Bush appointee at SEC resigns amid charges of cover-up

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The resignation of Securities and Exchange Commission (SEC) Chairman Harvey Pitt November 5 has underscored the complicity of the US government and its regulatory agencies in the wave of corporate corruption scandals that have rocked the financial markets.

The announcement that Pitt was quitting was timed for election night, after most ballots had been cast. He was implicated in a controversy surrounding the selection of a chairman of the new Public Company Accounting Oversight Board (PCAOB).

The oversight board was the central plank of the Sarbanes-Oxley Act, a piece of legislation passed this summer that was presented as a solution to the accounting scandals that brought down Enron, WorldCom and other corporations. However, like every measure employed by corporate America to give itself a face-lift, the PCAOB has quickly succumbed to the underlying rot that cannot be covered up.

From the beginning the oversight board has been a limited proposal. It is tasked with registering all accountants who audit public companies, proposing rules and standards for the accounting industry and developing corresponding sanctions against companies violating these rules. To ensure that there was no chance that it would get out of hand, the five-person board was selected by the SEC which reserved the right to overrule any of the board's proposals.

The SEC, particularly since Bush's appointment of Pitt, is an organization with close ties to the accounting industry. Pitt's own connections are numerous. He once served as a principal lawyer for all of the major auditing firms. In a speech shortly after assuming the post of SEC chairman, and shortly before the collapse of Enron last year, Pitt stated that the SEC would become a "kinder and gentler place for accountants." Earlier this year he was denounced for meeting with the CEO of a former client, the auditing giant KPMG, even as KPMG was being investigated by the SEC in relation to its auditing work for Xerox.

The other two Republicans on the board—Cynthia Glassman and Paul Atkins—are both former employees of one of the "big four" accounting firms: Ernst & Young LLP and PricewaterhouseCoopers LLP, respectively. SEC chief accountant and Pitt's closest collaborator, Robert Herdman, was a long-time top executive at Ernst & Young, a company that is currently facing a number of charges related to its complicity in accounting scandals.

The composition of the SEC was chosen precisely because of its subservience to the accounting industry, which, because of its position as a supposedly independent auditor of corporate financial statements, is deeply implicated in the whole mess of corruption. Following the collapse of Enron, the administration and Congress faced a wave of popular anger and investor unrest that forced it to undertake some limited reform measures.

The selection of the new oversight board, however, became mired in precisely the kind of scandal it was supposed to cure. Pitt was forced out following revelations that the candidate he and the Bush administration had backed as chairman of the PCAOB, William Webster, once served on the auditing committee of a company charged with financial fraud.

Webster, a Washington lawyer and former director of the FBI and CIA, has made a career of "cleaning up" organizations plagued by corruption scandals. He took over the CIA under Reagan as the Iran-Contra scandal was erupting. In 1993, he was hired by General Motors to conduct an investigation into the company's practice of shredding documents related to automobile safety, an issue that came up in relation to a lawsuit brought forward by car-crash victims. Webster was appointed as a federal overseer of the Teamsters and has been criticized by union members for failing to go after the top officials in the bureaucracy, including former president Ron Carney.

The selection of Webster—who has no real knowledge of the accounting profession nor history of advocating accounting reform—was a clear signal to the accounting industry and corporate America that no serious effort would be made to implement any changes. With Webster at its head, the new board was to be, as *BusinessWeek* commented in its November 11 issue, a "weak underling" of Pitt, and through Pitt of the accounting industry.

By a 3-to-2 vote that split along party lines, the SEC board chose Webster over John Biggs, who had been previously promoted as the leading candidate. During the first weeks of September, Biggs—who until last week was the CEO of the teachers' pension fund, TIAA-Cref—was on the fast track to nomination. According to Biggs and Harvey Goldschmid, one

of the Democratic members of the SEC board, Pitt had assured Biggs of his support.

