Scott Sullivan, WorldCom’s former chief financial officer and Ms. Cooper’s boss, has been indicted. He has denied any wrongdoing. Four other officers have pleaded guilty and are cooperating with prosecutors.

Federal investigators are still probing whether Bernard J. Ebbers, the company’s former chief executive, knew about the accounting improprieties. Since the initial discoveries, WorldCom’s accounting misdeeds have grown to $7 billion.

Behind the tale of accounting chicanery lies the untold detective story of three young internal auditors, who temperamentally didn’t fit into WorldCom’s well-known cowboy culture. Ms. Cooper, 38 years old, headed a department of 24 auditors and support staffs, many of whom

Hunting Down Fraud

- March: Cynthia Cooper, vice president of internal audit, hears that CFO Scott Sullivan has used reserves to boost profits.
- March 6: Ms. Cooper alerts audit committee. Mr. Sullivan backtracks.
- May 25: An auditor uncovers $500 million in fraudulent computer expenses.
- June 17: Ms. Cooper confronts other WorldCom officials about the accounting problems.
- June 20: She presents findings to WorldCom’s board. Mr. Sullivan is later fired.
- June 25: WorldCom announces it inflated its profits by $3.8 billion over previous five quarters.
How Three Unlikely Sleuths Discovered Fraud at WorldCom

Continued From First Page

viewed her as quiet but strongwilled. She grew up in a modest neighborhood near WorldCom's headquarters and had spent nearly a decade working at the company, rising through its ranks. She declined to be interviewed for this story. Mr. Morse, 41, was known for his ability to use technology to ferret out information. The third member of the team was Glyn Smith, 34, a senior manager under Ms. Cooper. In his spare time he taught Sunday school, took photographs and bicycled. His mom had taught him and Ms. Cooper accounting at Clinton High School.

Frightened that they would be fired if their superiors found out what they were up to, the gumshoes worked in secret. Even so, their initial discrete inquiries were stonewalled. Arthur Andersen, WorldCom's outside auditor, refused to respond to some of Cooper's questions and told her that the firm had approved some of the accounting methods she questioned. At another critical juncture in the trio's investigation, Mr. Sullivan, then the company's CFO, asked Ms. Cooper to delay her investigation until the following quarter. She refused.

Ms. Cooper's first inkling that something big was amiss at WorldCom came in March 2002. John Stupka, the head of WorldCom's wireless business, paid her a visit. He was angry because he was about to lose $400 million he had specifically set aside in the third quarter of 2001, according to two people familiar with the meeting. His plan had been to use the money to make up for shortfalls if customers didn't pay their bills, a common occurrence in the wireless business. It was a well-accepted accounting device.

But Mr. Sullivan decided instead to take the $400 million away from Mr. Stupka's division and use it to boost WorldCom's income. Mr. Stupka was unhappy because without the money, his unit would likely have to report a large loss in the next quarter.

Mr. Stupka's group already had complained to two Arthur Andersen auditors, Melvin Dick and Kenny Avery. They had sided with Mr. Sullivan, according to federal investigators.

But Mr. Stupka and Ms. Cooper thought the decision smelled funny, although not obviously improper. Under accounting rules, if a company knows it is not going to collect on a debt, it has to set up a reserve to cover it in order to avoid reflecting on its books too high a value for that business. That was exactly what Mr. Stupka had done. Mr. Stupka declined to comment.

Ms. Cooper decided to raise the issue again with Andersen. But when she called the firm, Mr. Avery brushed her off and made it clear that he took orders only from Mr. Sullivan, according to the investigators. Mr. Avery and Mr. Dick declined to comment. Patrick Dorton, a spokesman for Andersen, said his firm thought that the $400 million wireless reserve was not necessary.

"That was like putting a red flag in front of a bull," says Mr. Morse. "She came back to me and said, 'Go dig.'"

Some internal auditors would have left it at that and moved on. After all, both the company's chief financial officer and its outside accountants had signed off on the decision. But that was not Ms. Cooper's style. One favorite pastime among the auditors who reported to her was applying the labels of the Myers-Briggs & Keirsey personality test to their fellow staffers. Ms. Cooper was categorized as an INTJ—Intuitive, Introverted, Thinking and Judging. "INTJs," according to the test criteria, are "natural leaders" and "strong-willed," representing less than 1% of the population.

