WorldCom

The rise and fall
Bernie Ebbers

♦ Former WorldCom chief

♦ Convicted on *nine* counts of securities fraud and false filings.

♦ Faces up to 85 years in jail.
Cookin’ the Books

♦ $11 billion accounting fraud.

♦ Aimed at concealing company’s weakening performance.

♦ Propped up WorldCom’s stock price.

♦ Pushed company into bankruptcy three years ago.
Corruption

♦ Money
♦ Power
♦ Pressure

*The perfect storm...*
Government’s Case

♦ Linchpin – Scott Sullivan
  – Ex-financial chief

♦ Ebbers repeatedly admonished him to make sure the numbers worked.
Smoking Gun . . .

- Massive round-number adjustments made to *line costs* – the fees paid to other telcos that carried WorldCom calling traffic.

- Line costs shifted to capital expenditures
  - $3.8 billion in expenses
Ebbers portrayed as “aw shucks”

- College dropout
- Doesn’t know a lick about accounting.
- Excels at accumulating motels and phone comp
Flagging Personal Finances

♦ Ebbers owned 20 million shares of WorldCom.
  – Purchased on credit from banks.
  – Stock was used as collateral on loans.

♦ Margin Calls Escalated
World Com Loans Ebbers

- As stock price falls . . .
- Banks asked Ebbers to sell stock and repay the loans.
- $408 million to pay off the banks.
Secular Decline

- WorldCom stock was plunging.
- Telecom industry had all but collapsed.
Ebbers forced out as CEO

♦ April 29, 2002

♦ Internal audits revealed about $4 billion in accounting errors.

♦ WorldCom filed for Chapter 11 protection.
Bubble-era Contemporary

♦ Joe Nacchio – CEO Qwest
  – Sued by SEC.
  – Oversaw a $3 billion accounting fraud.
  – Cost investors $89 billion in market losses.
Ebbers vs. Nacchio

♦ Ebbers just an old basketball coach
  – Unschooled in details of accounting
  – “I didn’t know” defense

♦ Nacchio knew exactly what was going on.
  – “Everybody knew”
  – “I did nothing wrong . . .”
Fallout

♦ J.P. Morgan Chase
  – Last Wall Street firm to settle claims that misled investors by *failing to warn* them WorldCom was in bad shape when it sold a big bond issue in 2002.
Biggest Hit to a Bank

♦ Citigroup
  – Underwrote questionable bonds.
  – Employed a famously conflicted WorldCom fan, analyst Jack Grubman.
  – City settled for $2.65 billion.
Cost of Waiting

♦ J.P. Morgan was offered a deal using Citibank formula.
  – If they settled then Morgan would have been on the hook for around $1.4 billion (May 2004)

♦ Tide Turns – Judge Rules
  – Gambled and lost
  – On the hook now for up to $10 billion in damages
    • Morgan compelled to settle.
Emerges from Bankruptcy

- Now known as MCI.
- Competing merger offers from Verizon and Qwest.
Appeal

“We know our client . . . there’s not one chance in the world . . . That he would cook the books”.

R. Weingarten,
Attorney for Ebbers