However, Biggs has backed reforms such as prohibiting accounting firms from simultaneously serving as both auditor and consultant to the same company. Arthur Andersen performed this dual role for Enron, and a similar relationship exists at many large corporations. The consulting fees are often more lucrative than those earned from auditing work, giving accounting firms a strong incentive to cover up fraud. Biggs also has some ties to the trade union bureaucracy.

When the word was leaked that Biggs was the top choice, accounting industry lobbyists and their friends among Republican congressional leaders balked. Michael Oxley, Chairman of the House Financial Service Committee and the key player in toning down the accounting reform legislation, voiced his opinion that a more "moderate" choice was preferable. Pitt then came out publicly to deny that Biggs had been selected, saying that the original leaks were "deliberate plants of false information."

After the SEC voted for Webster, it came to light that he was until recently the chairman of the audit committee of US Technologies, a Washington-based investment firm that is facing investor lawsuits charging fraud. After US Technologies' auditor raised concerns about the company's accounting procedures and its inability to file financial reports on time, the auditing committee, with Webster at its head, fired the auditor rather than address the concerns. It hardly seems an oversight that Webster's tenure at US Technologies was omitted from the biographical sketch released by Pitt.

Webster told Pitt about the controversy surrounding his role at US Technologies, but Pitt deliberately withheld the information from other members of the SEC board and the White House. This angered White House officials, who had openly backed Webster once the accounting industry opposed Biggs. Bush's Chief of Staff Andrew Card had personally called Webster to urge him to accept the position.

The revelations surrounding Pitt's cover-up made the SEC chairman too much of a liability for the Bush administration, which pressured him to step down. This did not represent, however, a rejection of the policies carried out by Pitt. The White House has continued to support Webster. Pitt's mistake was not that he worked to cover up corporate fraud, but that he did so in such a blatant manner.

The new chairman of the SEC is yet to be determined, but potential candidates include Republican Commissioner Paul Atkins, former SEC general counsel James Doty, former New York City Mayor Rudolph Giuliani, and Frank Zarb, former chairman of the National Association of Securities Dealers. Doty once served as a personal lawyer for the Bush family and while at the SEC helped clear Bush of charges relating to his sale of Harken stock.

It may be several months before the new commissioner is chosen. Indeed, the administration has indicated that it is in no particular hurry to appoint anyone. This will allow Pitt to remain temporarily as a lame-duck chairman, helping to stall any reform proposals. Pitt has said he will stay at his position until a "smooth transition" is effected.

The Republicans have interpreted their victory in the mid-term congressional elections as a mandate to carry out their right-wing domestic agenda, including in the sphere for corporate reform. In addition to cutting back on the oversight board, the SEC has already begun to sharply curtail proposals for a "global settlement" on conflicts of interest in the investment banking sector. Pitt has already labored to make acceptable to the finance industry any plan designed to separate stock research from investment banking.

These tendencies will only exacerbate a crisis within the American economy that shows no signs of letting up. A certain section of the corporate elite have voiced concerns that the controversy surrounding Webster and Pitt will permanently damage the credibility of the accounting board, the SEC and American financial markets as a whole. Former chairman of the SEC, Arthur Levitt, worried that the selection process was "a very serious blow to investor interests and a very serious blow to investor confidence."

"While a number of past chairmen have sparred with colleagues in spirited public debate," noted an editorial in the *Wall Street Journal*, "the recent charges and personal attacks are almost unheard of at an agency known for collegiality. The agency appears more politicized than it has been in decades, potentially threatening its ability to cope with the most severe crisis of confidence in securities markets since the 1930s."

The forced resignation of Pitt is a sharp expression of this crisis. What has become apparent over the past year is that the speculative growth of the stock market during the late 1990s was based upon an unprecedented level of fraud and criminality. The fact that no measures, even the most limited, can be carried out without becoming embroiled in this fraud is further indication of the corporate and political establishment's inability to cope with the crisis it has created.