And so Ms. Cooper decided to appeal the decision. As head of auditing, it was her responsibility to bring sensitive issues to the audit committee of WorldCom's board. She brought the reserves question to the attention of the committee's head, Max Bobbitt. At a committee meeting at the company's Washington offices on March 6, she and Mr. Sullivan presented their cases, according to minutes from the meeting. Mr. Sullivan backed down, according to people familiar with his decision.

The next day he tracked down Ms. Cooper. Unable to reach her immediately, Mr. Sullivan called her husband, a stay-at-home dad to their two daughters, to get her cellphone number. He finally caught up with her at the salon. In the future, she was not to interfere in Mr. Stupka's business, Mr. Sullivan warned, according to people familiar with the reserves question.

The confrontations put Ms. Cooper in a sticky position. Mr. Sullivan was her immediate supervisor. Plus, her vague discomfort with the way WorldCom was handling its accounting led her into areas that were not normally her bailiwick. Although her department did a small amount of financial audit-
A Curious E-Mail from Afar

Several weeks later, Mr. Smith, a manager under Mr. Cooper, received a curious e-mail from Mark Abide, based in Richardson, Texas, who was in charge of keeping the books for the company's property, plants and equipment.

Mr. Abide had attached to his May 21 e-mail a local newspaper article about a former employee in WorldCom's Texas office who had been fired after he raised questions about a minor accounting matter involving capital expenditures. "This is worth looking into from an audit perspective," Mr. Abide wrote. Mr. Smith, who declined to be interviewed, forwarded the e-mail to Ms. Cooper, according to investigators and a lawyer involved in the case.

The e-mail piqued Ms. Cooper's interest. As part of their initial foray into financial auditing, Ms. Cooper and her team had already stumbled on to the issue of capital expenditures, a subject that would prove to be crucial to their quest.

The team had run into an inexplicable $2 billion that the company said in public disclosures had been spent on capital expenditures during the first three quarters of 2001. But the team found that the money had never been authorized for capital spending.

Capital costs, such as equipment, property and other major purchases, can be depreciated over long periods of time. In many cases, companies spread those costs over years. Operating costs such as salaries, benefits and rent are subtracted from income on a quarterly basis, and so they have an immediate impact on profits.

Ms. Cooper and her team were beginning to suspect what was up with the mysterious $2 billion entry: It might actually represent operating costs shifted to capital expenditure accounts—a stealthy maneuver to make the company look vastly more profitable.

When Ms. Cooper and Mr. Smith asked Sanjeev Sethi, a director of financial planning, about the curious adjustment, he told them it was "prepaid capacity," a term they had never heard before. Further inquiries led them to understand that prepaid capacity was a capital expenditure. But when they asked what it meant, Mr. Sethi told them to ask David Myers, the company's controller, according to Mr. Morse and a person familiar with Ms. Cooper's situation. Mr. Sethi did not return phone calls.

Ms. Cooper and Mr. Smith opted instead to call Mr. Abide, who had pointed out a capital expenditures problem in his e-mail. When they asked him about "prepaid capacity," he too answered very cryptically, explaining that those entries had come from Buford Yates, WorldCom's director of general accounting.

While perusing records looking for accounting irregularities later that same day, May 28, Mr. Smith made the big discovery of the $500 million in unob-
Ms. Cooper had begun confiding in her parents, with whom she was especially close. Without going into detail, she told her mother that she was worried about what her team was finding, and that it was definitely a very big deal, according to a person close to Ms. Cooper.

Meanwhile, Mr. Sullivan began to ask questions about what Ms. Cooper’s team was up to. One day the finance chief approached Mr. Morse at the company cafeteria. When Mr. Morse saw him coming, he froze. The auditor had only spoken to Mr. Sullivan twice during his five-year tenure at WorldCom.

“What are you working on?” Mr. Morse later recalled Mr. Sullivan demanding. Mr. Morse looked at his shoes. “International capital expenditures,” he says he replied, referring to a separate, and less-threatening auditing project. He quickly walked away.

Days later, on June 11, Ms. Cooper got an unexpected phone call from Mr. Sullivan. He told her that he would have some time later in the day, and invited her to come by and tell him what her department was up to, according to a person familiar with Ms. Cooper’s situation.

That afternoon, Ms. Cooper, Mr. Smith and another auditor arrived at Mr. Sullivan’s office. They talked about pending promotions and other administrative matters, according to lawyers involved in the case.

As the meeting was breaking up, Ms. Cooper turned to Mr. Smith and suggested that he tell Mr. Sullivan what he was working on. It was meant to seem like a casual comment. In fact, the two auditors had planned it out beforehand, so that they could gauge Mr. Sullivan’s reaction, according to a person familiar with Ms. Cooper’s situation.

Mr Smith briefly described the audit, without going into the explosive material they already had found.

Mr. Sullivan urged them to delay the audit until after the third quarter, saying there were problems he planned to take care of with a write-down, according to several people familiar with the meeting.

Ms. Cooper replied that no, the audit would continue. Mr. Sullivan didn’t respond, and the meeting ended in a stalemate.

Concerned now that Mr. Sullivan might try to cover up the accounting improprieties, Ms. Cooper and Mr. Smith appealed to Mr. Bobbitt, the head of WorldCom’s audit committee. Mr. Bobbitt had to travel to Mississippi from his home in Florida for a board meeting scheduled for June 14, so the day before he met with Ms. Cooper and Mr. Smith at a Hampton Inn in Clinton.

It was clear to Ms. Cooper’s team that their findings would be devastating for the company, and the prospect of going before the board with their evidence was sobering. They worried about whether their revelations would result in layoffs and obsessed about whether they were jumping to unwarranted conclusions that their colleagues at WorldCom were committing fraud. Plus, they feared that they would somehow end up being blamed for the mess.

Ms. Cooper’s staff began to notice that she was losing weight. Mr. Morse’s wife noticed he was preoccupied and short tempered.

During the third week in June, Mr. Smith called his mother, who was vacationing in Albuquerque, according to a person familiar with the conversation. Without providing specifics, he told her that he was about to take actions at WorldCom that were not going to make people happy. He asked his mother, Ms. Cooper’s former high school accounting teacher, to remember him in her prayers and to pray for him to be strong.

Ms. Cooper prepared for several meetings with the audit committee. At one, on June 20, Mr. Sullivan was scheduled to defend himself.

One evening, as Ms. Cooper worked late with accountants from KPMG, she suddenly dropped her head into her arms on the conference-room table. Mr. Malone of KPMG led her onto a balcony, put his arm around her and showed her the sunset, according to a person familiar with the meeting.

Ms. Cooper, Mr. Smith and Mr. Malone headed to Washington to brief the board’s audit committee. At the meeting on Thursday, June 20, Mr. Malone described the transfer of line costs to capital accounts and told the audit committee that, in his view, the transfers didn’t comply with generally accepted accounting principles, according to a document WorldCom later submitted to the SEC.

Mr. Sullivan tried to give an explanation for the accounting adjustments but asked for more time to support the line-cost transfers. The committee gave Mr. Sullivan the weekend to explain himself. He got to work constructing what he called a white paper that argued that the accounting treatments he used were proper, according to the document.

It didn’t work. On June 24, the audit committee told Mr. Sullivan and Mr. Myers they would be terminated if they didn’t resign before the board meeting the next day. Mr. Sullivan refused and was fired. Mr. Myers resigned.

The next evening, WorldCom stunned Wall Street with an announcement that it had inflated profits by $3.8 billion over the previous five quarters. Afterward, Ms. Cooper drove to her parents’ house, which was near WorldCom’s headquarters. She sat down at the dining-room table without saying anything, says Ms. Ferrell, her mother. “She was deeply, deeply pained. She was grief stricken that it was true and that all these people would feel the consequences of having gone astray,” Ms. Ferrell says. “We were all so proud of WorldCom and it’s just been the saddest, most tragic thing.”

Mr. Morse worked late that night, and his wife phoned after she watched the news. The anchors were calling the company World-Con, she reported. Did he know anything about it?

The SEC on June 26 slapped the company with a civil suit alleging, among other things, that they failed to disclose the fraud and that they engaged in a scheme to make WorldCom appear more profitable than it was.
pany with a civil fraud suit, and trading of WorldCom's stock was halted. Ultimately the company was delisted by the Nasdaq Stock Market.

Mr. Sullivan is preparing to go to trial. "We will demonstrate at the appropriate time that a number of the negative points that WorldCom's internal auditors have recently suggested about Mr. Sullivan are not accurate," says Irvin Nathan, a lawyer for Mr. Sullivan. "The fact is that he was always supportive of internal audit and was instrumental in the promotion of Cynthia Cooper and securing resources for her staff."

Mr. Myers, Mr. Yates, Ms. Vinson and Troy Normand, the director of legal entity accounting, have all pleaded guilty to securities fraud and a variety of other charges. David Schertler, an attorney for Mr. Yates, says that while his client pleaded guilty, "all the evidence would suggest he was acting under the orders of supervisors."

Ms. Cooper and her team have continued to work at WorldCom's Clinton headquarters and are responding to requests related to the various investigations of the company. Ms. Cooper, Mr. Smith and Mr. Morse have been interviewed by FBI agents in connection with the Justice Department's investigation.

Some WorldCom employees have told the auditors that they wish they had left the accounting issues alone.

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Journal Link: See further coverage of the WorldCom scandal, including bios of key players, in the Online Journal at WSJ.com/WorldCom.


WorldCom Official Tried to Quash Employee's Accounting Concerns

By Yochi J. Dreazen

The former controller of WorldCom Inc. tried to prevent a subordinate from raising accounting concerns with the embattled telecommunications firm's auditors.

A batch of e-mails released by congressional investigators probing WorldCom shows former controller David Myers ordering Steven Brabbs, an executive in the company's London offices who was raising questions about the company's accounting methods, to have no further contact with Arthur Andersen LLP.

"Do not have anymore meetings with AA for any reason," Mr. Myers wrote in an e-mail to Mr. Brabbs on Jan. 22, referring to Andersen. He warned Mr. Brabbs not to offer him any more excuses about his communication with Andersen and then sent Mr. Brabbs a blunt warning: "Don't make me ask you again."

The e-mails could potentially ratchet up the legal woes facing Mr. Myers, who resigned from WorldCom the day it announced $3.85 billion in accounting irregularities. The disclosure sent the value of the company's stock plummeting and led it to seek Chapter 11 bankruptcy-court protection, the largest such filing in U.S. history. The company has since expanded its planned financial restatement to $7.2 billion after finding more improperly booked items.

Mr. Myers, 44 years old, was arrested last month and charged with securities fraud, conspiracy and other related charges. Mr. Myers, who has been released on $2 million bail, is negotiating a possible plea that could result in his cooperation in the investigation, say people familiar with the matter. Mr. Myers is said to be in advanced talks with prosecutors, these people say, but the e-mail messages could complicate the situation by raising new questions about his role.

"Those sorts of documents in writing give signposts along the way to a person's intent," said former federal prosecutor Stephen M. Ryan, who isn't involved in the WorldCom case.

In the case of Mr. Myers, the e-mails could potentially be viewed as proof that the controller was trying to keep Arthur Andersen from evaluating the company's accounting treatment, Mr. Ryan said, though he added that Mr. Myers may simply have been trying to keep information flowing in an orderly fashion.

Congressional officials, for their part, said they were confident the e-mails had no benign explanation. "It was an attempt to intimidate Mr. Brabbs into shutting up," maintains Peggy Petersen, a spokeswoman for House Financial Services Committee Chairman Michael Oxley (R., Ohio), whose committee released the e-mails.

An attorney for Mr. Myers declined to comment. WorldCom spokesman Brad Burns said the company is "cooperating with all of the investigations and will continue to do until there's a full resolution of them." Mr. Brabbs, who still works for WorldCom, couldn't be reached to comment.

The e-mails paint a picture of the pressures and conflicts building within WorldCom as senior executives began to notice that something was seriously wrong with the company's books.

In March 2000, Mr. Brabbs, whose title at that time was director, International Finance & Control, noticed a U.S. executive had reduced his division's expense figures by $33.6 million, making the division's numbers look better than they actually were, according to a memo that he later sent in an e-mail to a colleague.

When Mr. Brabbs asked his counterparts in the U.S. about the change, he was told it was made because of a directive from former WorldCom chief financial officer Scott Sullivan, according to the same